COMMISSION de SURVEILLANCE du SECTEUR FINANCIER

ANNUAL REPORT

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Perceptible since the second quarter of 2003, the signs of a revival of activities must be interpreted prudently. Firstly, due to the feeble and progressive nature of this revival, the first results need to be confirmed so that 2004 meets the market participants' expectations. However, even if the positive development of the economic situation continues over the next months, we must be aware that there will be no return to the heydays, with such outstanding profitability as at the end of the last century. This stems from the simple fact that the financial centre has been undergoing an unprecedented transformation for some time now.

You can retort, with good reason, that what makes Luxembourg so original, is precisely, and has always been, its adaptability. The last decades perfectly illustrate this point: from the activities of euro-credits and portfolio management to investment funds, they all prove Luxembourg's ability to innovate and diversify. All of this is incontestable, except that Luxembourg has always met until now real needs by developing above all solutions peculiar to its situation. However, this stage seems to be over, as the States' room for manoeuvre keeps slimming down and the Luxembourg financial centre, like the others, is subject to many regulations and behaviours imposed by the international financial community. The national specificity of the financial centres is decreasing; this marks a fundamental break for Luxembourg which is used to cultivate its originality.

Certain observers describe this development using the terms "off-shore" and "on-shore", Luxembourg changing from "off-shore" centre to "on-shore" centre. The use of these terms is rather unpleasant, as they are very simplistic and do not adequately reflect reality. Thus, Luxembourg has never been a typical "off-shore" financial centre, as it has never been sheltered from tax or regulatory constraints, nor will it ever be a typical "on-shore" financial centre, because it will always depend on foreign capital. However, the centre fits into a new environment, a sort of global market, where the difference will be less made through regulatory aspects and more through diversification and the quality of the services offered by the players.

In this context, as I had predicted since 1999, not without making some waves, the banking secrecy is not considered anymore as element conditioning the development of the financial centre. Although its importance decreases – and will continue to decrease in the future -, it nonetheless constitutes an important asset, but only one among others. Quite opportunely, a note drawn up by the CSSF's CODEJU committee, under the aegis of the *Comité pour le développement de la place financière*, and published as annexe to this Annual Report, presents the implications of the concept of secrecy in the current context. This contribution is all the more interesting as it is balanced and answers various, sometimes even contradictory concerns.

As a conclusion, I would like to stress that the institution, which I am honoured to manage, keeps multiplying its efforts to contribute to the balanced development of the financial centre and to meet the growing commitments as regards international co-operation. The CSSF's annual report is an analysis and synthesis reflecting these multiple efforts, for which I thank all members of staff.

Jean-Nicolas SCHAUS
Director General

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Corporate governing bodies of the Commission de Surveillance du Secteur Financier

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CHAPTER I

INFORMATION CONCERNING THE LAW OF 2 AUGUST 2003

Information concerning the law of 2 August 2003 amending

- **the law of 5 April 1993 on the financial sector;**
- **the law of 23 December 1998 creating a *commission de surveillance du secteur financier*;**
- **the law of 31 May 1999 governing the domiciliation of companies**

The primary purpose of the aforementioned law, which came into force on 1 October 2003, is to ensure that the entire financial sector is subject to a prudential supervision. It also defines new categories of PFS, notably by bringing under the financial sector a certain number of connected or complementary activities to a financial activity.

The law of 2 August 2003, which provides the required legislative framework to new activities, aims at promoting the development of the Luxembourg financial centre towards a first-rate centre in the fields of specific competence.

In particular, the creation of specific statuses as regards IT and communication proves to be an interesting factor for the development of the financial centre, as submitting these activities to a state supervision is consistent with the wish of the financial players, who consider that the immediate advantages of the creation of such statuses lie in the limitation of emerging risks, as well as in the guarantee of the quality of services provided.

Moreover, this regulation, which makes Luxembourg one of the first countries to grant the status of supervised professional of the financial sector notably to subcontractors in the fields of IT and communication, will allow to promote the provision of these services from Luxembourg to the foreign financial sector.

Given that the law regulates a certain number of activities in Luxembourg, a person performing one of the activities subject to a PFS status does not have the choice to opt for a status, but is obliged to request and obtain the status concerned.
Consequently, it should be pointed out that banks and traditional PFS may not, in principle, delegate tasks that correspond to one of the activities of a PFS status to entities that are not appropriately authorised.
However, the law of 2 August 2003 does not affect the possibility to outsource an IT function to a third party abroad, as the law only concerns operators established in Luxembourg.
Nevertheless, as regards the possibility to delegate the IT function to a third party abroad, it should be referred to the restrictive conditions laid down by the supervisory authority (currently circular IML 96/126).

Where an entity of the financial sector delegates tasks corresponding to activities under a PFS status and where this PFS has been granted the appropriate authorisation, this entity only needs to notify the CSSF of the use of subcontractors. A prior authorisation of the CSSF to delegate these tasks to a duly approved provider of services is not required.

1. Scope of the CSSF's supervision

The law of 2 August 2003 submits the whole financial sector to prudential supervision. Thus, PFS not falling under a specific category and subject to the general provisions of the law of 5 April 1993 on the financial sector as amended providing for their approval, are also submitted to the supervision of the CSSF, as is also the case for professionals collecting debt and those who perform cash-exchange transactions.

The law of 2 August 2003 does not affect the appreciation power of the CSSF to submit an activity falling under the financial sector by nature to the general provisions of the law on the financial sector. However, the law restrictively lists the legal statuses that correspond to connected or complementary activities, so that the CSSF does not have the power to subject other connected or complementary activities to the general provisions of the law on the financial sector.

- **Information concerning the "group exception"**

Like the provision concerning investment services provided within a group, those entities carrying out an activity of the financial sector other than an investment service exclusively for a company of the group to which they belong, are not required to obtain prior authorisation and are consequently not under the supervision of the CSSF.

Indeed, article I paragraph (2) of the law of 2 August 2003 introduces into article 13 paragraph (2) of the law on the financial sector a supplementary indent, which excludes from the application of Chapter 2 relating to the requirement for approval those companies that provide a service within the scope of this Chapter other than an investment service, exclusively to one or more persons belonging to the same group as the company providing that service.

However, the group exception only applies in so far as there are no specific contrary provisions. Indeed, in accordance with the general principles of law, a specific legal rule may derogate from a general legal rule of the same level.
In order to avoid any ambiguity as regards the scope of the new indent of article 13 in relation to the status of company domiciliation agents (article 29 of the law of 5 April 1993 as amended), it must be stressed that notwithstanding article 13 paragraph (2), the companies which accept that one or more companies of the group to which they belong themselves establish a seat with them with a view to carrying out an activity within the scope of their corporate object and which provide any services relating to this activity, are also company domiciliation agents according to article 29 and therefore constrained to obtain prior approval and submitted to the supervision of the CSSF (please refer to the CSSF's interpretation of article 29).

As regards factoring, the group exception only applies on the condition that not only the assignee and assignor, but also the debtor of the assigned debts belong to the same group.
On the other hand, where debts are redeemed exclusively from companies belonging to the group, but where the debt is recovered from third-party debtors, the factoring company must be authorised under the status of professional performing credit offering according to article 28-4 of the law on the financial sector.

- **Interpretation of the concept of "group" according to the law of 2 August 2003**

The concept of group is not defined by the law of 2 August 2003. The CSSF considers that a group according to the law of 2 August 2003, can be defined as a group of companies composed of a parent company, its subsidiaries and entities in which the parent company or its subsidiaries hold a participation. This definition is inspired by directive 2002/87/EC of the European Parliament and of the Council of 16 December 2002 relating to financial conglomerates.

The CSSF considers that companies held by the same natural persons are not to be considered as a group according to article 13(2), even if these companies are located at the same address, have the same managers or have common interests or common customers.

2. The new PFS categories

As regards the new PFS categories, the law distinguishes those that correspond to financial activities by their nature from those whose activities are connected or complementary to a financial activity.

2.1. The new PFS whose activities are financial by nature

- **Registrar and transfer agents (article 24-G)**

Registrar and transfer agents are considered as investment firms. As far as the field of UCIs in particular is concerned, the tasks of the registrar and transfer agent consist in the receipt and execution of issues and redemptions of UCI securities, as well as the keeping of the register of participants. The registrar and transfer agent receives orders on units/shares of UCIs either directly from investors, or indirectly through distributors. In this context, it needs to be stressed that simply registering orders on units/shares of UCIs does not require an authorisation as distributor of units/shares of investment funds as referred to in article 24D) of the law of 5 April 1993 on the financial sector as amended. Indeed, the status as distributor of units/shares of investment funds exclusively aims at professionals whose activity consists in actively distributing units/shares of UCIs admitted to trading in Luxembourg, which implies that the professional is himself in charge of the placement of the units/shares.

As far as investment funds are concerned, this status allows a provider of services to perform for the account of one or several UCIs all the tasks comprised in the concept of central administration. Indeed, registrar and transfer agents of the financial sector are *ipso jure* empowered to act as an administrative agent of the financial sector (encompassing inter alia NAV calculation) and as a client communication agent for UCIs for which they are keeping a register.

The status as registrar and transfer agent is of course not required for entities, which are authorised as management companies of UCITS, as management companies of non-coordinated UCIs under Luxembourg law or as management companies not having designated a management company, as the activity of collective portfolio management also encompasses, further to the portfolio management and the marketing thereof, the functions of central administration, including the keeping of the register of unit/share holders, as well as the issue and redemption of units/shares.

- **Professionals performing credit offering (article 28-4)**

This status concerns professionals who grant all kinds of loans without calling on public savings to refinance.

This status covers, in particular, consumer credits, including financial leasing operations, except if the credit activity is carried out as non-core activity in the context of an activity governed by the law of 28 December 1988 on the right of establishment. The activity of granting consumer credits carried out by shopkeepers and craftsmen will be subject to the authorisation of the Minister in charge of the CSSF and to the supervision of the CSSF, if the loan portfolio represents more than 50% of the total volume of the sale of goods and services.

- **Professionals performing securities lending (article 28-5)**

This category concerns professionals performing securities lending/borrowing transactions as contracting party, i.e. who act on their own behalf and for their own account. The professional intermediaries active in the field of securities lending who act for the account of third parties must be authorised either as commission agents, if they act in their own name, or as brokers, if their role consists in locating the required securities and bringing the parties together.

- **Professionals performing money transfer services (article 28-6)**

This status concerns professionals whose activity consists in the receipt of funds from a customer and their transfer for the account of such customer to a third entity against book entry, in order to place such funds at the disposal of a beneficiary designated by the customer or to keep the abovementioned funds for disposal and transfer to a beneficiary.

- **Administrators of collective savings funds (article 28-7)**

Administrators of collective savings funds are not allowed to act for their own account, nor are they allowed to receive and keep the assets of savers as deposits.

- **Management companies of non-coordinated UCIs (article 28-8)**

This status concerns entities whose activity is limited to the management of non-coordinated foreign UCIs, i.e. entities, which do not manage a Luxembourg UCI nor a UCITS.

Indeed, the management companies under Luxembourg law which manage at least one approved UCITS in accordance with directive 85/611/EC, including their branches, as well as the management companies which manage at least one non-coordinated UCI under Luxembourg law, are governed by the law of 20 December 2002 concerning undertakings for collective investment.

The management activity may include central administration services. The managers of non-coordinated UCIs are allowed to provide these services only for UCIs for which they provide management services as such and to which they are thus closely linked.

2.2. PFS providing a connected or complementary activity to an activity of the financial sector

- **Domiciliation agents of companies (article 29)**

Although this status has not been amended by the law of 2 August 2003, it is nevertheless useful to provide certain explanations concerning the second point of article 29, which qualifies as domiciliation agents of companies those companies, that accept that one or several companies of the group to which they belong themselves establish a registered office with them in order to carry out an activity as part of their corporate object and which render any services connected with said activity.

In view of article 1(4) of the law of 31 May 1999 governing domiciliation of companies as amended, the CSSF considers that this provision must be interpreted in the sense that companies which domicile a company of the same group, without being a member exerting a significant influence on the conduct of business, are domiciliation agents of companies under article 29, but are granted a light regime insofar as the CSSF can relax the conditions for approval compared with the conditions applicable to traditional domiciliation agents. It must be noted that article 13(2) fourth point of the law on the financial sector does not apply to domiciliation agents of companies. A subsidiary that provides domiciliation services exclusively to other companies of the group to which it belongs itself, is thus subject to the requirement of a ministerial authorisation and the supervision of the CSSF according to article 29(1). As professional of the financial sector, it is obliged to comply with all the professional obligations of the financial sector, further to the professional obligations specific to the domiciliation agent of companies applicable pursuant to the law of 31 May 1999 on company domiciliation as amended.

- **Client communication agents (article 29-1)**

Traditional printing services within the financial sector, i.e. the production and printing of non-confidential documents, are not subject to authorisation. Client communication agents may however provide these services as non-core activity.

Archiving of confidential documents for personal use of customers of professionals of the financial sector, such as transaction confirmations, statements of account, tax returns, inter alia, is however subject to authorisation. Nevertheless, where these documents are not accessible to the service providers, for instance where they are stored in safes to which only the client professional of the financial sector has access, the status of client communication agent is not required.

The availability, via Internet, of a platform serving as support for the transmission of financial advice provided by third parties, is not an activity requiring the authorisation as client communication agent. The CSSF however considers that where the financial advice is provided on an individual basis (for instance by means of personalised passwords), the provider of services, who provides the platform, must be approved as financial advisor pursuant to article 25 of the law of 5 April 1993 on the financial sector as amended, if his client who uses the platform to transmit financial advice, has not been granted the required approval for this activity.

- **Administrative agents of the financial sector (article 29-2)**

The activities of these professionals cover back-office services and encompass, *inter alia*, the calculation of the net asset value of units/shares of UCIs. In order to avoid any misunderstanding, it must be stressed that this status does not cover the concept of central administration of UCIs in Luxembourg. Administrative agents may intervene actively in the work processes of their clients (account opening, definition of the software parameterisation, etc.).

The administrative agents of the financial sector are not obliged to exclusively act for the financial sector.

- **IT systems and communication networks operators of the financial sector (article 29-3)**

These professionals cannot intervene in the definition of IT software parameterisation, which remains under the control of the client, but are only allowed to perform the technical system parameterisation. They must exclusively act for the account of credit institutions, PFS, UCIs or pension funds under Luxembourg or foreign law[1].

The exclusive provision to the financial sector imposed by law aims, on the one hand, to preserve a uniform legal framework specific to the financial sector, and, on the other hand, to avoid that external services to the financial sector penalise those provided under the status as PFS. Given the importance of these connected services for financial market participants, the legislator wished to put forward the need for companies, which adopt this status, to exclusively serve clients of the financial sector, allowing thereby the supervisory authority of the financial sector to control all the outsourced activities.

A company, which already offers some of these services to entities outside the financial sector and wishes to extend its services to the financial sector by opting for this status, is compelled to create either a new entity authorised as PFS, or, after having become a PFS, an entity which will take over the services provided to entities outside the financial sector.

The PFS can thus provide certain services the CSSF will define on an individual basis (for instance: non-core activity, advice, monitoring of events, provision of IT premises for exclusive use) to clients outside the financial sector through a subsidiary or parent company, by complying with two principles:

- There must be no contract binding the final client outside the financial sector to the PFS and contracts between the customer and the subsidiary or the parent company must not mention services provided by the PFS, in order to avoid any legal proceedings of the client against the PFS.
- The contract binding the subsidiary or the parent company to the PFS concerning services authorised by the CSSF must contain two clauses, namely:
  - The subsidiary or parent company can, in no case, take legal and financial action against the PFS in a way that could jeopardise the perenniality of the PFS or of the services provided to customers of the financial sector.
  - It must be allowed to break off the contract, without damages for the PFS, in particular where the CSSF considers that the services provided outside the financial sector are not compatible with the quality or nature of the services provided within the financial sector (for instance: decrease in the quality of service, conflicts of interest, etc.).

Furthermore, an IT systems and communication networks operator of the financial sector cannot outsource its activity to another provider of services. The PFS cannot make use of the resources of the entity it belongs to or of its subsidiary, which implies extra skilled personnel and technical infrastructures. In order not to economically penalise the implementation of this new status, the PFS could use the staff and infrastructure needed for its activity and insource the activity of the entity it belongs to or of its subsidiary, i.e. provide for the company of origin (the group) the services initially provided for entities outside the financial sector. Legally, this implies that in order to provide existing services to entities outside the financial sector, the PFS signs a single contract with the entity to which it belongs or the group to which it belongs, which in turn is under contract with the clients outside the financial sector.

In order to clarify for which activities a status as IT systems and communication networks operator of the financial sector is required, respectively which services can be provided without being authorised as PFS, the principles which allow to assess which services require a PFS status, article 29-3 are set forth below. There are two situations conditioning the need for a service provider to obtain a PFS status, article 29-3.

[1] *Insurance undertakings, as they are not governed by the law of 5 April 1993 on the financial sector as amended, cannot, in this context, be considered as being part of the financial sector. However, foreign insurance undertakings can, depending on the countries, be considered as being part of the financial sector.*

First situation: the nature itself of the service

The provider of services has access rights as administrator of a production system, i.e. a system used for the recurrent and core activity of the professional of the financial sector, irrespective of the fact that this system contains confidential data, not only relating to the identification of customers, but also to the accounting or transactional nature (purchase and sale of securities, for instance). Due to the extent of his rights, he is considered as "operator" of the system, as he is able to modify or to create other access rights and can *a priori* execute production programs. The same is the case where he detains rights to administer data bases, which is a crucial sub-system of the production systems.

The service provider is also considered as "operator", even without full access rights, as soon as he is in charge of operating the production system. Thus, launching batch programs at the end of the day, even without full access rights, is considered as an operator activity and requires therefore an authorisation as PFS. On the other hand, a passive supervisory activity (monitoring) does not require a status, on the condition that the system generates the information to be used for supervision and that the provider does not intervene on the system and only informs a person in charge of the financial professional. This situation is acceptable without being granted an authorisation as PFS, as the provider does not manage the system.

Second situation: the professional of the financial sector is unable to comply with the provisions of circular IML 96/126

The recurrent services allow the provider to have access to confidential information and, in particular, to nominative data or data allowing to identify customers. Circular IML 96/126 provides that the financial professional must limit the occurrences where the provider has access to confidential data ("Where, in the case of a significant systems breakdown which requires repair on the premises, access to such information cannot be avoided, the institution must ensure that the third party responsible for the repairs is accompanied throughout his intervention by an employee of the institution responsible for IT matters"). Paragraphs e), f) and h) of point 4.5.2.1. of the circular clearly explain this matter.
There is no requirement for the provider to be authorised as PFS if the services he provides are not operating services. However, a PFS is not allowed, in principle, to delegate his work to a non-PFS provider who has recurring access to a system containing confidential information.
The law of 2 August 2003 specifies that the confidentiality requirement is not applicable to the professionals mentioned in articles 29-1, 29-2 and 29-3, insofar as the extent to which the information transmitted to such professionals is transmitted under a service agreement pertaining to an activity regulated by the aforementioned legal provisions and provided that such information is necessary for the execution of the said agreement.

The CSSF's experience shows that in borderline cases, where a professional of the financial sector argues that he supervises the recurrent access of his provider, this control becomes theoretical. Certain procedural provisions, which should ensure perfect control by a PFS, proved not very perennial and led to a substantial increase in the risks of disclosure. The CSSF is therefore not favourable to procedural solutions, which do not offer any guarantees as to access control to confidential information.

Consequently, the professionals of the financial sector can entrust the provider, who opts for one of the above-mentioned statuses, with tasks requiring access to confidential data. The provider must of course provide, within the scope of his global activity, the services foreseen by the agreement. The provider cannot be granted an authorisation beyond twelve months if he does not provide any service in relation to his status (art. 23(1)). As an example, he cannot keep an authorisation as system operator (art. 29-3) for an activity of IT development, even though he does not operate any system, irrespective of his customers.

Specific explanations to help-desk services

Help desk functions illustrate the preceding explanations. These functions consist of tasks concerning administration and operating systems, in particular, where a provider remotely accesses the workstation. Moreover, as the latter may be led to see confidential information during these interventions, he must be adequately authorised as PFS, so that the financial professional can entrust him with these services. The financial professional must prove to the CSSF that the tasks he performs within his help-desk activities are not such as to be considered as "system or network operator" and that he is not able to access confidential data. This might be the case where the assistance takes place over the phone and the service provider asks the user to execute the tasks in his place. Confidentiality therefore only depends on the user.

General considerations

The preceding situations are *a priori* applicable irrespective of the equipment in use, be they computers, network or telecommunication equipment, including, to a certain extent, telephony, if the operator is not subject to the laws governing the professional secrecy of communications.
As a consequence and in response to recurrent questions on recovery centres, the availability of such centres does not require an authorisation as PFS insomuch as the provider does not intervene on the production equipments or stand-by equipments (technical DRP term) containing production data. This situation originates in the impossibility of the financial undertaking to outsource these functions to a provider not authorised as PFS in accordance with articles 29-2 or 29-3 of the law, as the conditions listed under point 4.5.2.1. of circular IML 96/126 could not be complied with.

- **Professionals performing services of setting up and of management of companies (article 29-4)**

This article is directed at natural and legal persons whose professional activity consists in offering services connected with the setting up and management of companies to third parties.
First of all, it must be pointed out that the application of article 29-4 requires that the activity concerned be performed in a professional capacity, which implies that it has to be performed in a recurrent manner.
Moreover, article 29-4 exclusively concerns entities which act for the account of third parties that are customers of the professional concerned. The relationship professional-customer is therefore decisive as regards the application of this article.
The services connected with the setting up of companies consist in providing, for the account of the client, any type of service necessary to set up the type of company envisaged by the latter.
As regards the services related to the management of companies, article 29-4 is directed at entities that provide administrators, directors or managers to third-party companies. These entities can act either as intermediary charged with providing representatives, or by intervening actively in the management of the client company.
However, the administrators, directors or managers that are employees of a company whose professional activity consists in providing services connected to the setting up or management of companies, are not subject to the requirements of article 29-4, as the employer company is to be considered as professional. The persons who take on a post of administrator, director or manager for their own account and irrespective of any request of a third party based on a professional-client relationship, as described above, are thus not subject to this article.

Moreover, all the professionals allowed to perform domiciliation services of companies, i.e. the domiciliation agents of companies under article 29 of the law of 5 April 1993 on the financial sector as amended, as well as notaries and the registered members of other regulated professions listed in paragraph (1) of article 1 of the law of 31 May 1999 governing the domiciliation of companies as amended, are *ipso jure* authorised to perform services of setting up and management of companies. This list also includes lawyers, external auditors (*réviseurs d'entreprises*) and chartered accountants (*experts-comptables*). These persons are thus not obliged to obtain the authorisation of the Minister having the CSSF in his remit, nor are they

subject to the prudential supervision of the CSSF. Indeed, these professionals have the required skills by virtue of their education and qualifications and are therefore subject to the supervision of the supervisory bodies of their respective professions.

3. Conditions of approval

In principle, the new PFS are subject to the same conditions of approval as traditional PFS, except for contrary specific legal provisions. However, the CSSF can adapt and adjust certain conditions, such as notably the credit requirement, according to the activity performed. Thus, the notion "credit standing" can be interpreted as acknowledgement of the experience acquired in this field as regards certain categories.

4. Wording of the authorisation of PFS

The CSSF considers that only the activities actually performed by a PFS must be mentioned in the given authorisation. The activities that the professional is *ipso jure* empowered to carry on in accordance with the law of 5 April 1993 on the financial sector as amended will therefore not be mentioned in the authorisation, unless they are actually carried on.
Where a PFS wishes at a later stage to perform one of these activities, this activity must be added to the authorisation by way of notification.
There is no objection however as to the fact that the corporate purpose of the PFS lists all the activities he can carry out *ipso jure* in accordance with the law.

5. Purpose of the prudential supervision

Within the scope of its supervisory mission, the CSSF will verify, inter alia, the technical qualification of the entity concerned allowing it to perform the envisaged activity according to the rule book. The CSSF will thus attach particular attention to the verification of the means implemented to ensure data confidentiality, such as verifying access to premises, authentication procedures of persons and protective measures and data segregation.

6. Information concerning the legal exception of the professional secrecy

Article 41(5) establishes a legal exception to the professional secrecy with regard to a financial professional (bank or PFS), in order to enable him to outsource certain tasks allowing access to confidential information concerning his clients. Even if these tasks are entrusted to subcontractors which are themselves authorised as PFS or bank, the professional who delegates the tasks must be authorised by law to transmit data concerning his clients.

In this respect, the CSSF was confronted with the following hypothesis.
A bank intends to perform subcontracting services regarding administrative tasks exclusively for its subsidiary which is itself authorised as PFS. The activity concerned is thus provided exclusively for the account of the group, so that the bank is therefore not required to obtain a ministerial authorisation as PFS.
However, the subsidiary, which is a PFS itself, is subject to the obligation of professional secrecy in accordance with article 41. The subsidiary can therefore not disclose any information on its clients to a third party, and in particular, to the subcontracting bank, unless a legal exception to the banking secrecy exists.

Such an exception has been introduced by the law of 2 August 2003. In accordance with the latter, the financial professionals subject to article 41(1) can delegate some of their activities giving access to information governed by professional secrecy within the scope of an outsourcing agreement, to third-party service providers specifically appointed by law, in compliance with the legal provisions. They are client communication agents, administrative agents of the financial sector and IT systems and communication networks operators of the financial sector (articles 29-1, 29-2 and 29-3).

As a result, the subsidiary cannot outsource the tasks regarding client communication, administrative or back-office tasks or tasks relating to the functioning of its IT system and communication networks to the parent company which is authorised as credit institution, unless the latter is authorised as client communication agent, administrative agent of the financial sector or IT systems and communication networks operator of the financial sector, respectively.

7. Multiple functions of the same entity

The PFS can hold several statuses concurrently. An entity that holds several statuses foreseen by the law of 5 April 1993 on the financial sector as amended is subject to proof of the highest capital or credit standing of the statuses concerned.

The status of universal bank allows credit institutions to perform any type of activities of the financial sector, as well as one or several connected or complementary activities, provided that they fall within the scope of its usual activity.
In particular, a credit institution can act as central administration for the account of UCIs without being subject to the requirement of a specific agreement as registrar and transfer agent.

8. Cascade outsourcing

A PFS is not allowed to outsource the core activity for which it has obtained authorisation. Nothing however prevents it from delegating a secondary activity to a third-party service provider, in compliance with the legal provisions.
For instance, a registrar and transfer agent is not allowed to delegate the keeping of the register of the unit holders or the issues and redemptions of units/shares of UCIs to credit institutions.

9. Obligations as regards the fight against money laundering

The new PFS must comply with all the professional obligations of the financial sector and in particular with the obligation to know their clients and to co-operate with the authorities.
In accordance with paragraph (5) of article 39 of the law of 5 April 1993 as amended, the financial professional is exempt from the obligation to know his clients and the beneficial owners, if the client is a credit institution or a PFS subject to an equivalent identification requirement.
As regards the outsourcing statuses (articles 29-1, 29-2 and 29-3), the clients of these new PFS categories are by definition credit institutions, PFS, UCIs or pension funds, so that the exemption from the identification requirement provided in article 39(5) is always applicable to their Luxembourg clients.
The same applies for foreign clients, which are subject to an equivalent identification requirement, which is notably the case of the financial professionals established in FATF countries.

CHAPTER II

SUPERVISION OF THE BANKING SECTOR

1. Developments in the banking sector in 2003
2. Developments in the regulatory framework
3. Prudential supervisory practice

1. Developments in the banking sector in 2003

1.1. Characteristics of the Luxembourg banking sector

Luxembourg banking law recognises three types of banking licences, namely licences governing the activities of universal banks (166 institutions having this status on 31 December 2003), those governing the activities of banks issuing mortgage bonds (3 institutions having this status on 31 December 2003) and those governing the activities of institutions issuing electronic means of payment (no institution having this status on 31 December 2003).

The universal banks comprise three categories according to legal status and geographical origin:

- banks under the law of Luxembourg (119 on 31 December 2003);
- branches of banks originating from a Member State of the European Union (43 on 31 December 2003);
- branches of banks originating from non-Member States of the European Union (7 on 31 December 2003)

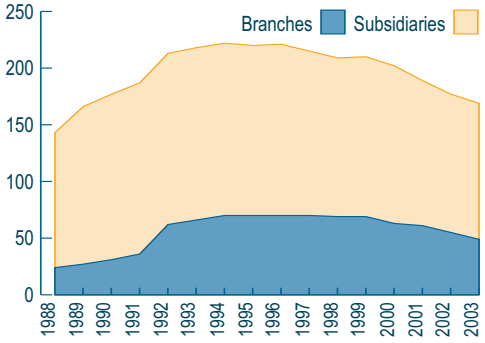
In addition, there is the special case of the unit formed by the *caisses rurales* (26 on 31 December 2003) and their central establishment, the Banque Raiffeisen, which, according to the law relating to the financial sector, is to be considered as a single credit institution.

1.2. Developments in the number of credit institutions

The downward trend of the number of credit institutions established in Luxembourg was again confirmed in 2003. Indeed, the total number of banks only amounts to 169 as at 31 December 2003, compared to 177 as at 31 December 2002. The 169 entities comprise 119 Luxembourg-registered banks (2002: 122) and 50 branches (2002: 55).

Developments in the total number of banks established in Luxembourg

Year	Number of branches	Number of subsidiaries	Total number
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



The development of the total number of credit institutions notably depends on the following phenomena:

- Mergers, generally originating in the restructuring of the parent companies abroad, necessarily affect their Luxembourg presences, although the rate of mergers slowed down in 2003. Thus, three banks withdrew for this reason in 2003, against seven in 2002.

- Eight banks decided to cease their activities in 2003. One bank split into two new entities.

Liquidations / Mergers / Splits	Date of withdrawal from the official list of credit institutions
Crédit Agricole Indosuez Luxembourg	Withdrawal on 28.02.2003 (split into two new entities: Crédit Agricole Investor Services Bank Luxembourg and Crédit Agricole Indosuez Luxembourg)
Frankfurter Sparkasse, Luxembourg branch	Withdrawal on 31.03.2003
ING Bank (Luxembourg) S.A.	Merger with ING Luxembourg S.A. (formerly Crédit Européen S.A.) on 05.05.2003
BFI Bank AG, Luxemburg branch	Withdrawal on 23.05.2003
Volksbank Saar-West eG, Luxembourg branch	Withdrawal on 30.06.2003
BHW Allgemeine Bausparkasse AG, Luxembourg branch	Merger with BHW Bausparkasse AG, Luxembourg branch, on 01.08.2003
Banco Bradesco (Luxembourg) S.A.	Merger with Banco Mercantil de São Paulo International S.A. on 29.09.2003
Banque pour l'Europe S.A.	Withdrawal on 27.10.2003
Banco Popolare di Verona e Novara, Luxembourg branch	Withdrawal on 31.10.2003
KHB International S.A. Luxembourg	Withdrawal on 12.12.2003
WGZ-Bank Westdeutsche Genossenschaftszentrale eG, Luxembourg branch	Withdrawal on 31.12.2003
Banque Fédérative du Crédit Mutuel, Luxembourg branch	Withdrawal on 31.12.2003

Four new banks started their activities in 2003. The banks Crédit Agricole Investor Services Luxembourg and Crédit Agricole Indosuez Luxembourg have been created through the split of Crédit Agricole Indosuez Luxembourg.

Creation	Shareholders	Date of registration on the official list of credit institutions
Kaupthing Bunadarbanki, Luxembourg branch	Kaupthing Bunadarbanki (Iceland)	1 January 2003
Crédit Agricole Investor Services Bank Luxembourg	Crédit Agricole Indosuez, Paris	28 February 2003
Crédit Agricole Indosuez Luxembourg	Crédit Agricole Indosuez, Paris	28 February 2003
Islandsbanki hf, Luxembourg branch	Islandsbanki hf (Iceland)	1 July 2003

The breakdown of the credit institutions according to geographical origin has changed as follows (2002 figures between brackets). The banks of German origin are still the highest in number with 49 (56) entities, followed by Belgian and Luxembourg banks, with 19 (19) entities. Other banks originate from France with 17 (17 entities), Italy with 16 (17) entities, Switzerland with 13 (11) entities, Sweden with 7 (6) and the United States with 6 (6) entities.

Geographic origin of the banks

Country	Number
Germany	49
Belgium/ Luxembourg	19
France	17
Italy	16
Switzerland	13
Sweden	7
United States	6
Japan	5
United Kingdom	5
China	4
Portugal	4
Brazil	3
Israel	3
Netherlands	3
Denmark	2
Others	13
Total	**169**

1.3. Developments in the local branch networks in Luxembourg

The downward trend in branch networks recorded since the 1990s continued in 2003, as shown below.

	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003
Local branches	262	260	254	240	231	226	225	214	207	200
Banks concerned	11	11	11	11	11	10	9	9	8	8

The reduction in the number of local branches is one of the phenomena reflecting the general trend towards concentration in the sector. In this case, concentration takes place on a more local level, mainly affecting a specific type of activity, namely retail banking, and is motivated by cost-cutting measures. The services traditionally provided by local branches are being increasingly substituted by technical facilities (ATMs, home banking, phone banking, internet banking, etc.).

On the other hand, certain banks tend to relinquish the concept of small convenience branches providing only retail services for the benefit of larger branches, which serve, besides the customers of the retail banking, also private banking customers, and which dispose of an adequate infrastructure for this type of activity.

1.4. Development in banking-sector employment

Total employment of Luxembourg credit institutions on 31 December 2003 reached 22,529 persons, representing a decrease of 771 persons (-3.3%) as compared to 31 December 2002.

Employment in the Luxembourg banking sector has been decreasing for two years due to the economic situation – the world economy growth has been slowing down – and due to structural reasons – consolidation and reorganisation of the production means. Banking employment thus decreased by 1,332 persons over two years, a development contrasting with the net creation of 2,664 jobs in 2000 and 2001.

However, the phenomenon in question does not affect the different credit institutions and business lines in the financial centre in the same manner. Firstly, it has to be noted that only 53% of the Luxembourg credit institutions cut their workforce in 2003. Among them are the large banks, which, affiliated to a large international group, must contribute to consolidated cost-cutting. Secondly, the restructurings mostly concern activities with less value added and high benefits from economies of scale. This trend appears in the employment statistics as the declines in workforce concentrate solely on bank employees and workers, whereas employment of senior managers and executives grows by 3% in a year.

Finally, the drop in workforce as observed in the banking sector does not necessarily come with a reduction in interior employment in the Grand Duchy. Indeed, the possibilities of reorganisation given to credit institutions by the new laws relating to management companies[1] and the other professionals of the financial sector[2] include the transfer of staff from banks to other professionals of the financial sector. These outsourcing practices even entail, in certain cases, a transfer of staff outside the financial sector, as is the case notably for the outsourcing of certain IT functions.

Distribution of the number of employees per bank

Number of employees	Number of banks	
	2002	2003
>1000	4	4
500 to 1000	6	4
400 to 500	3	4
300 to 400	7	6
200 to 300	9	11
100 to 200	18	19
50 to 100	23	21
<50	105	100

[1] *Law of 20 December 2002 as amended concerning undertakings for collective investment.*
[2] *Please also refer to Chapter I on the law of 2 August 2003 concerning professionals of the financial sector.*

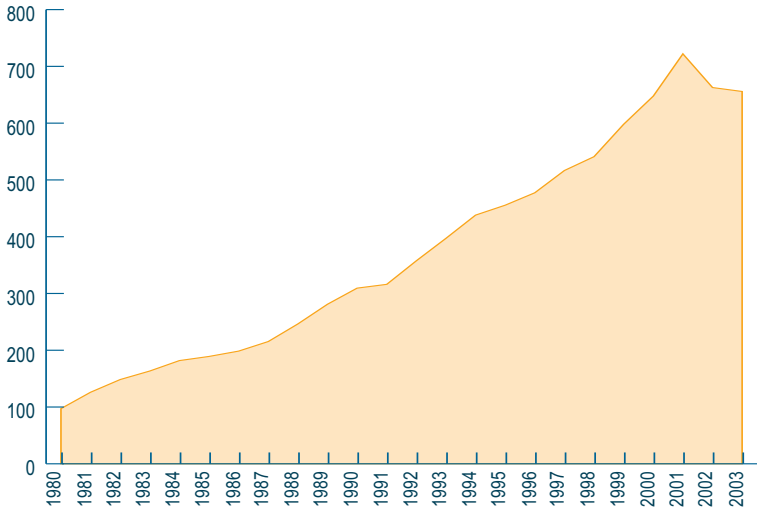
	Total		Management			Office staff			Technical staff			Total workforce		
	Luxemb.	Foreigners	Men	Women	Total	Men	Women	Total	Men	Women	Total	Men	Women	Total
1993	8158	8567	2097	335	2432	6713	7396	14109	68	116	184	8878	7847	16725
1994	8116	9522	2308	384	2692	7086	7700	14786	47	113	160	9441	8197	17638
1995	8170	10113	2533	451	2984	7318	7813	15131	49	119	168	9900	8383	18283
1996	8113	10469	2658	490	3148	7476	7809	15285	48	101	149	10182	8400	18582
1997	8003	11086	2765	547	3312	7631	8013	15644	44	89	133	10440	8649	19089
1998	7829	12005	2900	577	3477	7846	8377	16223	47	87	134	10793	9041	19834
1999	7797	13400	3119	670	3789	8362	8961	17323	34	51	85	11515	9682	21197
2000	7836	15232	3371	783	4154	9030	9801	18831	35	48	83	12436	10632	23068
2001	7713	16148	3581	917	4498	9222	10046	19268	33	62	95	12836	11025	23861
2002	7402	15898	3654	977	4631	8941	9657	18598	25	46	71	12620	10680	23300
2003	7117	15412	3720	1049	4769	8486	9211	17691	23	40	63	12229	10300	22529

1.5. Development in balance sheet totals

Balance sheet totals posted by credit institutions fell to EUR 655,768 million at the end of 2003 from EUR 662,700 million at the end of 2002, which represents a decrease of 1.05% during 2003.

Developments in balance sheet totals posted by credit institutions – *in billions of 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	655.77



Aggregated balance sheet total - *in millions of EUR*

ASSETS	2002	2003[3]	Variation in %	LIABILITIES	2002	2003[3]	Variation in %
Loans and advances to credit intitutions	342,707	339,933	-0.81%	Amounts owed to credit institutions	311,643	307,541	-1.32%
Loans and advances to customers	127,466	117,467	-7.84%	Amounts owed to customers	210,648	215,987	+2.53%
Fixed-income securities	142,697	148,975	+4.40%	Debts evidenced by certificates	71,801	69,199	-3.62%
Variable-yield securities	3,813	3,920	+2.79%	Various items	6,194	5,030	-18.79%
Participating interests and shares in affiliated undertakings	9,645	6,981	-27.62%	Permanent shareholders' equity (*)	62,414	58,010	-7.06%
Fixed assets and other assets	36,372	38,492	+5.83%	*of which profit for the year*	*2,709*	*2,878*	*+6.26%*
Total	**662,700**	**655,768**	**-1.05%**	**Total**	**662,700**	**655,768**	**-1.05%**

(*) Including share capital, reserves, subordinated liabilities and provisions.

[3] *Preliminary figures for the year ending 31.12.2003.*

- **Assets**

As far as assets are concerned, the drop in the balance sheet total essentially stems from a reduction in loans and advances to customers. Loans and advances to credit institutions and participating interests and shares in affiliated undertakings also fell. The other items of the banks' total assets however increased as compared to the end of 2002. The growth has been more substantial for fixed-income securities.

Loans and advances to credit institutions fell by 0.8% in 2003 to EUR 339,933 million, compared to a decrease of 5.4% in 2002, which was due to several important loans which had not been renewed. Loans and advances to credit institutions remained almost stable and represented 51.8%, reflecting the importance of interbank activities for the Luxembourg financial centre.

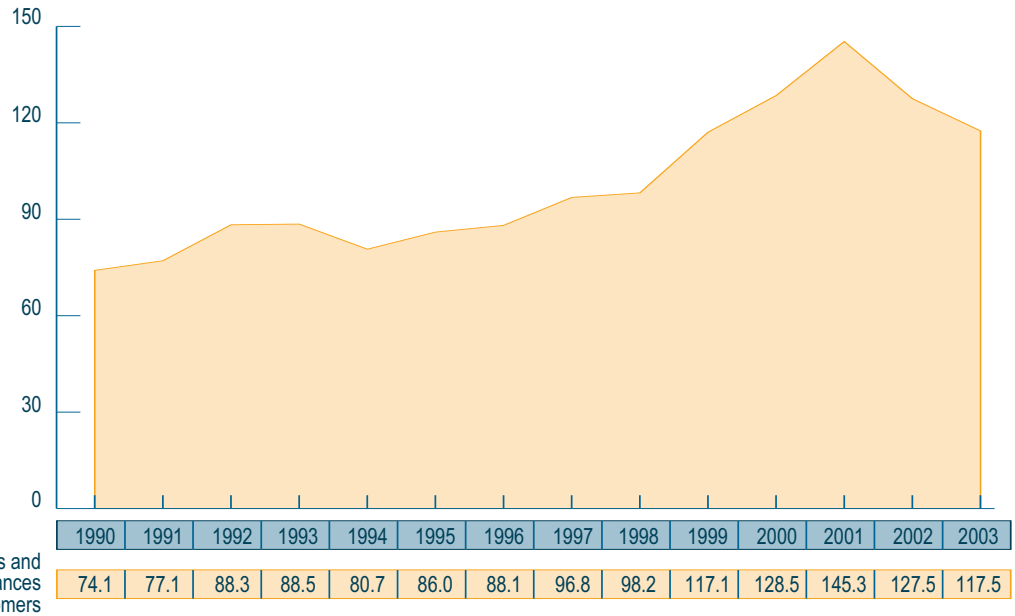
Qualitative breakdown of interbank assets

	2001	2002	2003
Central and multilateral banks	0.33%	0.30%	0.15%
Banks Zone A[4]	98.62%	98.48%	98.25%
Banks Zone B[5]	1.05%	1.23%	1.60%

This breakdown shows that the vast majority of loans and advances to credit institutions consist of commitments on Zone A banks, i.e. banks of industrialised countries. The breakdown in relative terms remained relatively stable over the last three years. Loans and advances on central and multilateral banks, which have been weak anyhow, have however experienced a substantial fall.

The item **loans and advances to customers** fell by 7.8% and amounts to EUR 117,467 million, i.e. 17.9% of the balance sheet total, compared to EUR 127,466 million in 2002.

Developments in loans and advances to customers *– in billions of EUR*



[4] *Countries Zone A: Germany, Saudi Arabia, Australia, Austria, Belgium, Canada, South Korea, Denmark, Spain, United States, Finland, France, Greece, Hungary, Ireland, Iceland, Italy, Japan, Liechtenstein, Luxembourg, Mexico, Norway, New Zealand, Netherlands, Poland, Portugal, United Kingdom, Slovakia, Sweden, Switzerland, Czech Republic, Turkey.*

[5] *Countries Zone B: all countries other than Zone A.*

Breakdown of loans and advances to customers

	2001	2002	2003
Public authorities Zone A	4.68%	5.59%	6.78%
Public authorities Zone B	0.30%	0.19%	0.19%
Private customers and financial institutions	94.97%	94.17%	92.97%
of which: legal entities	*54.14%*	*54.96%*	*52.50%*
of which: natural persons	*18.33%*	*21.32%*	*23.85%*
of which: financial institutions	*27.53%*	*23.66%*	*23.59%*
Leasing	0.05%	0.05%	0.06%

Loans and advances to legal entities dropped by 13% in 2003. The volume of loans and advances to financial institutions fell by 9.1%. A more restrictive credit policy of banks as regards their corporate clients can explain this development. This trend is even more perceptible for exposures to certain risk sectors[6]. The volume of loans and advances to natural persons however increased by 1.9%. Overall, this resulted in an increase in relative terms of loans and advances to natural persons and a fall in loans and advances to legal entities. Loans and advances to public authorities, generally in the form of securities, continued to grow in relative terms in 2003. They are still only fairly represented with less than 7% of the total loans and advances to customers.

Qualitative breakdown of loans and advances to private customers and financial institutions

	2001	2002	2003
Secured by public authorities	2.94%	3.97%	3.31%
Secured by credit institutions	17.69%	17.94%	16.63%
Secured by other tangible securities	27.97%	31.56%	32.57%
Unsecured	51.40%	46.53%	47.49%

After having grown in relative terms in 2001 and 2002, the secured part slightly decreased in 2003.

The portfolio of **fixed-income securities** rose by 4.4% following a decrease of the same order in 2002. This item reached EUR 148,975 million or 22.7% of the total balance sheet in 2003. The growth is essentially due to a strengthening of banks' holdings of high quality securities, notably in bonds of the public sector, as well as in bonds of credit institutions and other issuers of Zone A.

Qualitative breakdown of fixed-income securities

	2001	2002	2003
Public sector zone A	24.10%	24.53%	25.37%
Public sector zone B	0.97%	0.61%	0.68%
Credit institutions zone A	50.98%	50.82%	50.14%
Credit institutions zone B	1.06%	0.97%	0.78%
Other issuers zone A	17.57%	18.73%	18.94%
Other issuers zone B	5.33%	4.34%	4.09%

[6] *Please also refer to Chapter II, point 1.11. concerning exposures to high-risk sectors.*

The volume of the portfolio of **variable-yield securities**, i.e. equities, remains marginal, since Luxembourg banks are not very active in own-account trading of such stocks. This portfolio slightly recovered in 2003 (+2.8%), thanks to the improvement of stock exchange performances over the year.

The item **participating interests and shares in affiliated undertakings** decreased substantially in 2003 (-27.6%) and only represents 1.1% of the total balance sheet. The participating interests in banks, representing almost the whole item, dropped considerably over the year, notably due to provisions and withdrawal from certain activities abroad.

- **Liabilities**

As regards liabilities, amounts owed to credit institutions and amounts owed to customers developed in the opposite way.

Amounts owed to credit institutions fell to EUR 307,541 million (-1.3%). The interbank market remains the main source of refinancing of banks, with 46.9% of liabilities.

Amounts owed to customers, representing 32.9% of total liabilities, however increased by 2.5% to EUR 215,987 million at the end of 2003. Amounts owed to the public sector and legal entities rose whereas they had dropped in 2002. Amounts owed to natural persons (mainly deposits from private customers) continued to fall (-7.3% in 2003).

Breakdown of amounts owed to customers

	2001	2002	2003
Amounts owed to the public sector	5.95%	2.84%	3.92%
Amounts owed to legal entities	63.84%	66.22%	68.30%
Amounts owed to natural persons	30.21%	30.94%	27.79%

Amounts owed represented by securities fell by 3.6% in absolute terms compared to 2002. With 10.6% of the total liabilities, this source of financing remains interesting especially for banks issuing mortgage bonds.

Permanent shareholders' equity, including subscribed capital, reserves, provisions, subordinated debts and accruals, decreased by 7.1% over the year to EUR 58,010 million at the end of 2003. This drop stems mainly from a reduction in accruals and the volume of provisions made by the banks on their exposures.

1.6. Movements in profit and loss account

The aggregated profit and loss account of the Luxembourg credit institutions just resumed its growth recently. Following a decrease of 5% in 2002, net results of the Luxembourg banks thus rose by 6% over 2003. The net provisioning, whose fall of 47% reflects the improvement of international economic perspectives, explains this growth. It must be remembered that in 2002, this item grew by 118% in a highly uncertain economic context.

Profit and loss account - *in millions d'EUR*

	2001	Relative share	2002	Relative share	2003[7]	Relative share
Interests and dividends received	51,942		41,257		34,116	
Interests paid	47,560		37,116		30,035	
Interest-rate margin	**4,382**	**55%**	**4,141**	**51%**	**4,081**	**54%**
Fee income	2,792	35%	2,615	32%	2,529	33%
Income from financial operations	355	4%	261	3%	475	6%
Other income	410	5%	1,044	13%	495	7%
Banking income	**7,939**	**100%**	**8,061**	**100%**	**7,580**	**100%**
General administrative expenses	3,227	41%	3,182	39%	3,091	41%
of which: staff costs	*1,758*	*22%*	*1,809*	*22%*	*1,751*	*23%*
of which: other administrative expenses	*1,470*	*19%*	*1,373*	*17%*	*1,340*	*18%*
Depreciation	396	5%	308	4%	289	4%
Result before provisions	**4,316**	**54%**	**4,571**	**57%**	**4,200**	**55%**
Creation of provisions	1,261	16%	1,824	23%	1,372	18%
Write-back of provisions	725	9%	658	8%	754	10%
Taxes	920	12%	685	8%	700	9%
Result for the financial year	**2,861**	**36%**	**2,720**	**34%**	**2,882**	**38%**

The **interest-rate margin,** which decreases by 1%, combines two contrasting developments: the fall in interest revenues (-5%) and the rise in dividends from participating interests (24%).

The drop in interest revenues reflects the decrease in the money market rates, which continued in 2003 and which reduces above all the permanent equity invested in a liquid form. The growth in income from participating interests stems from the recent turnaround of the economic situation, which has also benefited to the foreign subsidiaries of Luxembourg banks.

(in millions of EUR)	2001	2002	2003[8]
Dividends received on participating interests	652	499	619

The reduction in **fee income** (-3%) is mainly due to the decrease in management fees. These fees, which are based on the assets under management, are decreasing owing to the depreciation of assets that followed the collapse of stock markets in 2002 and at the beginning of 2003. The downward trend of the fee income however reversed in the second quarter of 2003. Thanks to the performance of the stock markets, fee income thus recorded three consecutive quarters of growth. Furthermore, fees linked to financial operations for third parties remained unchanged.

Income from financial operations increased substantially. Their 82% rise is mainly due to the reversal of value adjustments on securities that are marked-to-market.

The 6% decrease in the banking income is mainly due to the item **other income,** whose 53% fall is attributable to the substantial extraordinary capital gains realised by Luxembourg banks in 2002.

Faced with a continuous decline in operating income, banks respond by cutting their expense budgets. This effort of cost-cutting resulted in a 3% decrease in **general costs** year-on-year. Administrative expenses however, falling by another 2%, seem to have bottomed-out. Staff costs decreased by 3% due to total employment that has dropped by 3% as well.[9]

[7+8] *Provisional figures for the year ending 31.12.2003.*

[9] *See also Chapter II, point 1.4. relating to developments in banking sector employment.*

Despite the relative control of costs, gross income drops by 8%. The cost/income ratio increases to 45%, its average value over the last five years. This ratio compares favourably with the norm that large bank groups set as a target.

The banks decreased their **net provisioning** by 47%. This reduction has to be seen in the light of the spectacular strengthening (+118%) of this item in 2002. The reversal of the economic situation confirmed in the second half of 2003 and allowed the banks to reverse the provisions created as a precaution in 2002 and to reduce their new provisioning in 2003. The overall level of provisions remains relatively high.

Finally, **taxes** increase by 2%, while they had fallen by 26% in 2002 due to weak operational results. The increase in gross results had only been achieved at that time thanks to extraordinary results (capital gains) benefiting from a tax exemption.

Structural ratios

	2001	2002	2003
Cost/income ratio	45.6%	43.3%	44.6%
Profit before taxes / average assets	0.55%	0.49%	0.54%
Profit before taxes / risk-weighted assets	22.4%	21.3%	23.5%
Profit before taxes / tier-1 capital	17.5%	14.4%	14.4%
Interest margin / banking income	55.2%	51.4%	53.8%
Income excluding interest / banking income	44.8%	48.6%	46.2%
Interest margin / average assets	0.64%	0.60%	0.62%
Creation of provisions for loans and advances to customers[10]	0.95%	1.01%	0.91%
Creation of provisions for affiliated undertakings[11]	1.2%	11.8%	7.2%
Creation of provisions for participations[12]	3.2%	11.7%	18.4%

The economic recovery is also reflected by the structural ratios in the form of an upturn of profitability indicators and a decrease in provision ratios. In this context, it has to be noted that the substantial increase in provisioning for participations (as a percentage of the gross amount of participations) is due to the withdrawal of a Luxembourg bank abroad. The growth is therefore not attributable to net provisioning, the latter having decreased by 20% as compared to 2002.

Movement in certain indicators of profit and loss account by employee

(in millions of EUR)	2001	2002	2003
Banking income / employee	0.333	0.346	0.337
Staff costs / employee	0.074	0.078	0.078

With a banking income decreasing more rapidly than total employment, banking income by employee falls by EUR 9,397 to reach EUR 336,558 at the end of 2003. However, staff costs per employee remain stable at EUR 78,000.

[10] *As a % of gross amount.*
[11] *As a % of gross amount.*
[12] *As a % of gross amount.*

1.7. Off-balance sheet items and financial derivatives

Banks in the Luxembourg financial centre used derivatives totalling EUR 737.2 billion in 2003 against EUR 692.4 billion in 2002, representing an increase of 6.5%. The use of financial derivatives thus slightly grew compared to 2002. The ratio between the volume of derivatives and the balance sheet total reached 112.4% against 104.5% in 2002.

The strongest increase is recorded for options, which represent a volume of EUR 37.1 billion in 2003 against EUR 28.1 billion in 2002, i.e. an increase of 31.9%. This growth mainly concerns options traded on regulated markets and have thus affected the total volume of instruments traded on a regulated market: EUR 30.5 billion in 2003 against EUR 20.5 billion in 2002, representing an increase of 49%.

Options, generally linked to the issuance of covered instruments, stem from a small number of specialised credit institutions.

Instruments traded over the counter still remain the most widely used products (95.9% of the total in 2003 against 97% in 2002), with a volume amounting to EUR 706.7 billion against EUR 671.9 billion in 2002.

The volume of interest rate swaps, mainly used within the scope of the asset-liability management, grew a further 4.7% (EUR 662.1 billion in 2003 against EUR 632.3 billion in 2002). The interest rate swap thus remained the most significant derivative in terms of volume.

Use of financial derivatives by credit institutions

	2002		2003[13]	
	in billions of EUR	as a % of total balance sheet	in billions of EUR	as a % of total balance sheet
Interest rate swaps	632.3	95.4%	662.1	101.0%
Future or forward rate agreements	23.2	3.5%	27.1	4.1%
of which: over the counter	*21.4*	*3.2%*	*24.8*	*3.8%*
of which: regulated market	*1.8*	*0.3%*	*2.3*	*0.4%*
Futures (currencies, interest rates, other rates)	8.8	1.3%	10.8	1.7%
Options (currencies, interest rates, other rates)	28.1	4.2%	37.1	5.7%
of which: over the counter	*18.2*	*2.8%*	*19.7*	*3.0%*
of which: regulated market	*9.9*	*1.5%*	*17.4*	*2.6%*

During 2003, the CSSF refined the reporting of third-party assets held by banks[14]. While this category previously comprised all the securities deposits of the professional and non-professional customers, this amount is now broken down into the following categories:

- assets deposited by UCIs;
- assets deposited by clearing or settlement institutions;
- assets deposited by other professionals intervening in the financial markets;
- other deposited assets.

The CSSF has not published the amount of securities deposits before 2003, as this figure was difficult to interpret. Indeed, the technical functioning of the securities deposits in the banking system implies that the same securities can be deposited and sub-deposited with several professionals, entailing that the same securities are counted twice or even more times, which can lead to wrong interpretations of the total amount of securities deposits.

[13] *Provisional figures as at 31.12.2003.*

[14] *For credit institutions under Luxembourg law and branches originating from third countries; branches originating from a Member State of the European Union are subject to a simplified reporting.*

This risk is however diminished, but not totally eliminated for the deposits of only the non-bank customers, UCIs and clearing or settlement establishments, so that the CSSF considered that these amounts can be published.

(in billions of EUR)	2003
Assets deposited by UCIs	895.4
Assets deposited by clearing or settlement establishments	275.9
Other deposited assets	338.1

1.8. Developments in own funds and in the solvency ratio

1.8.1. Number of banks required to meet a solvency ratio

As at 31 December 2003, the number of banks required to meet a non-consolidated solvency ratio stood at 120, 119 of which were under Luxembourg law and one branch of non-EU origin. Among these banks, 95 carry out limited trading activities, and are therefore authorised to calculate a simplified ratio. Trading activities in the true sense remain confined to a limited number of banks.

Number of banks required to meet a solvency ratio	Integrated ratio		Simplified ratio		Total	
	2002	2003	2002	2003	2002	2003
Non-consolidated	24	25	99	95	123	120
Consolidated	15	14	16	14	31	28[15]

1.8.2. Developments in the solvency ratio

The figures below are based on consolidated figures for banks required to meet a consolidated solvency ratio.

At the end of 2003, the capital adequacy ratio reached a new record level, benefiting both from the increase in eligible own funds and the decrease in total capital requirements. The solvency ratio itself lies at 16.5%, easily exceeding the minimum threshold of 8% prescribed by current prudential regulations. Taking into account only core equity capital (Tier 1), the aggregate ratio for the Luxembourg financial market rose from 10.6% as at 31 December 2002 to a provisional figure of 12.7% at year-end 2003.

Lower activity in lending operations during 2003 resulted in a decrease in capital requirements for credit risk (-4.5%). Lending operations still make up the bulk of capital requirements. Capital requirements for risks linked to the banks' trading portfolios, negligible in terms of volume, decreased substantially as compared to 2002 (-10.2%). Capital requirements for foreign exchange risks remain marginal, confirming the downward trend that started in 2000.

Eligible own funds continue their positive development of the previous years. Thus, core capital, which represents 78% of total eligible own funds, rose by 5.5% due to the rise in the items "Paid-up capital" and "Share premium accounts, reserves and profits brought forward". Additional own funds (after capping) confirm their downward trend of the previous years and record a provisional volume of EUR 7,170 million as at 31 December 2003, i.e. -2.4% as compared to the previous year. The use of super additional own funds, as in 2002, needs also to be noted. Finally, participations decreased substantially (-67.4%). This fall can be mainly explained by a refocusing on non-strategic participations in other credit and financial institutions by certain banks of the financial centre. The impact on the solvency ratio denominator is significant as the participations concerned are to be fully deducted from eligible own funds.

[15] *Banks, the participating interests of which are deducted from own funds on an individual basis do not need to calculate a consolidated ratio.*

(in millions of EUR)

Numerator	2002 consolidated	2003 consolidated (provisional)
Original own funds before deductions	***24,748***	***25,750***
Paid-up capital	6,999	7,794
Silent participation	2,595	2,591
Share premium account, reserves and profits brought forward	12,277	12,887
Funds for general banking risks	2,036	1,824
Profits for the financial year	242	292
Specific consolidation items	598	361
Items to be deducted from original own funds	***-1,102***	***-796***
Own shares	-10	-1
Intangible assets	-90	-94
Losses brought forward and loss for the financial year	-188	-59
Specific consolidation items	-814	-642
ORIGINAL OWN FUNDS (TIER 1)	**23,645**	**24,954**
Additional own funds before capping	***7,387***	***7,227***
Upper TIER 2	***3,261***	***3,039***
Of which: cumulative preference shares with no fixed maturity	22	22
Of which: subordinated upper TIER 2 debt instruments	2,522	2,215
Lower TIER 2	***4,126***	***4,188***
Lower TIER 2 subordinated debt instruments and cumulative preference shares with fixed maturity	4,126	4,188
ADDITIONAL OWN FUNDS AFTER CAPPING (TIER 2)	**7,348**	**7,170**
Super additional own funds before capping	***121***	***115***
SUPER ADDITIONAL OWN FUNDS AFTER CAPPING (TIER 3)	**47**	**38**
OWN FUNDS BEFORE DEDUCTIONS (T1+T2+T3)	**31,041**	**32,162**
ITEMS TO BE DEDUCTED FROM OWN FUNDS	**2,427**	**792**
Items of share capital in other credit and financial institutions in which the bank owns interests exceeding 10% of their share capital	707	544
Items of share capital in other credit and financial institutions in which the bank owns interests less or equal to 10% of their share capital	1,720	248
ELIGIBLE OWN FUNDS	**28,614**	**31,370**

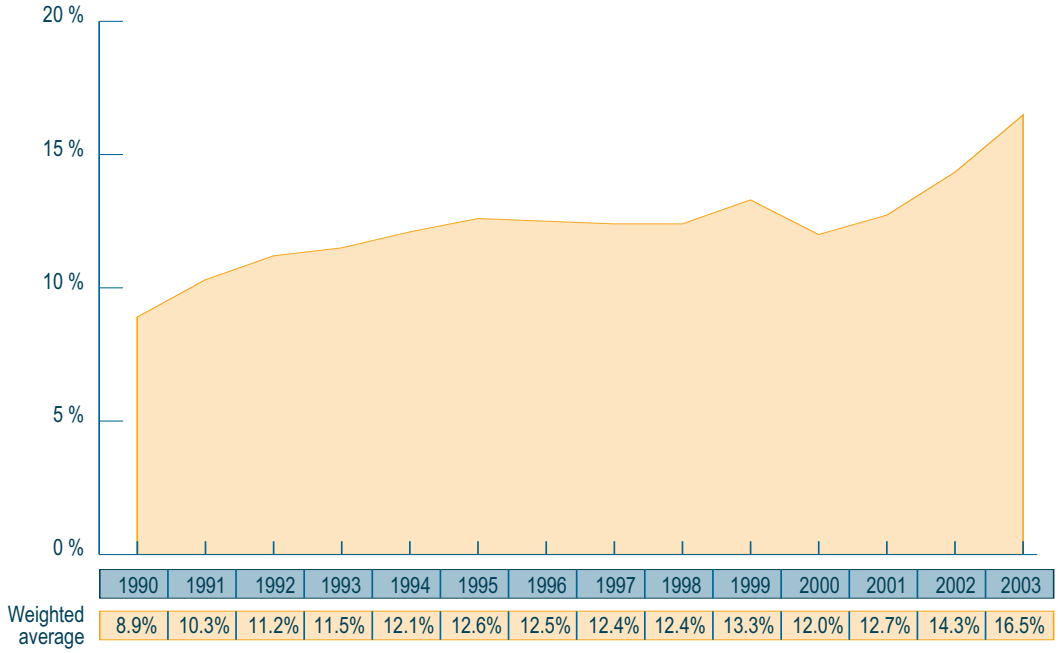
Denominator	2002	2003
TOTAL CAPITAL ADEQUACY REQUIREMENT	**15,962**	**15,221**
To cover credit risk	15,625	14,928
To cover foreign exchange risk	76	59
To cover trading risk	261	234

Ratio	2002	2003
SOLVENCY RATIO (base 8%)[16]	**14.3%**	**16.5%**
SOLVENCY RATIO (base 100%)	**179.3%**	**206.1%**
TIER 1 SOLVENCY RATIO (base 8%)	**10.6%**	**12.7%**

[16] *Eligible own funds/(total capital adequacy requirement * 12.5).*

The graph below shows the development of the solvency ratio (base 8%) since 1990. The weighted average is the ratio between total eligible own funds in the financial centre and total weighted risks. This average takes into account all credit institutions according to their volume of business.

Developments in the solvency ratio (base 8%) since 1990



	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003
Weighted average	8.9%	10.3%	11.2%	11.5%	12.1%	12.6%	12.5%	12.4%	12.4%	13.3%	12.0%	12.7%	14.3%	16.5%

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

In non-aggregate terms, the high solvency ratio in the financial centre is reflected by a rather low number of banks whose ratio is situated within the medium capitalisation bands, i.e. below 11%. For instance, as at 31 December 2003, the percentage of banks with a solvency ratio below 10% stands at 6.7%. Conversely, more than two thirds of credit institutions of the financial centre record a solvency ratio exceeding 15%.

Distribution Ratio	Number of banks 2002	2003	as % of total 2003
<8%	0	0	0.0%
8%-9%	3	2	1.7%
9%-10%	3	6	5.0%
10%-11%	4	8	6.7%
11%-12%	9	7	5.9%
12%-13%	10	3	2.5%
13%-14%	6	7	5.9%
14%-15%	5	5	4.2%
15%-20%	24	29	24.4%
>20%	59	53	44.5%
Total	**123**	**120**	**100.0%**

1.9. International expansion of Luxembourg banks

The year 2003 was characterised by an international expansion that has been clearly slowing down compared to the previous years; certain activities abroad have even been abandoned.

Thus, certain subsidiaries of German banks closed their Irish presences. On the other hand, significant provisions had to be made on subsidiaries acquired at high prices before the stock market crisis in 2000.

As shown in the table below, external acquisitions are only few in numbers in 2003. Groups originating from Switzerland however continue to entrust their Luxembourg subsidiary with the mission to strengthen their presence within the European Union. Finally, restructurings within the groups sometimes lead the banks to increase their participating interests in other subsidiaries.

Overall, the international expansion of Luxembourg banks reveals mixed trends and the profitability of the companies acquired remains to be confirmed.

These reasons led the CSSF to consider the applications for approval more prudently. The CSSF pays particular attention to the fact that acquisitions should be made within a well-defined strategy taking into account the factor of profitability. Pure growth strategies should be avoided.

Creations and acquisitions in 2003 by Luxembourg banks of subsidiaries and branches abroad

Name of bank	Entity formed or acquired
Kredietbank Luxembourgeoise S.A.	acquisition of Theodoor Gilissen Bankiers N.V., Amsterdam
Société Générale Bank & Trust	acquisition of a majority participation in CBG Compagnie Bancaire Genève S.A.
Banque Privée Edmond de Rothschild Europe	opening of a branch in Brussels
UBS (Luxembourg) S.A.	opening of a branch in Vienna
Pictet & Cie (Europe) S.A.	opening of a branch in Madrid
Dexia Banque Internationale à Luxembourg	aquisition of 51% of Dexia Fund Services Italia in Milan
Dexia Banque Internationale à Luxembourg	increase of the participation to 100% in Dexia Securities NV in Amsterdam

Branches established in the EU / EEA as at 31 December 2003

Country of origin	Luxembourg branches established in the EU / EEA	Branches of EU / EEA banks established in Luxembourg
Germany	1	20
Austria	1	-
Belgium	2	1
Denmark	-	-
Spain	3	-
Finland	-	1
France	-	6
Greece	-	-
Ireland	3	-
Iceland	-	2
Italy	-	4
Liechtenstein	-	-
Norway	-	-
Netherlands	-	-
Portugal	2	2
United Kingdom	4	4
Sweden	1	2
Total	**17**	**42**

Freedom to provide services in the EU / EEA as at 31 December 2003

Country	Luxembourg banks providing services in the EU / EEA	EU / EEA banks providing services in Luxembourg
Germany	41	28
Austria	22	6
Belgium	48	17
Denmark	25	7
Spain	34	4
Finland	19	3
France	49	48
Greece	21	-
Ireland	19	27
Iceland	3	-
Italy	38	2
Liechtenstein	1	1
Norway	8	3
Netherlands	39	24
Portugal	25	6
United Kingdom	33	40
Sweden	19	1
Total of notifications	**444**	**217**
Total number of banks concerned	**67**	**217**

1.10. Banks issuing mortgage bonds

The banks issuing mortgage bonds continued their positive development during 2003. Indeed, as at 31 December 2003, the balance sheet total of the three banks issuing mortgage bonds totalled EUR 26.841 billion and the total volume of public sector mortgage bonds issued by these three banks reached EUR 17.725 billion, compared with EUR 12.99 billion at the close of the financial year 2002.

Issues of mortgage bonds are guaranteed by ordinary cover assets and by substitute cover assets. As at 31 December 2003, cover assets totalled EUR 19.2 billion, meaning that the mortgage bonds in circulation benefit from total over-collateralisation (nominal value) of EUR 1.475 billion, i.e. 8.3% of total volume. The ordinary cover assets of municipal bonds for the three banks in question break down as follows:

- claims on or guarantees from public organisations: EUR 5.11 billion;
- bonds issued by public organisations: EUR 10.585 billion;
- municipal bonds of other issuers: EUR 799 million;
- derivative transactions: EUR 1.142 billion.

Besides these ordinary cover assets, the banks used substitute cover assets amounting to EUR 1.563 billion as at 31 December 2003.

Due to the faultless quality of investments of specialised banks and the scale of over-collateralisation in relation to the mortgage bonds issued, public sector mortgage bonds continue to receive an AAA rating from the rating agency Standard & Poor's.

The CSSF strengthened its prudential supervision of the banks issuing mortgage bonds during 2003. In June 2003, the CSSF introduced a new requirement within the scope of special monthly reporting to be made by the banks issuing mortgage bonds: in order to take account of the interest rate risk and the real value of derivative products, the banks are required to report on a monthly basis, besides the amount of nominal over-collateralisation, the amount of over-collateralisation established according to the current net value. As at 31 December 2003, the over-collateralisation of cover assets compared to mortgage bonds issues, established according to the current net value, reached EUR 2.119 billion for the three banks.

Furthermore, following the publication of circular CSSF 03/95, aiming at clarifying the missions and obligations conferred upon the special auditor by law, the reports were drawn up according to these new requirements.

Although the law of 21 November 1997 allows the banks issuing mortgage bonds to issue municipal bonds as well as mortgage bonds, the Luxembourg banks continued to limit their main activities in 2003 to municipal bonds covered by sovereign debtors. However, the first mortgage bonds are expected to be issued in 2004.

1.11. Exposure to high-risk sectors

The twenty most important credit institutions of the financial centre have been requested by circular letter of 29 November 2001 to provide information concerning their exposures to certain sectors more particularly hit by the unfavourable economic environment. Thus, they report, on a quarterly basis, their exposures towards the sectors of telecommunications, media and technology, transport, aviation, tourism and leisure industry, as well as the insurance sector. These twenty institutions cover 63.6% of the total balance sheet of the financial centre in 2003.

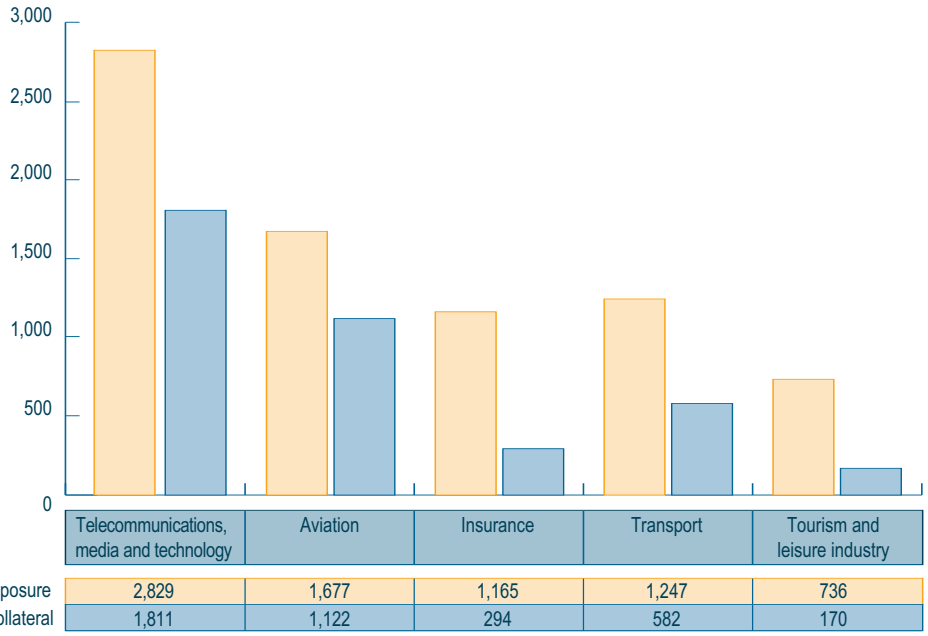
In 2003, the CSSF closely monitored the development of the reported risk exposures. The following table summarises the recent development of loans, net of specific provisions, drawn by the different sectors. Overall, the risk exposures taken into consideration represent 1.2% of the total balance sheet of the banks of the financial centre at the end of 2003.

(in millions of EUR)	Exposure at the end of 2002	Exposure at the end of 2003	Variation in %
Telecommunications, media and technology	3,855	2,829	-27%
Aviation	2,107	1,677	-20%
Insurance	1,392	1,165	-16%
Transport	1,071	1,247	+16%
Tourism and leisure industry	734	736	0%

The global risk exposure recorded a substantial decrease of 16.4% during 2003. Exposure towards the telecommunications, media and technology sector registered the most significant decrease, i.e. 26.6% over the year. This development has to be put into the context of a 7.8% fall of loans and advances to customers and can be explained by the adoption by banks of a more restrictive credit policy. The banks thus adopted a more prudent approach for their positions towards certain high-risk sectors.

The following graph shows the degree of credit risk mitigation of the exposures. Overall, the exposures are covered up to 50% through guarantees/collateral. The coverage ratio is highest for the aviation sector (66.9%) and for the telecommunications, media and technology sector (64%).

Risk positions at the end of 2003: exposure and guarantee/collateral – *in millions of EUR*



The CSSF applies strict eligibility requirements as regards guarantees/collateral. Only guarantees and collateral of outstanding quality and liquidity are taken into account for internal analysis. In certain cases, haircuts that take into account the non-covered residual risk are deducted from the gross amount of guarantees.

The table below sets out own funds of banks with exposures to high-risk sectors. It also gives a fair outline of the coverage of risk exposures considered by own funds.

Sector	Own funds of banks with risk exposures (in millions of EUR)	Ratio between exposure and own funds	
		Highest ratio for systemic banks	Ratio for the three most exposed banks
Telecommunications, media and technology	23,244	21%(*)	16%(*)
Aviation	22,634	33%	23%
Insurance	21,194	7%	7%
Transport	21,844	19%	18%
Tourism and leisure industry	21,018	10%	9%

(*) highest ratio among those calculated separately for the telecommunications, media and technology sectors.

The first ratio analysed by the CSSF relates the risk-sector exposure to the own funds of the individual banks. For each sector, the table shows the highest ratio observed among the systemic banks. The second ratio calculates the same percentage as regards the three banks having the highest risk-sector exposures. Neither of these ratios indicates an abnormal concentration. The risk concentration of banks is highest for the aviation sector. However, the exposure towards this sector decreased substantially from the third quarter 2001.

The decrease in ratios relating the sector exposure to the own funds of the banks has been particularly marked in 2003 due to the joint impact of a policy consisting in reducing risk exposures and a strengthening of the banks' own funds.

Capital buffers constituted mainly by lumpsum provisions allow most of the banks to absorb possible losses incurred in high-risk sectors without their own funds being directly affected.

Several stress tests allowed the CSSF to better differentiate the quality of guarantees and the counterparty risk. Overall, these tests did not reveal a particularly preoccupying situation as regards the risk-sector exposures in 2003. The decrease in net exposures and the strengthening of own funds more than offset the increased exposures to certain sectors that the CSSF closely monitors.

Finally, the CSSF carried out punctual analyses of other high-risk sectors in 2002/2003. Thus, it took particular interest in the exposures of Luxembourg banks to the real estate sector. A study was carried out concerning the institutions of the financial centre that are particularly active in the financing of residential and commercial real estate. The CSSF examined the exposures of the banks to the Luxembourg real estate sector, differentiating on the one hand between the loans granted to private persons for the financing of their private real estate and, on the other hand, the loans granted to promoters to finance apartment blocks and loans granted to finance office buildings. The banks were also requested to provide their own appraisal of the exposures to the real estate sector by differentiating between these three types of financing.

The responses to the CSSF's survey show that the quality of the loans granted to private persons and to promoters of apartment blocks remains high in general. New applications for loans are accepted according to strict criteria concerning the quality of the borrower and the part of own financing. The quality of the portfolio of loans granted for the financing of office buildings (9.7% of the exposures of the banks participating in the survey on the Luxembourg real-estate sector) is overall satisfactory. Speculative commitments (rate of pre-sale or pre-leasing below 70%) are a minority part. The banks closely follow the development of these loans of which some encounter problems. The majority of the banks have adopted a more prudent, even restrictive approach, to accept new applications for loans concerning the financing of office buildings.

2. Developments in the regulatory framework

2.1. Circular CSSF 03/95 on the minimum requirements regarding management and control of the pledge register, cover assets and the limit of mortgage bonds in circulation

The circular, which is aimed at banks issuing mortgage bonds and at their special auditor, specifies a certain number of provisions of article 12-7 of the law of 5 April 1993 on the financial sector as amended relating to the supervision of cover assets recorded in the pledge register.

Firstly, it defines the requirement as regards the professional qualifications of the auditors in order carry out the mandate of special auditor of a bank issuing mortgage bonds.

Secondly, the circular provides further explanations on the monitoring of cover assets. Indeed, the special auditor must ensure that the cover assets are duly constituted and registered in the pledge register, that they continue to exist and reach the amount provided for by law. The circular thus specifies the way the bank must maintain and manage the pledge register in order to allow the special auditor to carry out his duties.

Moreover, the circular sets out the various limits imposed on the banks issuing mortgage bonds, whose compliance must be supervised by the special auditor. To this end, it lists the various ratios that banks issuing mortgage bonds must respect within the scope of the legal requirement, which provides that the total nominal amount of mortgage bonds in circulation must at any time be fully covered by cover assets.

Finally, the circular lays down the minimum requirements regarding the contents of the special auditor's report that must be submitted to the CSSF on a yearly basis.

2.2. Circular CSSF 03/100 concerning the publication on the Internet of CSSF instructions:
- *Recueil des instructions aux banques* of the CSSF
- Schedule of Conditions for the technical implementation of the CSSF reporting requirements – SOC/CSSF

In its circular of 1 April 2003, the CSSF announces the publication of the *Recueil des instructions aux banques* and of the Schedule of Conditions for the technical implementation of the CSSF reporting requirements - SOC/CSSF on its website (direct link: www.cssf.lu/fr/report/rperiod/html).

The CSSF *Recueil* contains the prudential and accounting instructions for the periodic reporting of the banks to the CSSF, as well as instructions specifying the form and content of the accounts intended for publication. The Schedule of Conditions for the technical implementation of the CSSF reporting requirements – SOC/CSSF contains the technical instructions for the communication in electronic form of the periodic reporting of banks and UCIs.

The CSSF *Recueil* and the SOC are published exclusively on the Internet in PDF format and can be freely accessed. Any changes thereto will be notified to the entities supervised by the CSSF through circulars or circular letters as in the past.

The CSSF website contains only the instructions relating to the prudential tables (tables B, E and O). Technical instructions relating to the statistical tables (tables S), of which the Luxembourg Central Bank (BCL) is in charge, are available on the BCL website (www.bcl.lu).

The new version of the *Recueil*, as published on the website, is a revised and updated version of the *Recueil* published by the IML in 1992 when the new accounting scheme was introduced. However, it does not contain any fundamental change as compared to last IML version. Thus, several changes concern the presentation, others concern the substance and a set of changes take into account the instructions or specifications communicated to the banks since 1992 by means of circulars, circular letters or on an *ad-hoc* basis. The instructions concerning the information to be published ("VISA" procedure) as communicated in the circular letters the CSSF published annually since the introduction of the new accounting scheme in 1992 have been integrated into Part V "Information for publication" of the *Recueil*. Details of all these changes are available for consultation on the CSSF website in the marked-up version.

The new version of the SOC only contains minor changes to the contents as compared to the former version dated November 1997; these changes are marked up in the text. All the changes are contained in a separate document called "MAJSOC" and published together with the SOC.

2.3. The implementation of the IAS[17] regulations in Luxembourg

Before taking a decision on the implementation of the IAS regulations in Luxembourg, the CSSF launched a survey with the banks on 13 December 2002. This survey revealed that the vast majority of banks of the financial centre is in favour of applying the IAS for published accounts (annual and consolidated) as well as for the prudential reporting. Concerns have however been voiced as regards the tax effect.

In order to take concrete measures, the CSSF actively participates in a working group under the aegis of the Ministry of Justice, gathering professional organisations (banks, insurance undertakings, trade, industry), as well as public organisations (authorities for prudential, tax, statistical matters). The purpose of this working group is to define a coordinated approach as regards the introduction of IAS in the financial centre and to achieve the adaptation of the tax and company law.

As regards the publication of consolidated accounts, the non-listed banks have the possibility to apply the IAS standard as from its transposition into national law, while the listed banks will have to publish their consolidated accounts as of 2005. The banks of which only the bonds are listed however have the right to publish their consolidated accounts according to the IAS standards solely as of 2007. Banks already have the option to publish their consolidated accounts according to IAS standards on the condition that they append a conciliation with the accounting rules currently in force.

The CSSF considers giving the banks the option to publish both their consolidated and annual accounts under IAS standards insomuch as a solution is found regarding taxes and maintenance of capital. The application to annual accounts may be admitted as from the close of 2007.

[17] *International Accounting Standards (IAS) or International Financial Reporting Standards (IFRS) according to the denomination of the new international accounting standards adopted by the International Accounting Standards Board (IASB).*

The application of the IAS standards to the published accounts requires an amendment of the law of 17 June 1992 on the banks accounts, which will also address the transposition of the Directives "Fair Value" and "Modernisation of accounting Directives".

As regards prudential reporting, the CSSF considers introducing an IAS reporting as from 2007 on an individual as well as consolidated basis. The reporting will cover all the IAS requirements by taking also into account the prudential concerns specific to the CSSF.

3. Prudential supervisory practice

3.1. Objectives of supervisory practice

Supervision of banks aims at the following:

- ensuring the security of the public's savings by monitoring the solvency and prudent management of individual banks;
- ensuring financial stability and proper functioning of the banking system as a whole;
- protecting the reputation of the financial sector by censuring ethically unacceptable conduct.

In order to fulfil these objectives of public interest, the CSSF monitors application by credit institutions of the laws and regulations relating to the financial sector.

3.2. Monitoring of quantitative standards

Quantitative standards, designed to ensure financial stability and risk spreading by credit institutions, relate to:

- evidence of minimum equity capital;
- a maximum ratio between own funds on the one hand and risk exposure on the other;
- limitation of the risk concentration on a single debtor or a group of associated debtors;
- liquidity ratio;
- limitation of qualified participating interests.

In 2003, the CSSF did not have to intervene in any instances of violations of capital ratio. It intervened on four occasions with regard to non-compliance with liquidity ratios and on thirteen occasions with regard to exceeded limits on large exposures. These breaches often resulted from difficulties in interpreting regulations and could be rapidly regularised.

3.3. Monitoring of qualitative standards

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

- analytical reports prepared by external auditors;
- management letters and similar reports prepared by external auditors;
- on-site inspections undertaken by CSSF agents;
- reports prepared by internal auditors of the banks.

These reports are processed according to a methodology described in the CSSF's internal procedures. The reaction of the CSSF 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 of managers or activities.

During 2003, the CSSF sent 132 (204 in 2002) deficiency letters to banks based on shortcomings in terms of organisation.

The most frequent issues that arose were the following:

- procedure manual (degree of precision, regular updates, etc.);
- equal powers of the approved managers;
- adequate segregation of duties;
- unsatisfactory or ill-tested business continuity plan;
- hierarchical position of the internal audit;
- supervisory system of margin lending: frequency of assessments, consideration of all the exposures (including forward transactions and assimilated), deficiencies in the legal records, procedure to start liquidation of cover assets;
- IT security, control of access rights;
- process of sending and delivering mail;
- cash transactions not exclusively carried out by the cashier;
- insufficient supervision of the internal and dormant accounts;
- weaknesses relating to rules of conduct as laid down in circular CSSF 2000/15 and notably absence of a written warning on the risks concerning derivatives.

3.4. Analytical report

The analytical report prepared by the external auditor is one of the most important instruments to assess the quality of the organisation and the exposure to different risks. The CSSF requires the preparation of an analytical report on a yearly basis for each Luxembourg credit institution as well as for each Luxembourg branch 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, carrying out an activity of the financial sector.

Analytical reports were made compulsory in 1989 through a circular, which was reformed in 2001 (circular CSSF 01/27) in order to take account of the development of the regulatory and prudential framework.

In 2003, the CSSF analysed 253 analytical reports, 27 of which were consolidated analytical reports and 81 were analytical reports of subsidiaries.

3.5. Co-operation with external auditors

Article 54 of the law of 5 April 1993 on the financial sector as amended governs the relationship between the CSSF and the external auditors. This article confers upon the CSSF the power to establish the regulations relating to the audit mandate and the content of the audit report. The professional supervised shall communicate all the reports issued by the external auditor within the course of the audit of annual accounts to the CSSF.

Furthermore, the external auditors are also required to inform the CSSF immediately of any serious facts, defined more specifically under article 54(3) of the aforementioned law, which have come to their attention in the course of their duties.

The supervision of the CSSF is largely based on the work of the external auditors and their reports. Since 2002, the CSSF holds annual meetings with the main audit firms in order to exchange views on specific issues encountered. Discussions also concerned the quality of the reports and the results of the inspections.

Besides these more general meetings, the CSSF held separate meetings with two auditors to discuss specific issues encountered with two banks.

3.6. On-site inspections

The CSSF intensified its efforts as regards on-site inspections even more in 2003. Thus, 62 inspections were carried out in 2003, against 47 in 2002.

The programme of inspections to be carried out during the year is set up at the beginning of the year and is based on the assessment of the risk areas of the various credit institutions. The objective thereof is on the one hand to be present at the important credit institutions and on the other hand to supervise the other institutions following a schedule covering several years.

Inspections carried out by CSSF agents generally follow standard inspection procedures, in the form of discussions with the persons responsible, assessment of procedures and the verification of files and systems.

During the year under review, the CSSF focused especially on compliance with the rules as regards money laundering. Twenty inspections concerned this subject (please refer to point 3.7. hereafter).

As the CSSF accompanies the banks' preparation for the implementation of the new regulations on own funds ("Basel II"), fifteen on-site visits concerned this subject (please refer also to Chapter X, point 2.1.1. regarding the new capital adequacy regime).

A substantial part of the on-site inspections consisted in specific investigations into particular issues and matters. In 2003, seventeen inspections concerned this category. The other inspections concerned various subjects such as market activity and lending activities.

3.7. Combating money laundering

In order to safeguard the reputation of the Luxembourg financial centre, the control of compliance with the anti-money laundering regulations is one of the CSSF's priorities and aims at ensuring that the Luxembourg financial sector applies first-rate know-your-customer standards, without taking account of commercial considerations. The International Monetary Fund regularly reviews the CSSF's action: the IMF detected no significant flaw and the CSSF endeavours to immediately implement the punctual recommendations of the IMF.

The CSSF uses the following instruments to supervise compliance with these rules: inspections carried out by CSSF agents, reports of external auditors and those prepared by internal auditors.

During the year under review, the CSSF sent 94 deficiency letters to the banks in relation with shortcomings concerning money laundering (93 in 2002). These letters, based on on-site inspections and external or internal audit reports, list the shortcomings identified and enquire about the corrective measures envisaged. In more serious cases, the CSSF requires that a detailed plan of action with time limits be set up.

In 2003, the CSSF carried out twenty missions to control compliance with anti-money laundering rules. The banks concerned were chosen according to volume and type of activity as well as to the origin of their clients. Overall results were positive as far as identification of customers and of the funds' origin are concerned. Furthermore, a high level of awareness of the persons responsible was noted.

The following weaknesses led the CSSF to intervene with the banks:

- The banks do often not have enough information on the professional background of their clients, the funds' origin and the reason for starting the relationship. The CSSF insists that the banks collect sufficient information on these points, where applicable with corroborating documents. Even if the regularisation actions required by the CSSF sometimes encountered

public incomprehension in Luxembourg, the CSSF considers that the Luxembourg public must get used to be questioned by banks on the funds' origin, the activities carried out, the justification of certain transactions through corroborating documents, etc.

- The banks must gain a better understanding of the transactions carried out by their clients in order to detect those that do not correspond to the profiles defined when entering into the relationship.

- As regards the supervision of operations in order to detect any suspicious transactions, it becomes more and more essential that computerised processes be set up.

- The name of the originator must be indicated on the transfer orders.

- Where technical aspects relating to client identification are delegated to professional intermediaries, this co-operation must be settled by a regularly updated contract. This co-operation, even if it involves other professionals subject to a prudential supervision, does not exempt the banks from their professional obligations as regards the identification of the funds' origin, the reason for entering a relationship and the type of transactions concerned.

- Where the banks rely on independent intermediaries, they must enquire about the reputation of the latter and ensure that they have the appropriate authorisation to carry out this type of activity.

- The CSSF reminded the banks that employees likely to apply anti-money laundering rules must get regular training in order to be brought up to date on the fast developing regulations.

The programme of inspections for 2004 provides for the continuation of inspections concerning compliance with anti-money laundering obligations.

The yearly analytical report prepared by external auditors must specifically cover compliance with legal requirements and the adequate application of internal procedures concerning the prevention of money laundering. The main deficiencies observed are about the same as those noted by the CSSF.

The Law requires that banks with branches or subsidiaries abroad ensure that these entities comply with Luxembourg professional obligations in addition to the standards of the host country. The CSSF verifies compliance with this requirement by means of analytical reports of external auditors to be prepared for each subsidiary carrying out an activity of the financial sector. Furthermore, the CSSF requires that the internal audit of the Luxembourg parent company periodically verify that subsidiaries and branches abroad comply with the group's directives on anti-money laundering. The results of these inspections must be included in the summary report, which has to be submitted to the CSSF on an annual basis.

The CSSF had to intervene on several occasions with respect to weaknesses as regards the fight against money laundering observed at subsidiaries and branches abroad. It has to be particularly stressed that the groups' managements must pay special attention to this matter and ensure that the groups' directives be uniformly applied by all the entities.

3.8. Management letters

Management letters drawn up by external auditors for the attention of the banks' management are an important source of information on the quality of the organisation of credit institutions. In these reports, the external auditors point out weaknesses they observed in the internal control system in the course of their assignment. During 2003, the CSSF analysed 111 management letters.

3.9. Meetings

The CSSF regularly conducts meetings with bank executives to discuss business and any problems. It also requires prompt notification by the banks if a serious problem arises.

In 2003, 220 meetings were held between CSSF representatives and bank executives.

3.10. Specific controls

According to article 54(2) of the law of 5 April 1993 on the financial sector as amended, the CSSF has the right to require an external auditor to conduct a specific audit in a given institution. As in previous years, the CSSF did not formally make use of this right, but invited some banks to appoint themselves an external auditor to audit a specific area. Five controls of this type took place in 2003.

3.11. Internal audit 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 each year. In 2003, the CSSF analysed 135 summary reports. It also requested 74 specific internal audit reports in order to obtain more detailed information on particular subjects.

3.12. Specific problems: fraud and malfunctioning

As in previous years, some banks were exposed to fraudulent activities of employees or malfunctioning of the organisation, which led to financial losses. The present section describes typical cases in order to enable banks to draw organisational lessons. These cases illustrate how compliance with certain essential organisational rules allows to prevent such situations, or at least makes them less likely to happen.

Organisation of the "discretionary management" function

The CSSF was confronted with a case of malfunctioning of the discretionary management function similar to those encountered in the previous years.

The problem stems from the fact that clients who are not officially under a discretionary management and who are therefore supposed to be at the origin of the transactions made on their accounts, start to let their manager, on a more or less tacit agreement, carry out the transactions decided by the latter. This situation can entail disputes in case of losses and the burden of proof is particularly difficult to establish as the following situations can arise:

- The manager has carried out transactions without the client being aware of it, simulating orders over the telephone; the bank must of course compensate the client.

- The manager effected transactions on his own initiative, but based on a tacit agreement with the client. As long as the transactions generate gains, the client does not contest them. As soon as losses are sustained, the client affirms not to be aware of these transactions.

- The client gave orders over the phone, but contested them afterwards.

A posteriori, it is difficult to establish how the contested transactions have been initiated. Hence the importance of an organisation that allows to provide evidence supporting the bank's legal position. The main elements of an adequate organisation are as follows:

- The systems to send mail must be infallible and imperative. As the general terms and conditions of the banks provide in general for a time frame of 30 days to dispute operations, it is essential that banks are able to establish the proof that the statements of account have been sent to the client. This is why clients should sign an acknowledgment upon receipt of the mail (from a person other than the manager) at the bank. Moreover, the mail should only be sent to the address as indicated initially and any change thereto should only be made by means of a written request by the client.

- The functions "discretionary management", "management advice" and "execution only" must be clearly separated. The managers should have no doubt whatsoever concerning the nature of the relationship with the clients. The legal documents and internal control system should be adapted to the various situations.

- A complete service of private banking, which can include discretionary management, hold mail accounts and similar services cannot in general be provided in each branch, but only in the centres guaranteeing that they dispose of the equipment allowing to carry out this service accordingly.

Finally, the CSSF insists that the banks lodge complaints against the employees who committed criminal offences.

3.13. Fit and proper

The CSSF noted that the scope of the fit and proper principle, pertaining to the professional standing and experience of the persons approved within a supervised entity, as well as the extent of the implications of the approved directorate's joint responsibility is not always perceived. The CSSF thus aims at reminding certain aspects of the nature and scope of these concepts.

Article 7 of the law of 5 April 1993 on the financial sector as amended requires that the members of the board of directors, management and the shareholders or persons with a significant influence over the conduct of business, provide proof of their professional standing, which shall be assessed on the basis of judicial records and any other evidence showing that the persons concerned have a good reputation and show irreproachable conduct.

Further to the criteria of professional standing, the members of management must meet the criteria of professional experience, i.e. they must fulfil indispensable requirements to assume in a professional manner the responsibility of the management of a financial undertaking, such as the fact that they have already carried out similar activities at a high level of responsibility and autonomy.

The criteria of professional standing and experience must not only be fulfilled at the time of the nomination, but also throughout the exercise of the function. Where incidents undermine the trust placed in a person, the CSSF can require his departure.

The professional standing can be called into question due to various situations such as serious non-compliance with regulations and legislation, such as those aimed at combating money laundering, or irregular professional behaviour.

The responsibility of the manager can also be called into question on account of the joint responsibility of the approved directorate. It should be borne in mind that in accordance with the Luxembourg regulations, the members of the directorate approved by the CSSF must have equal powers to determine the bank's goals and are thus responsible for all its activities, even

for those that have not been directly assigned to them according to the internal organisation chart of the bank. A member of management can thus be led to resign on account of a colleague's dealings. In particular, he can be held responsible for the fact of having tolerated or remained passive in the face of a situation where he should have stepped in and objected to, i.e. for facts in which he was not involved, but for which he is however responsible due to his position within the entity.

3.14. Supervision on a consolidated basis

As at 31 December 2003, 33 banks under Luxembourg Law[18] (against 31 in 2002), as well as one Luxembourg-incorporated finance company[19] (idem in 2002) were supervised by the CSSF on a consolidated basis.

The conditions governing submission to a consolidated supervision, the scope, content and methods of supervision on a consolidated basis are laid down in Section III, chapter 3 of the law of 5 April 1993 on the financial sector as amended. The rules in question implement Directive 92/30/EEC on the supervision of credit institutions on a consolidated basis. The practical application of the rules on supervision on a consolidated basis is explained in circular IML 96/125.

It has to be noted that the CSSF pays particular attention to the "group head" function set up at the Luxembourg establishment falling under its consolidated supervision. Thus, the CSSF sees more specifically to the way the Luxembourg parent company communicated its policies and strategies to its subsidiaries as well as to the controls set up at the Luxembourg parent company in order to monitor the organisation and activities of the subsidiaries, as well as their exposures.

The CSSF uses many means to supervise on a consolidated basis:

- The CSSF requires a periodic reporting reflecting the financial situation and the consolidated risks of a group subject to its consolidated supervision.

- Another source of information are the reports prepared by the external auditors. Circular CSSF 01/27 defining the mission of the external auditor requires that a consolidated long form report of a group subject to the consolidated supervision of the CSSF be drawn up. This consolidated report aims at providing the CSSF with an overview of the group's situation and at giving indications on the risk management and structures of the group.

- The CSSF requires for each important subsidiary an individual long form report.

- The CSSF requires that the scope of intervention of the internal audit of the Luxembourg parent company be extended to the subsidiaries in Luxembourg and abroad. By virtue of circular IML 98/143 on the 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. This report must mention the controls carried out within the subsidiaries and the results thereof.

[18] *ABN Amro Bank (Luxembourg) S.A., Banca Popolare di Verona e Novara (Luxembourg) S.A., Banque Delen Luxembourg, Banque de Luxembourg S.A., Banque Degroof Luxembourg S.A., Banque Générale du Luxembourg S.A., Banque Puilaetco (Luxembourg) S.A., Banque Safra-Luxembourg S.A., BNP Paribas Luxembourg, Commerzbank International S.A., Credem International (Lux), Crédit Agricole Indosuez Luxembourg, Crédit Agricole Investor Services Bank Luxembourg, Danske Bank International S.A., DekaBank Deutsche Girozentrale Luxembourg S.A., Deutsche Bank Luxembourg S.A., Dexia Banque Internationale à Luxembourg, Dresdner Bank Luxembourg S.A., DZ Bank International S.A., Fideuram Bank (Luxembourg) S.A., HSH Nordbank International S.A., IKB International, ING BHF-BANK International S.A., ING Luxembourg S.A., John Deere Bank S.A., Kredietbank S.A. Luxembourgeoise, Natexis Private Banking Luxembourg S.A., Norddeutsche Landesbank Luxembourg S.A., Nordea Bank S.A., Sanpaolo Bank S.A., Société Générale Bank & Trust, UBS (Luxembourg) S.A., West LB International S.A.*

[19] *Clearstream International*

- The information of the CSSF is supplemented by many 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 Luxembourg banks subject to consolidated supervision, information on any interventions 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 Luxembourg credit institution under consolidated supervision.

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.

3.15. International co-operation on matters of banking supervision

The CSSF has concluded memoranda of understanding with the banking supervisory authorities of most Member States of the European Economic Area[20] with a view to specify the terms of co-operation. These memoranda concern in particular the supervision of credit institutions involved in cross-border operations by way of the freedom to provide services or through the creation of branches.

Moreover, in accordance with the legal provisions in force, the CSSF co-operates and exchanges information on an informal basis with a number of its counterpart authorities.

In 2003, the CSSF held three bilateral meetings with various banking supervisory authorities in order to exchange prudential information on institutions under supervision having a presence in both countries.

Alongside the consultations required under European Directives, the CSSF informs the relevant authorities of all significant facts relating to supervision. In particular, it consults the relevant authorities regarding acquisitions of significant participating interests and restructurings of share ownership.

In 2000, the CSSF signed a memorandum of understanding with the Belgian and French authorities relating to supervision of the DEXIA Group. In 2001, a similar agreement, this time relating to supervision of the banking activities of the FORTIS Group, was signed between the CSSF and the Belgian and Dutch authorities.

Following the takeover of the Clearstream group by the Deutsche Boerse AG, the German and Luxembourg authorities signed a memorandum at the beginning of 2004 defining the modes of co-operation between both authorities as regards the supervision of the Clearstream group.

The authorities considered that the new structures of these groups, by introducing a decentralised organisation of operational management units and centres of competence, called for an adaptation of the prudential supervisory modalities to the activities of these groups. The key objective of such a co-operation between authorities is to ensure that all banking activities of these groups are adequately supervised. To this end, the authorities ensure in particular that the various sets of regulations are applied in a harmonised manner in order to avoid any unbalanced treatment within the groups.

[20] *Namely Germany, Belgium, Spain, Finland, France, Ireland, Italy, Norway, Netherlands, Portugal, United Kingdom and Sweden.*

SUPERVISION OF THE BANKING SECTOR

The co-operation between authorities is enacted on several levels:

- close consultation between the authorities in order to coordinate and align their prudential supervision;

- continuous and systematic exchange of information on any significant event likely to impact the group or its main constituent entities;

- regular consultation for the principal purpose of updating the list of points requiring the attention of the authorities within these groups, drafting of control plans and, finally, examining the appropriateness of on-site inspections to be carried out by the competent authority in close co-operation with the other relevant authorities.

Besides frequent exchanges of information between persons directly responsible of the supervised entities in each authority, the CSSF attended eleven formal meetings in 2003 within the framework of this co-operation.

The CSSF considers that this new form of co-operation substantially improves the effectiveness of supervision of cross-border banking groups and it is convinced that these can be supervised thoroughly by national authorities collaborating via memoranda of understanding so as to cover all dimensions of a group's activities. This underlines the belief of the CSSF that there is no need for centralised supervision of cross-border groups at EU level.

CHAPTER III

SUPERVISION OF UNDERTAKINGS FOR COLLECTIVE INVESTMENT

1. Developments in the UCIs sector in 2003
2. Newly created entities approved in 2003
3. Closed down entities in 2003
4. Developments regarding UCIs investing principally in other UCIs
5. Developments in the regulatory framework
6. Management companies
7. Prudential supervisory practice

1. Developments in the UCIs sector in 2003

1.1. Key trends

In 2003, the undertakings for collective investment (UCIs) sector saw a fairly significant growth in terms of net assets managed, while the number of UCIs in operation decreased. Indeed, the net assets managed amounted to EUR 953.3 billion at the end of the year against EUR 844.5 billion twelve months earlier (+12.9%). 1,870 UCIs were registered on the official list as at 31 December 2003 against 1,941 at the end of the previous year (-3.7%). On a yearly basis, this represents the first fall in the number of UCIs since the entry into force of the law of 30 March 1988 relating to UCIs as amended.

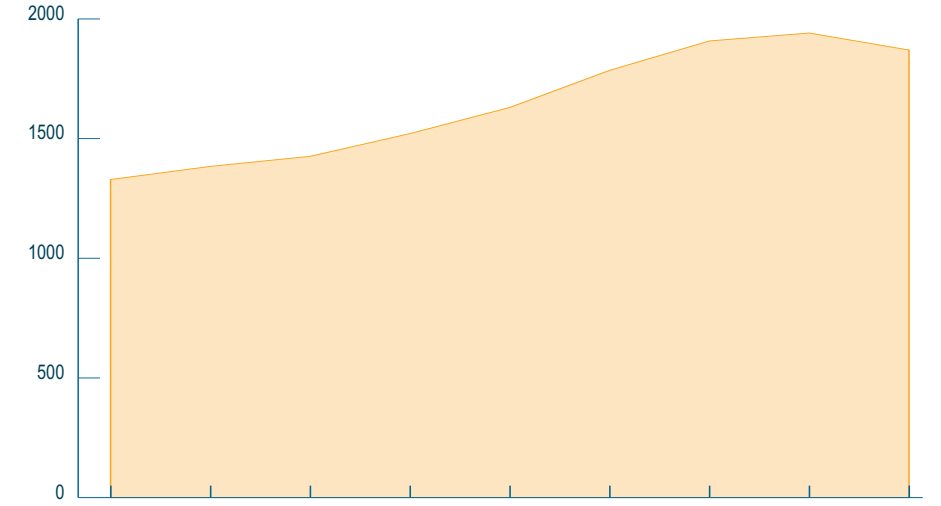
Development in the number and net assets of UCIs

in billions of EUR

Year	*Number of UCIs*	*Registrations*	*With-drawals*	*Net change*	*In %*	*Net assets*	*Net issues*	*Variation in net assets*	*In %*	*Average net assets by UCI*
1995	1,329	166	120	46	3.6	261.8	2.0	14.3	5.8	0.197
1996	1,384	182	127	55	4.1	308.6	22.5	46.8	17.9	0.223
1997	1,426	193	151	42	3.0	391.8	50.1	83.2	27.0	0.275
1998	1,521	234	139	95	6.7	486.8	84.1	95.0	24.2	0.320
1999	1,630	265	156	109	7.2	734.5	140.1	247.7	50.9	0.451
2000	1,785	278	123	155	9.5	874.6	168.1	140.1	19.1	0.490
2001	1,908	299	176	123	6.9	928.4	121.7	53.8	6.2	0.487
2002	1,941	222	189	33	1.7	844.5	57.3	-83.9	-9.0	0.435
2003	1,870	175	246	-71	-3.7	953.3	82.6	108.8	12.9	0.510

While the year 2002 was already marked by a large number of mergers and liquidations of UCIs and compartments, this trend became even more noticeable in 2003 with the implementation of the law of 20 December 2002 as amended, leading many promoters to restructure and reorganise their various products. Thus, the number of UCIs registered on the official list decreased by 71 entities. The number of UCIs newly registered on the official list in 2003 reached only 175 entities and is thus continuously falling since the record year 2001 with 299 new registrations. Moreover, the number of withdrawals continued to rise, reaching a record level of 246.

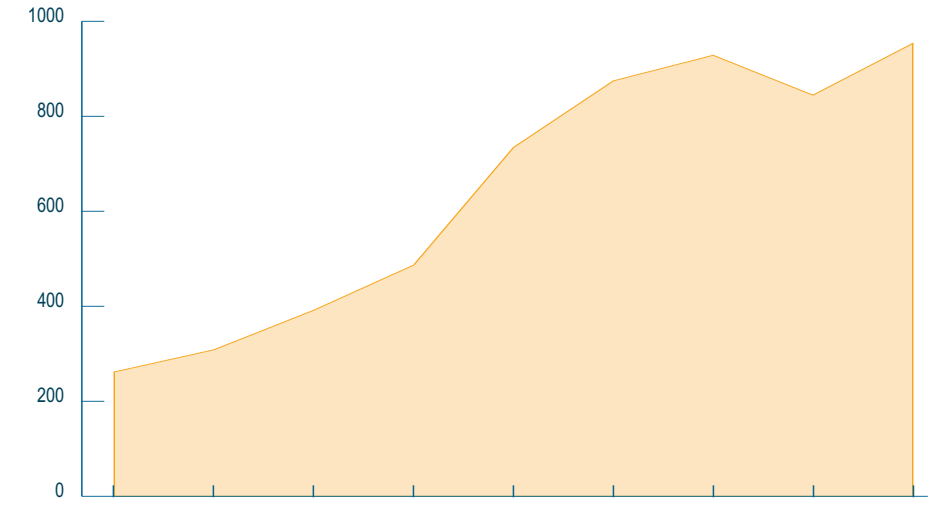
Number of UCIs



	1995	1996	1997	1998	1999	2000	2001	2002	2003
Entities	1,329	1,384	1,426	1,521	1,630	1,785	1,908	1,941	1,870

The reflation of the world economy, together with a continuous influx of new capital, meant that the total net assets of Luxembourg UCIs reached EUR 953.3 billion at the end of the year. This amount is the highest since the record level of EUR 967.7 billion in March 2002.

UCI net assets *(in billions of EUR)*



	1995	1996	1997	1998	1999	2000	2001	2002	2003
Net assets	261.8	308.6	391.8	486.8	734.5	874.6	928.4	844.5	953.3

The breakdown of UCIs across *fonds communs de placement* (FCP), *sociétés d'investissement à capital variable* (SICAV) and *sociétés d'investissement à capital fixe* (SICAF) reveals that at 31 December 2003, FCPs were still the most prevalent with 957 entities out of a total of 1,870 UCIs in operation, compared with 888 entities operating as SICAVs and 25 as SICAFs.

Breakdown of UCIs by legal status

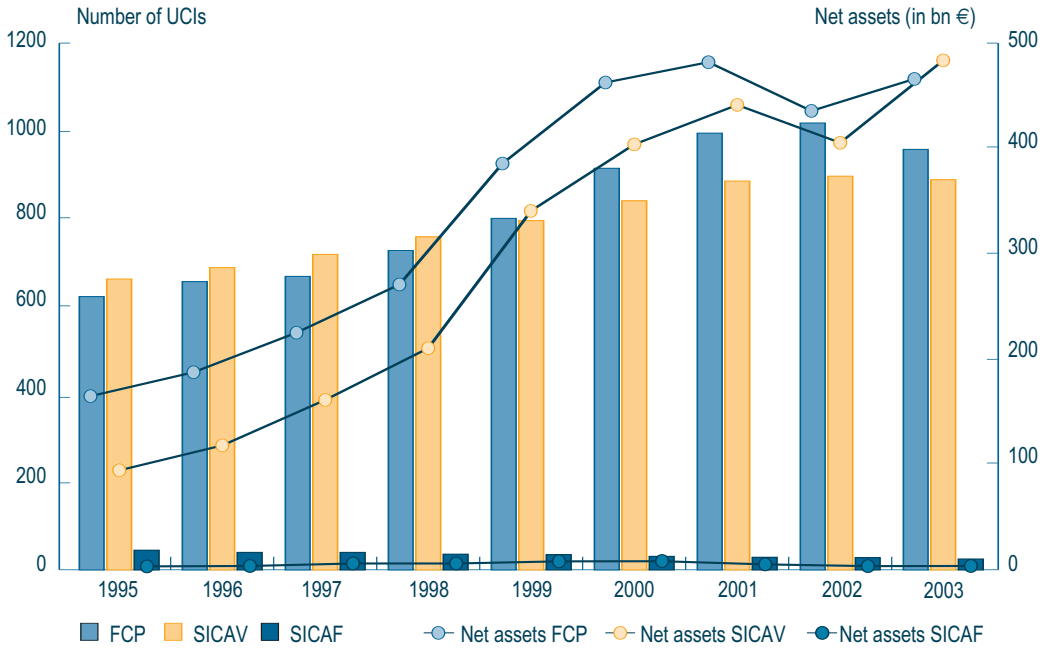
in billions of EUR

At year end	FCPs		SICAVs		SICAFs		Total	
	Number	Net assets	Number	Net assets	Number	Net assets	Number	Net assets
1995	622	164.7	662	94.2	45	2.9	1,329	261.8
1996	656	187.4	688	117.9	40	3.3	1,384	308.6
1997	668	225.0	718	161.1	40	5.7	1,426	391.8
1998	727	270.8	758	210.3	36	5.7	1,521	486.8
1999	800	385.8	795	341.0	35	7.7	1,630	734.5
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

At the end of 2003, FCP net assets totalled EUR 466.2 billion and represented 48.9% of the UCI total net assets. SICAV and SICAF assets, which amounted to EUR 483.8 billion and EUR 3.3 billion, represented 50.7% and 0.4% respectively of the total.

In 2003, the SICAV net assets grew by 19.3%, while the FCP net assets rose only by 7.0%. SICAV net assets exceed those of FCPs at the end of 2003, while the SICAF net assets practically stagnated.

Breakdown of UCIs by legal status



The following table illustrates the spread of UCIs depending on whether they fall within the scope of Part I or Part II of the law of 30 March 1988 as amended and the law of 20 December 2002 as amended or the law of 19 July 1991 relating to UCIs reserved for institutional investors.

Breakdown of UCIs falling within the Parts I and II of the law of 30 March 1988 as amended and the law of 20 December 2002 as amended and institutional funds

in billions of EUR

At year end	Part I		Part II		Institutional UCIs	
	Number	Net assets	Number	Net assets	Number	Net assets
1995	952	171.9	335	88.1	42	1.8
1996	988	209.2	353	96.2	43	3.2
1997	980	280.4	367	102.2	79	9.2
1998	1,008	360.2	400	111.0	113	15.6
1999	1,048	564.2	450	137.0	132	33.3
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

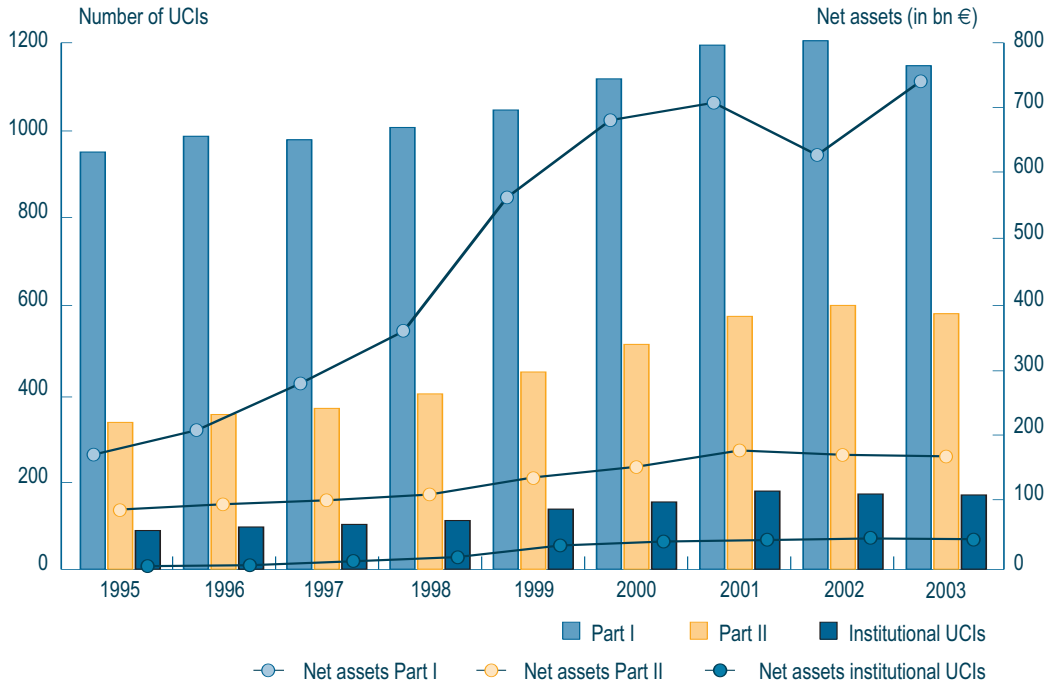
UCIs that fall under Part I of the law of 30 March 1988 as amended and the law of 20 December 2002 as amended respectively are those which comply with the provisions of the Community Directive on UCITS and which can therefore benefit from the marketing facilities provided. Part II encompasses all the other UCIs which pool funds from the public, whereas institutional funds are UCIs whose securities are not intended to be placed with the public. In terms of the regulatory provisions and especially the applicable restrictions regarding investment policies, they are nonetheless very similar to the UCIs subject to Part II of the law of 30 March 1988 as amended.

The number of UCIs under Part I and II of the law of 30 March 1988 as amended and the law of 20 December 2002 as amended slightly fell. Moreover, the net assets of UCIs under Part I rose considerably, while the assets of the UCIs under Part II decreased slightly (-1.3%).

As regards institutional UCIs, their number increased by three entities whereas their net assets decreased by 2.5%. It can be stressed in this context that the law of 30 March 1988 as amended, as well as the law of 20 December 2002 as amended allow for the creation of compartments and classes of units reserved for one or several institutional investors as regards UCIs under these laws. The current reporting of UCIs does not allow to identify the institutional investors in Part I and II of the laws.

As far as UCIs under the laws of 30 March 1988 and 20 December 2002 as amended are concerned, the distribution of UCIs subject to Part I and UCIs subject to Part II still remains fairly stable. Thus, 61.4% of all the UCIs in operation as at 31 December 2003 were Community UCITS governed by Part I of the above-mentioned laws and 31.2% were other UCIs not directly admitted to free marketing in the other EU countries. Institutional UCIs represented 7.4% of the 1,870 Luxembourg UCIs. At the same date, 77.7%, 17.8% and 4.5% of net assets were held in funds that fall under Part I, Part II and institutional investors respectively.

Breakdown of UCIs falling within Parts I and II of the law of 30 March 1988 as amended and the law of 2 December 2002 as amended and institutional funds



In 2003, only two UCIs changed from Part I of the law of 30 March 1988 as amended to submit to Part I of the law of 20 December 2002 as amended, while 52 UCIs subject to Part II of the law of 1988 were subject to Part II of the law of 2002. No UCI under Part II of the law of 30 March 1988 as amended changed into UCITS under Part I of the law of 20 December 2002 as amended. Eleven UCIs chose to submit to Part I of the law of 20 December 2002 as amended as soon as they were created and 29 UCIs opted for Part II of the law.

Breakdown of UCIs by legal status and according to Parts I and II of the law of 30 March 1988 as amended and the law of 20 December 2002 as amended and institutional UCIs

	FCP	*SICAV*	*Others*	*Total*
Part I (law 1988)	602	528	6	1,136
Part I (law 2002)	9	4	0	13
Part II (law 1988)	218	268	16	502
Part II (law 2002)	42	38	1	81
Institutional UCIs	86	50	2	138
Total	**957**	**888**	**25**	**1,870**

The following table compares the development in 2003 of the number of UCIs and net assets according to legal status as well as to the scope of the laws.

Breakdown of UCIs according to Parts I and II of the law of 30 March 1988 as amended and the law of 20 December 2002 as amended and institutional UCIs

	2002				2003				Variation 2002/2003			
Number of UCIs	*FCP*	*SICAV*	*SICAF*	*Total*	*FCP*	*SICAV*	*SICAF*	*Total*	*FCP*	*SICAV*	*SICAF*	*Total*
Part I	650	548	8	1,206	611	532	6	1,149	-6.00%	-2.92%	-25.00%	-4.73%
Part II	284	300	18	602	260	306	17	583	-8.45%	2.00%	-5.56%	-3.16%
Institutional UCIs	83	48	2	133	86	50	2	138	3.61%	4.17%	0.00%	3.76%
Total	**1,017**	**896**	**28**	**1,941**	**957**	**888**	**25**	**1,870**	**-5.90%**	**-0.89%**	**-10.71%**	**-3.66%**
Net assests (in bn €)	*FCP*	*SICAV*	*SICAF*	*Total*	*FCP*	*SICAV*	*SICAF*	*Total*	*FCP*	*SICAV*	*SICAF*	*Total*
Part I	284.414	343.117	1.379	628.910	321.419	418.316	1.361	741.096	13.01%	21.92%	-1.31%	17.84%
Part II	120.785	49.121	1.733	171.639	114.294	53.178	1.842	169.314	-5.37%	8.26%	6.29%	-1.35%
Institutional UCIs	30.571	13.237	0.151	43.959	30.509	12.265	0.118	42.892	-0.20%	-7.34%	-21.85%	-2.43%
Total	**435.770**	**405.475**	**3.263**	**844.508**	**466.222**	**483.759**	**3.321**	**953.302**	**6.99%**	**19.31%**	**1.78%**	**12.88%**

In 2003, almost all the net issues were recorded for UCIs under Part I of the law of 1988 or the law of 2002 (Community UCIs), and principally for UCIs under the form of SICAVs. UCIs under Part II of these laws totalled only EUR 2.266 billion of net issues while for institutional UCIs, net redemptions exceed two billion euros.

Breakdown of net issues according to Parts I and II of the law of 30 March 1988 as amended and the law of 20 December 2002 as amended and institutional UCIs

in billions of EUR

	FCP	*SICAV*	*Others*	*Total*
Part I	26,985	55,586	-156	82,415
Part II	- 3,056	5,052	270	2,266
Institutional UCIs	-680	-1,392	0	-2,072
TOTAL	**23,249**	**59,246**	**114**	**82,609**

1.2. Developments in umbrella funds

As opposed to the previous years where the number of umbrella funds grew continuously, the number of these UCIs fell slightly as compared to 2002. This structure, which brings together under the same legal entity several subfunds centered on investment in a given currency, geographical region or economic sector, enables investors to re-focus their investment without having to switch to another investment fund. Within a single umbrella fund, many promoters offer a range of subfunds investing in equities, debt securities or money market paper, enabling the investor to benefit from the best outlook for available returns. The structure of umbrella funds also enables promoters to create new subfunds and to manage a collective pool of assets which would not normally be large enough for separate management in a traditionally structured fund.

As shown in the table below, the trend according to which the number of umbrella funds greatly exceeds that of traditionally structured UCIs continued in 2003. The proportion in number of umbrella funds in relation to the total number of UCIs rose from 61.3% to 63.1%, whereas the proportion in terms of net assets managed increased from 85.9% to 86.1%.

Umbrella funds

in billions of EUR

At year end	*Total number of UCIs*	*Number of umbrella funds*	*As a % of the total*	*Number of subfunds*	*Average number of subfunds per umbrella fund*	*Total number of entities*	*Net assets of umbrella funds*	*As a % of the total*	*Net assets per subfund*
1995	1,329	573	43.1	2,841	4.96	3,597	174.4	66.6	0.061
1996	1,384	632	45.7	3,187	5.04	3,939	222.0	71.9	0.070
1997	1,426	711	49.9	3,903	5.49	4,618	296.1	75.6	0.076
1998	1,521	797	52.4	4,454	5.59	5,178	384.3	78.9	0.086
1999	1,630	913	56.0	5,119	5.61	5,836	604.9	82.4	0.118
2000	1,785	1,028	57.6	6,238	6.07	6,995	739.1	84.5	0.118
2001	1,908	1,129	59.2	6,740	5.97	7,519	797.8	85.9	0.118
2002	1,941	1,190	61.3	7,055	5.93	7,806	724.8	85.9	0.103
2003	1,870	1,180	63.1	6,819	5.78	7,509	820.9	86.1	0.120

As at 31 December 2003, 1,180 out of 1,870 UCIs had adopted a multiple subfund structure. The number of traditionally structured UCIs decreased from 751 to 690 (-8.1%) while the number of subfunds in operation fell from 7,055 to 6,819 (-3.3%). Thus a total of 7,509 economic entities were trading as at 31 December 2003, i.e. 3.8% less than at the close of the previous year, which can be mainly explained by the substantial number of restructurings that took place in 2003.

The average number of subfunds per undertaking decreased to 5.78 as at 31 December 2003. However, this figure conceals a wide dispersion between the smallest and largest UCIs.

As at 31 December 2003, umbrella fund net assets totalled EUR 820.9 billion, i.e. an increase of EUR 96.1 billion (+13.3%) compared with the previous year-end. With more than EUR 120 million, average net assets are still below those of traditionally structured UCIs, which totalled EUR 192 million per entity as at 31 December 2003.

1.3. Valuation currencies used

With regard to the valuation currencies used, most entities (4,921 out of a total of 7,509) are denominated in euros, followed by those in US dollars (1,796) and those in Swiss francs (238). In terms of net assets, the entities denominated in euros comprise EUR 600.130 billion of a total EUR 953.302 billion, ahead of entities expressed in US dollars (EUR 239.763 billion) and Swiss francs (EUR 51.486 billion).

1.4. UCIs' investment policy

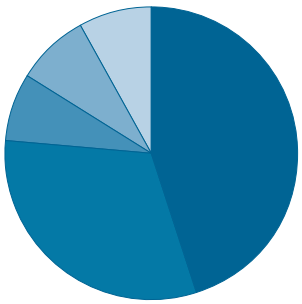
The net assets of UCIs investing in bonds increased by 11.03% compared with the end of 2002, the assets of funds investing in equities by 25.22%, the assets of funds investing in mixed transferable securities by 19.33% and the assets of funds investing in other securities by 7.64%. The net assets of UCIs investing in money market and/or in cash funds however decreased by 12.33% as compared to the end of 2002.

In absolute figures, the net assets managed by UCIs or UCI subfunds invested in bonds reached EUR 431.262 billion (i.e. 45.2% of the total net assets), followed by funds invested in equities (EUR 298.396 billion or 31.3%), money market and cash funds (EUR 77.638 billion or 8.1%), funds invested in other securities (EUR 75.670 billion or 7.9%) and mixed funds (EUR 70.336 billion or 7.4%). Funds investing in other securities include in particular funds investing in other UCIs or UCIs specialised in the investment in unlisted securities, real estate funds, funds investing in derivatives or venture capital funds.

Net assets and units/shares in UCIs by investment policy

	2002		2003		Variation	
	Number of units	*Net assets (in bn €)*	*Number of units*	*Net assets (in bn €)*	*Number of units*	*Net assets (in bn €)*
Fixed-income transferable securities	2,225	388.419	2,224	431.262	-0.04%	11.03%
Variable-yield securities	3,296	238.288	2,920	298.396	-11.41%	25.22%
Mixed transferable securities	920	58.940	916	70.336	-0.43%	19.33%
Money market instruments and/or liquid assets	248	88.561	270	77.638	8.87%	-12.33%
Other	1,117	70.300	1,179	75.670	5.55%	7.64%
Total	**7,806**	**844.508**	**7,509**	**953.302**	**-3.80%**	**12.88%**

Net assets of UCIs by investment policy



Fixed-income transferable securities	45.2%
Variable-yield transferable securities	31.3%
Mixed transferable securities	7.4%
Money market instruments and liquid assets	8.2%
Other	7.9%

The following table illustrates, per quarter, the flow of subscriptions and redemptions broken down into the main investment policies:

1 - Fixed-income transferable securities (bonds)
2 - Variable-yield securities (equities)
3 - Mixed transferable securities
4 - Money market instruments and liquid assets
5 - Other

in millions of EUR

	1st quarter 2003			*2nd quarter 2003*			*3rd quarter 2003*			*4th quarter 2003*			*Total*		
Pol.	Subsc.	Red.	N. iss.	Subsc.	Red.	N. iss	Subsc.	Red.	N. iss	Subsc.	Red.	N. iss	Subsc.	Red.	N. iss
1	159,562	145,245	14,317	191,336	175,824	15,512	219,355	209,917	9,438	224,767	217,683	7,084	795,020	748,669	46,351
2	30,064	35,917	-5,853	39,628	35,638	3,990	48,874	35,272	13,602	50,956	33,615	17,341	169,522	140,442	29,080
3	7,843	5,395	2,448	5,538	5,092	446	17,814	15,462	2,352	7,868	5,386	2,482	39,063	31,335	7,728
4	23,034	22,224	810	19,332	21,703	-2,371	15,948	18,134	-2,186	15,433	18,009	-2,576	73,747	80,070	-6,323
5	15,928	17,658	-1,730	7,113	5,443	1,670	13,934	10,746	3,188	15,477	12,832	2,645	52,452	46,679	5,773
Total	**236,431**	**226,439**	**9,992**	**262,947**	**243,700**	**19,247**	**315,925**	**289,531**	**26,394**	**314,501**	**287,525**	**26,976**	**1,129,804**	**1,047,195**	**82,609**

SUPERVISION OF UNDERTAKINGS FOR COLLECTIVE INVESTMENT

While the first quarter of 2003 was characterised by a general prudence of the investors, which resulted in net redemptions for the category of UCIs and/or subfunds investing mainly in equities, more interest was shown for this category of UCIs and/or subfunds in the second, and especially the two last quarters. Overall, only the category of UCIs and/or subfunds investing mainly in money market instruments and/or liquid assets was subject to net redemptions in 2003.

The following table breaks down the UCIs according to their investment policy. As only 13 UCIs fell under Part I of the law of 20 December 2002 as amended as at 31 December 2003, the detailed presentation published since 1990 has been maintained and the few units of these 13 aforementioned UCIs have been integrated appropriately in the three categories of Part I. This categorisation of the investment policies will be reviewed during 2004 to adapt to the needs of the law of 20 December 2002 as amended.

UCIs' investment policy

Situation as at 31 December 2003	*Number of entities*	*Net assets (in bn EUR)*	*Net assets (as a % of total)*
UCITS subject to Part I			
- Fixed-income transferable securities	1,917	393.952	41.3
- Variable-yield transferable securities	2,689	282.013	29.6
- Mixed transferable securities	803	65.131	6.8
UCITS subject to Part II[1]			
- Fixed-income transferable securities	183	20.089	2.1
- Variable-yield transferable securities	139	5.182	0.6
- Mixed transferable securities	77	3.014	0.3
UCITS subject to Part II[2]			
- Venture capital	19	0.407	0.0
- Unlisted transferable securities	14	2.056	0.2
- Leveraged funds	8	0.378	0.0
- Other open-ended UCIs	930	56.140	5.9
- Money market instruments and liquid assets	118	66.461	7.0
- Cash	121	10.501	1.1
Other UCIs subject to Part II			
- Real estate	7	2.343	0.2
- Futures and/or options	49	2.743	0.3
- Other securities	0	0.000	0.0
Institutional funds			
- Fixed-income transferable securities	124	17.221	1.8
- Variable-yield transferable securities	92	11.201	1.2
- Mixed transferable securities	36	2.191	0.2
- Venture capital	1	0.000	0.0
- Unlisted transferable securities	5	0.040	0.0
- Leveraged funds	0	0.000	0.0
- Other open-ended UCIs	137	11.016	1.2
- Real estate	6	0.522	0.1
- Futures and/or options	3	0.025	0.0
- Money market instruments and liquid assets	31	0.676	0.1
Total	**7,509**	**953.302**	**100.0**

[1] *UCITS not governed by Part I of the law dated 30 March 1988 as amended pursuant to article 2 points 1 to 3 and Part I of the law of 20 December 2002 as amended pursuant to article 3, points 1 to 3, i.e. UCITS disallowing any repurchase, not promoted in the EU or only sold to individuals in third-party countries outside the EU.*

[2] *UCITS not governed by Part I of the law dated 30 March 1988 as amended pursuant to Article 2 point 4, i.e. UCITS which fall within one of the categories set by IML Circular 91/75 owing to their investment and borrowing policy.*

1.5. Developments in guarantee-type UCIs

Guarantee-type UCIs aim to offer investors greater security than that offered by traditional collective management products. According to the investment policy pursued by the funds in question, the guarantee ensures that the subscriber is reimbursed either a proportion of the capital invested 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.

In 2003, the number of guarantee-type UCIs rose from 75 to 76 entities, and the number of units increased from 151 to 166. This increase in units is due to the launch of 44 new units while the guarantee given matured or was not extended for 29 units.

As at 31 December 2003, the 166 units comprise 18 units guaranteeing investors only a proportion of their invested capital, 82 units guaranteeing repayment in full of their invested capital (money-back guarantee), and 66 units offering their investors a return on the initial subscription price.

Funds with a money-back guarantee remain dominant, but there is also a substantial number of funds guaranteeing their investors a return on their initial investment. These funds generally track a stock market index and, through the use of derivatives, enable investors to participate to some extent in the growth of this index.

The net assets of guarantee-type UCIs increased by EUR 3.49 billion, reaching EUR 20.89 billion in 2003, i.e. an increase of 1.8%. It is also worth noting that guarantee-type UCIs created by German promoters alone included 95.4% of the total net assets of guarantee-type funds.

Developments in guarantee-type UCIs

At year end	*Number of UCIs*	*Number of economic units*	*Net assets (in bn of EUR)*
1995	43	54	5.58
1996	52	67	7.08
1997	70	90	11.47
1998	86	99	15.00
1999	85	116	17.13
2000	79	119	14.30
2001	74	115	17.09
2002	75	151	17.40
2003	76	166	20.89

1.6. Promoters of Luxembourg UCIs

The breakdown of Luxembourg UCIs according to geographic origin of their promoters highlights the multitude of countries represented in the financial centre. Promoters of Luxembourg UCIs spread over 43 countries. The main countries actively promoting UCIs in Luxembourg are Switzerland, the United States, Germany, Italy and Belgium.

Origin of promoters of Luxembourg UCIs as at 31 December 2003

Country	*Net assets (in bn €)*	*in %*	*Number of UCIs*	*in %*	*Number of units*	*in %*
Switzerland	218,587	22.9%	242	12.9%	1,329	17.7%
United States	170,869	17.9%	116	6.2%	696	9.3%
Germany	162,964	17.1%	676	36.1%	1,209	16.1%
Italy	109,621	11.5%	73	3.9%	664	8.8%
Belgium	84,899	8.9%	130	7.0%	1,032	13.7%
United Kingdom	61,751	6.5%	101	5.4%	549	7.3%
France	50,536	5.3%	162	8.7%	695	9.3%
Japan	22,567	2.4%	67	3.6%	158	2.1%
Sweden	19,192	2.0%	35	1.9%	162	2.2%
Netherlands	16,578	1.7%	40	2.1%	190	2.5%
Others	35,738	3.8%	228	12.2%	825	11.0%
Total	**953,302**	**100.0%**	**1,870**	**100.0%**	**7,509**	**100.0%**

As compared to 2002, the United States has once more overtaken Germany and took second place of Luxembourg UCI promoters.

1.7. Marketing of Luxembourg UCIs and marketing of foreign UCIs in Luxembourg

Owing to the small size of the domestic market, the vast majority of Luxembourg UCIs are marketed outside Luxembourg. The UCIs governed by Part I of the law of 30 March 1988 as amended are authorised, based on a CSSF registration certificate, to market their units/shares in other EU countries without having to follow a further approval procedure with the competent authorities.

As the UCITS under Part I of the law of 20 December 2002 as amended cannot benefit from the European passport before 13 February 2004, the CSSF did not issue any certificates for these UCIs in 2003.

Until 31 December 2003, the CSSF had delivered a total of 2,854 Directive compliance certificates for registered UCITS, representing a decrease of 56 entities compared with 31 December 2002, and an increase of 265 entities compared with 31 December 2001. The certificates issued by the CSSF were intended for 1,020 different UCIs (2002: 1,068 UCIs, 2001: 997 UCIs, 2000: 979 UCIs), which means that 89% of UCIs falling under Part I of the law of 30 March 1988 as amended had requested at least one certificate.

The main target countries in decreasing order are: Germany (737 certificates), Austria (348), Italy (314), France (265), Spain (231), Belgium (187), Sweden (164), United Kingdom (156) and the Netherlands (148).

As regards foreign UCITS marketed in Luxembourg at the end of 2003, 131 foreign Community UCITS (70 of German origin, 26 of French origin, 22 of Irish origin, 10 of Belgian origin and 3 of British origin) took advantage of the marketing facilities provided by the Directive to offer their units/shares in Luxembourg.

Finally, it is worth noting that, as at 31 December 2003, 33 foreign UCIs (16 of German origin, 15 of Swiss origin and 2 of Belgian origin) were authorised to market their units/shares in Luxembourg on the basis of Article 70 of the law of 30 March 1988 as amended.

Marketing of foreign UCIs in Luxembourg

	2000	*2001*	*2002*	*2003*
Art. 56 – Country of origin				
Germany	107	112	93	70
France	26	27	26	26
Ireland	11	15	19	22
Belgium	8	9	9	10
United Kingdom	1	2	2	3
Denmark	1	1	1	-
Subtotal	**154**	**166**	**150**	**131**
Art. 70 - Country of origin				
Germany	6	5	13	16
Switzerland	49	49	16	15
Belgium	-	1	1	2
Subtotal	**55**	**55**	**30**	**33**
Total	**209**	**221**	**180**	**164**

2. Newly created entities approved in 2003

2.1. General data

The number of newly approved entities[3] in 2003 is on the decrease as compared to 2002, thereby confirming the trend observed over the last years. Thus, 1,086 new entities have been approved in 2003, representing a decrease of 18.8% as compared to 2002, by 27.5% as compared to 2001 and by 42.4% as compared to the record year 2000.

	2000	*2001*	*2002*	*2003*
Newly approved entities	1,885	1,497	1,338	1,086
of which : launched in the same year	*1,297*	*1,020*	*881*	*637*

The entities approved in the course of a year have not necessarily been launched that same year. Until 31 December 2003, only 637 entities out of the 1,086 entities approved during the year were active, i.e. 58.7% of the total number of approved entities. This percentage is slightly inferior to that of the previous years, which stodd between 65.8% and 68.8%. The lapse between the authorisation of a new entity and its effective launching can be explained notably by the period of time promoters have to wait between the notification to the host country's authority pursuant to European regulations and the effective marketing of units/shares in the host country.

[3] *The term "entity" refers both to traditional UCIs and the subfunds of umbrella funds. The number of new "entities" therefore denotes from an economic point of view the number of economic vehicles created.*

2.2. Analysis of the investment policy of new entities

The investment policy of new entities reflects the general market trends.

Thus, in 2003, the number of UCIs investing in bonds increased so that the proportion of newly approved entities investing in bonds reached a third of the total number of approved entities in 2003. At the same time, the proportion of newly approved entities investing in equities decreased substantially.

The proportion of the number of newly approved entities investing in mixed transferable securities and that of the number of newly approved entities investing in other UCIs remained stable.

	2000		*2001*		*2002*		*2003*	
	Number of entities	*As a % of the total*	*Number of entities*	*As a % of the total*	*Number of entities*	*As a % of the total*	*Number of entities*	*As a % of the total*
Equities	965	51.19%	658	43.95%	471	35.20%	265	24.40%
Mixed	148	7.85%	146	9.75%	135	10.09%	124	11.42%
Bonds	411	21.80%	360	24.05%	325	24.29%	364	33.52%
Money Market	25	1.33%	19	1.27%	60	4.49%	52	4.79%
Funds of Funds	320	16.98%	281	18.77%	332	24.81%	255	23.48%
Futures	5	0.27%	19	1.27%	7	0.52%	15	1.38%
Various	11	0.58%	14	0.94%	8	0.60%	11	1.01%
Total	**1,885**	**100.00%**	**1,497**	**100.00%**	**1,338**	**100.00%**	**1,086**	**100.00%**

Among the 1,086 newly approved entities in 2003, 16 entities, i.e. 1.5% benefited from the reduced subscription tax reserved for UCIs/subfunds investing in cash funds, money market instruments and short-term securities.

	2000	*2001*	*2002*	*2003*
Number of entities benefiting from reduced tax	49	30	67	16

2.3. Origin of promoters of new entities

The analysis of the origin of promoters of newly created entities reveals that:

- The promoters of Belgian, Swiss and German origin take the top places. It is the first time that Belgian promoters created the highest number of entities with almost 18% of the new entities. The Swiss and German promoters were less active with 16.2% and 14.7% respectively.

- The number of new entities created by Italian and French promoters increased substantially over the last year. Italian and French promoters created 11.7% and 9.1% respectively of the newly created entities.

- Promoters from the United States created less entities as in the previous years.

Origin of the promoters of new entities

	2000		2001		2002		2003	
	Number of entities	As a % of the total	Number of entities	As a % of the total	Number of entities	As a % of the total	Number of entities	As a % of the total
Belgium	166	8.81%	169	11.29%	197	14.72%	192	17.68%
Switzerland	348	18.46%	259	17.30%	289	21.60%	176	16.21%
Germany	339	17.98%	264	17.64%	227	16.97%	160	14.73%
Italy	214	11.35%	217	14.50%	97	7.25%	127	11.69%
France	175	9.28%	147	9.82%	82	6.13%	99	9.12%
United Kingdom	115	6.10%	111	7.41%	122	9.12%	86	7.92%
United States	189	10.03%	92	6.15%	99	7.40%	76	7.00%
Austria	15	0.80%	29	1.94%	47	3.51%	38	3.50%
Netherlands	86	4.56%	31	2.07%	28	2.09%	36	3.31%

3. Closed down entities in 2003

3.1. General data

While the number of matured entities remained almost stable over the last years, the number of liquidated or merged entities increased continuously. In 2003, a total of 1,178 economic entities have been closed down. This figure includes more than 1,000 entities that have stopped their activities or have been the object of mergers.

	1995	1996	1997	1998	1999	2000	2001	2002	2003
Liquidated entities	167	183	223	254	221	254	354	490	643
Matured entities	25	35	32	43	65	47	47	49	47
Merged entities	56	72	72	195	429	150	150	326	488
Total	**248**	**290**	**327**	**492**	**715**	**451**	**551**	**865**	**1,178**

3.2. Investment policy of closed down entities

The investment policy of the closed down entities reflects the general market trends. The proportion of closed down entities investing in equities rose even stronger in 2003 with 573 entities of this category that closed down, of which 268 have merged. Moreover, a vast number of reorganisations and restructurings have taken place in the other categories, namely 294 closed down entities in the category "Bonds", including 123 merged entities, 158 in the category "Mixed", including 54 merged entities and 110 in the category "Funds of Funds", including 33 merged entities.

	2000		2001		2002		2003	
	Number of entities	As a % of the total	Number of entities	As a % of the total	Number of entities	As a % of the total	Number of entities	As a % of the total
Equities	164	36.4%	239	31.6%	381	44.0%	573	48.6%
Mixed	42	9.3%	94	12.4%	114	13.2%	158	13.4%
Bonds	182	40.4%	335	44.3%	222	25.7%	294	25.0%
Money market	20	4.4%	26	3.4%	60	6.9%	18	1.5%
Fund of Funds	15	3.3%	30	4.0%	68	7.9%	110	9.3%
Futures	12	2.7%	17	2.2%	13	1.5%	9	0.8%
Various	16	3.5%	16	2.1%	7	0.8%	16	1.4%
Total	**451**	**100.0%**	**757**	**100.0%**	**865**	**100.0%**	**1,178**	**100.0%**

3.3. The main restructurings on Luxembourg UCIs in 2003

At international level, the trend of mergers and acquisitions of banks and financial groups continued during 2003. The UCIs promoted by the banks and financial undertakings concerned by these mergers and reorganisations were also affected to a large extent by this development.

Compared to the year 2002, the total number of large UCI restructurings more than tripled.

It has to be noted that the slight decrease in 2003 in the number of UCIs in Luxembourg is also due to the mergers that took place within the scope of the restructurings of the UCI range of certain promoters, which have been quite numerous in 2003.

The main arguments put forward by the UCI promoters who initiated a restructuring were the following:

- simplification of the UCI range in order to obtain a greater transparency in the products offered;
- creation of a key-UCI with numerous subfunds instead of several legal entities;
- optimisation of the UCI range according to economic, geographical criteria or the degree of risk involved.

62 large restructurings have affected Luxembourg UCIs in 2003, involving 87 legal entities and 461 subfunds.

While the restructurings of Luxembourg UCIs that took place in 2002 were due to more diverse reasons, the restructurings in 2003 can be divided into two large categories:

1. Management activities of a promoter group taken over by another one	19 cases
2. Restructuring of the UCI range of a promoter	43 cases
Total	62 cases

Finally, it has to be noted that besides the large restructurings presented in this chapter, 43 other mergers of smaller UCIs took place in 2003, involving a total of 91 subfunds.

4. Development regarding UCIs investing principally in other UCIs: funds of funds

4.1. General data

UCIs known as funds of funds *(fonds de fonds, Dachfonds)* are UCIs whose main investment policy provides for placement of the majority of net assets in other UCIs. Their portfolios therefore consist principally, if not exclusively, of shares of SICAVs or units of *fonds communs de placement* (FCPs) in Luxembourg or other countries.

Given that UCIs falling within Part I of the law of 30 March 1988 as amended may only invest up to 5% of their net assets in other open-ended UCIs, funds of funds fall under either Part II of the law of 30 March 1988 as amended or are subject to the law of 19 July 1991 relating to funds reserved to institutional investors (institutional UCIs).

With the introduction of the law of 20 December 2002 on UCIs as amended, the UCIs known as funds of funds can fall under Part I as well as under Part II of this law.

As mentioned in the 2002 Annual Report, the number of entities investing principally in other UCIs rose sharply between 1999 (213 entities) and 2002 (997 entities). This upward trend was confirmed in 2003 as the number of entities increased to 1,098 entities as at 31 December 2003. The rate of increase over the year was 10.1% in terms of entities.

It is worth noting that the share of net assets of entities investing mainly in UCIs known as funds of funds, compared with the net assets of all UCIs, rose in 2003 and reached 7.2% at the end of 2003. Their proportion reached only 1.8% in December 1998.

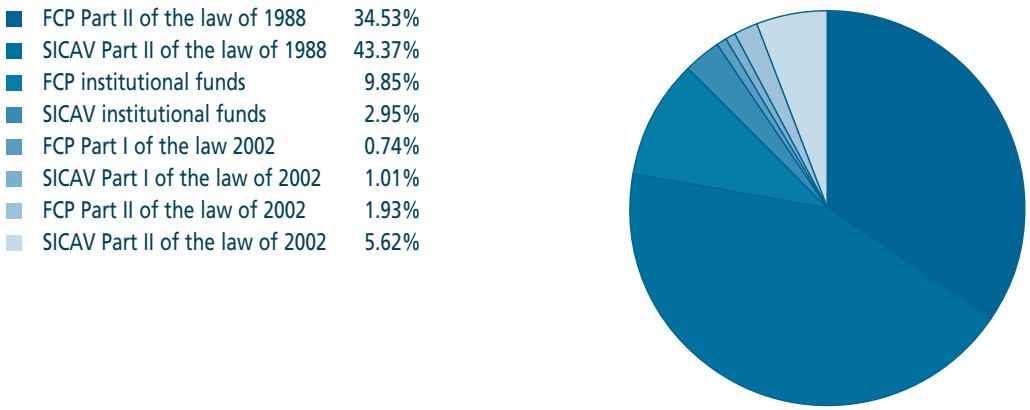
4.2. Legal status of funds of funds

As at 31 December 2003, 77.90% of UCIs known as funds of funds (846 entities) came under Part II of the law of 30 March 1988 as amended, while 12.80% (139 entities) were subject to the law of 19 July 1991.

As regards the law of 20 December 2002 as amended, 1.75% (19 entities) fall under Part I and 7.55% (82 entities) under Part II of this law.

An additional distinction according to the legal status of the UCI in question, *fonds commun de placement* (FCP) or *sociétés d'investissement* (SICAV), is shown in the following graph.

Breakdown of funds of funds according to governing laws and legal status (in terms of entities)

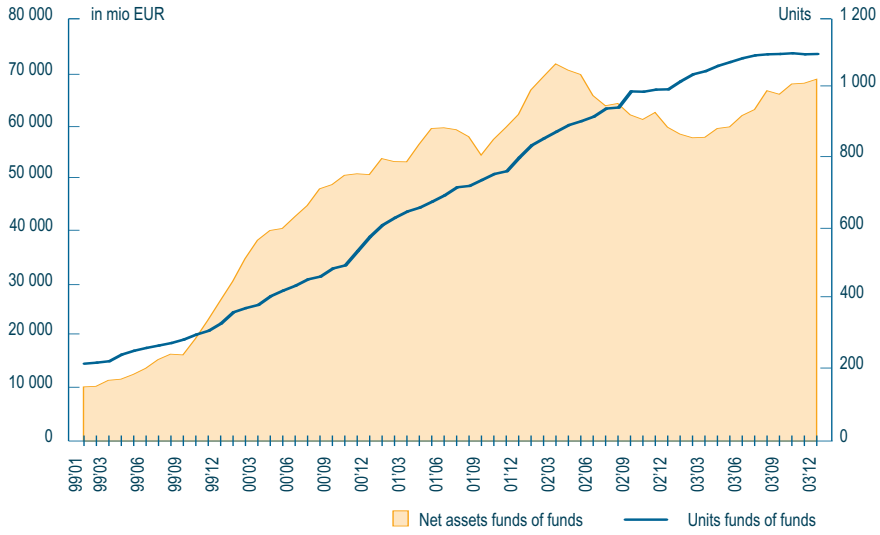


4.3. Development of the number of entities and net assets of funds of funds

The number of funds of funds entities continued to rise from January to September 2003. However, from October 2003 until the end of the year, the number of funds of funds entities did not grow any further, and reached 1,098 entities as at 31 December 2003.

The net assets of these funds reached a peak in March 2002 amounting to EUR 71.4 billion. Since then, however, the continuous slump of the stock markets has also affected net assets of funds of funds. The trend has been reversed by the revival of stock markets as from April 2003. The net assets of funds of funds amounted to EUR 68.5 billion as at 31 December 2003.

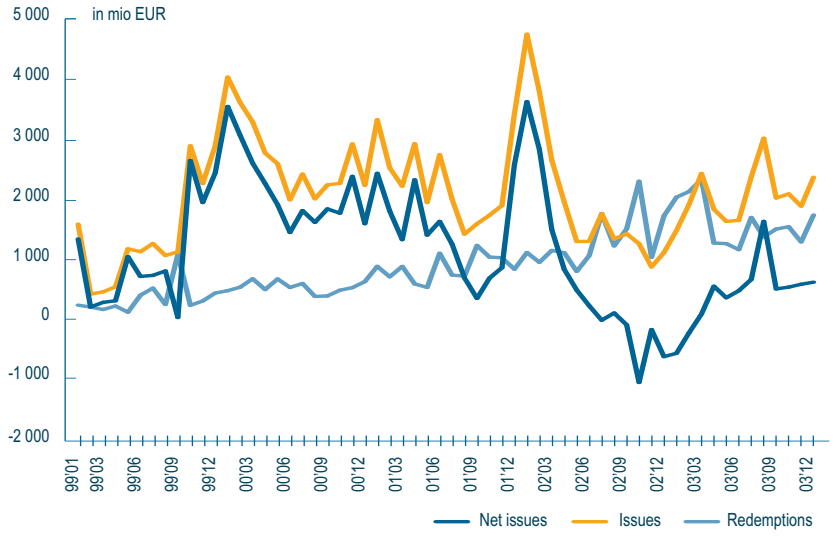
Development in the number of entities and net assets of funds of funds



4.4. Development in net issues of funds of funds

With regard to the inflow of new capital for this type of UCI, net issues totalled approximately EUR 5.4 billion for the year 2003. During the first two months of 2003, net issues were negative, thereby following a trend already observed during the last months of 2002. With the revival of the stock markets during the second quarter, the flows became positive and reached a slight peak in August 2003.

Development in issues, redemptions and net issues of funds of funds



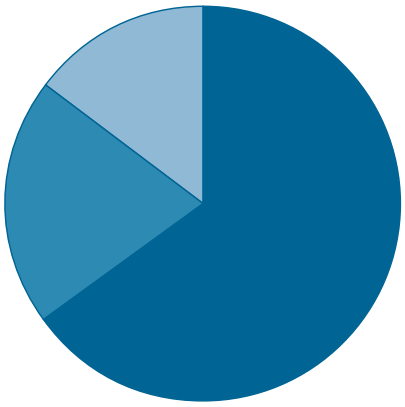
4.5. Categorisation of funds of funds according to specific investment policy

The funds of funds may be classified according to three specific investment policies:

1) those investing in other UCIs by employing a risk spreading policy (mixed funds of funds);
2) those investing in one or a very limited number of UCIs (maximum of 3) (feeder-type funds of funds);
3) those investing in funds that invest in hedge funds (funds of hedge funds).

Distribution of net assets of funds of funds according to specific investment policy

Mixed funds of funds	65.0%
Funds of hedge funds	20.4%
Feeder-type funds of funds	14.6%

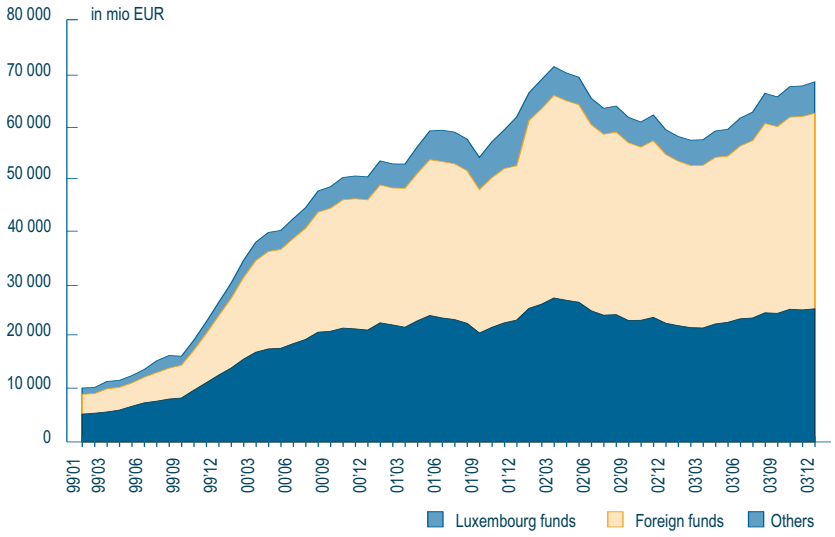


The category mixed funds of funds was in the lead in terms of net assets with 65.0%. The proportion of funds of hedge funds increased from 16.6% in 2002 to 20.4% at the end of 2003 and that of feeder-type funds of funds from 13.1% in 2002 to 14.6% at the end of 2003.

4.6. Nationality of UCIs acquired by funds of funds

As at 31 December 2003, the percentage of net assets of funds of funds invested in Luxembourg funds was 37.0%, while 54.3% were invested in foreign funds. The remaining 8.7% were invested in other financial products (cash, equities, bonds, derivatives, etc.). These proportions remained almost unchanged as compared to 31 December 2002.

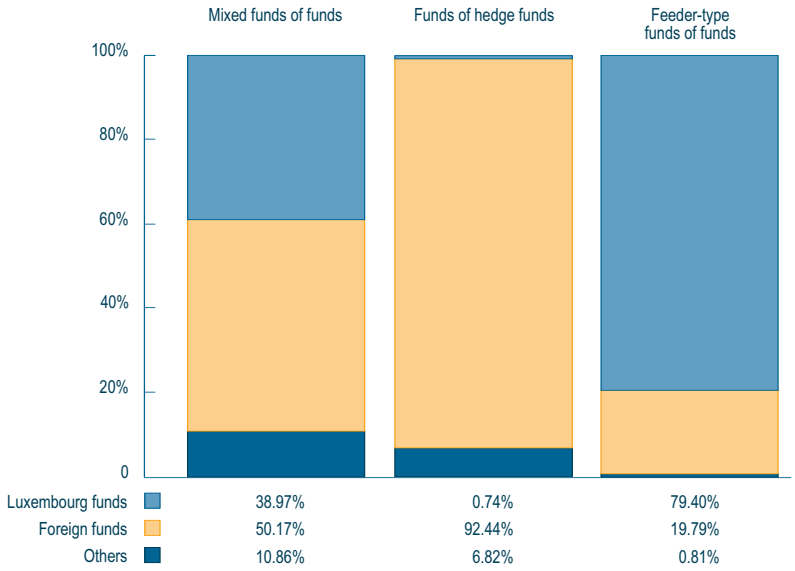
Development and distribution of net assets of funds of funds



4.7. Distribution of net assets of funds of funds according to nationality of UCIs acquired and specific investment policy

As at 31 December 2003, the share of assets of UCIs in the funds of hedge funds category investing in Luxembourg funds was almost nil, while the Luxembourg funds were the best represented in the category feeder-type funds of funds.

Distribution of net assets of funds of funds according to specific investment policy and investment product



5. Developments in the regulatory framework

5.1. The law of 19 December 2003 concerning the State budget of income and expenditure

Article 12 of the law of 19 December 2003 concerning the State budget of income and expenditure amends paragraph (3) of article 108 of the law of 30 March 1988 on UCIs as amended and paragraph (3) of article 129 of the law of 20 December 2002 on UCIs as amended.

Under the terms of this law, certain Luxembourg UCIs and certain compartments will be exempt from the subscription tax as from 1 January 2004, on the condition that the following four criteria are met:

- the UCI's or the compartment's securities must be reserved for institutional investors;
- the UCI's or the compartment's object must be the collective investment in money market instruments and the placing of deposits with credit institutions;
- the weighted residual portfolio maturity must not exceed 90 days;
- the UCI or the compartment must have obtained the highest possible rating from a recognised rating agency.

Where several classes of securities exist within the UCI or the compartment, the exemption only applies to classes whose securities are reserved for institutional investors.

5.2. Circular CSSF 03/97 concerning the publication by undertakings for collective investment in the reference database of the simplified and full prospectuses as well as the annual and semi-annual reports

The purpose of circular CSSF 03/97 of 28 February 2003 is to specify the publication modes of simplified and full prospectuses and the annual and semi-annual reports that UCIs shall publish for their investors in accordance with Chapter 17 of the law of 20 December 2002 regarding UCIs as amended.

The circular states that the *Centrale de Communications Luxembourg S.A.* (CCLux) set up a database of the financial centre in order to create an infrastructure allowing investors and professionals of the industry to access by electronic means all the prospectuses as well as the annual and semi-annual reports concerning Luxembourg UCIs.

Pursuant to article 114(2) of the law of 20 December 2002, simplified and full prospectuses as well as annual and semi-annual reports of UCIs subject to the aforementioned law must be published in the database of the financial centre. This obligation does not apply to UCIs subject to the law of 19 July 1991 regarding UCIs the securities of which are not intended to be placed with the public.

Moreover, it is highly recommended that UCIs subject to the law of 30 March 1988 regarding UCIs as amended also comply with this obligation of publication in the database.

The CSSF may grant, if duly justified, an exemption as regards the publication of prospectuses and annual and semi-annual reports in the database of the financial centre.

5.3. Circular CSSF 03/108 concerning Luxembourg management companies subject to Chapter 13 of the law of 20 December 2002 concerning undertakings for collective investment as amended, as well as Luxembourg self-managed investment companies subject to article 27 or article 40 of the law of 20 December 2002 as amended

The main purpose of circular CSSF 03/108 of 30 July 2003 is to specify the application modes of certain articles of Chapter 13 of the law of 20 December 2002 concerning UCIs as amended, which introduces a specific regime applicable to management companies that manage UCITS under the amended Directive 85/611/EEC.

The majority of the provisions of the circular apply *mutatis mutandis* to investment companies under the amended Directive 85/611/EEC that have not designated a management company in conformity with this Directive.

The circular specifies the conditions which must be fulfilled in order to obtain and maintain an authorisation, distinguishing between management companies whose activities are restricted to collective management as provided for by Article 77(2) of the law of 20 December 2002 as amended, and management companies which carry out collective management and management of investment portfolios on a client-by-client basis as provided for by Article 77(3). In this context, it provides clarifications as regards the programme of activity, central administration and infrastructure, shareholders, professional repute and experience of the directors, own funds and external audit.

The circular also contains rules concerning the prudential supervision of management companies referred to under Chapter 13 of the law of 2002 as well as the prudential supervision of investment companies under the amended Directive 85/611/EEC, which have not designated a management company under the terms of this Directive.

The schedules for financial information, which are to be drawn up on a quarterly basis and submitted to the CSSF with regard to prudential supervision, are appended to the circular.

5.4. Circular CSSF 03/122 concerning clarifications of the simplified prospectus

Circular CSSF 03/122 of 19 December 2003 provides lines of conduct concerning the content of the simplified prospectus and notably the interpretation of certain elements of information comprised in schedule C appended to the law of 20 December 2002 concerning UCIs as amended.

The circular notably aims to describe three elements of information of the simplified prospectus mentioned in schedule C, namely:

- the UCITS' objectives, the UCITS' investment policy and a brief assessment of the UCITS' risk profile,
- the historical performance of the UCITS,
- the other possible expenses and fees.

The circular thus indicates that the description of the UCITS' risk profile is of qualitative nature.

Under the terms of the circular CSSF 03/122, UCITS can calculate a Total Expense Ratio (TER). The circular lays down rules to comply with in case a UCITS does so.

Circular CSSF 03/122 also determines the authorisation procedure of the CSSF in relation to the simplified prospectus.

Moreover, UCITS, which, by virtue of the transitional provisions of the law of 20 December 2002 as amended, remain governed by part I of the law of 30 March 1988 relating to UCIs as amended until 13 February 2007 at the latest, are not compelled by the law to publish a simplified prospectus. If any such UCITS nevertheless intend to publish a simplified prospectus, they must meet the requirements imposed by annexe I, schedule C, for the simplified prospectus of UCITS subject to part I of the law of 20 December 2002 as amended.

6. Management companies

6.1. Management companies under Chapter 13 of the law of 20 December 2002 relating to undertakings for collective investment as amended

The year 2003 was marked by the approval of the first management company under Chapter 13 of the law of 20 December 2002 as amended allowed to benefit from the European passport by way of the right of establishment and the freedom to provide services in another Member State of the European Union.

As at 31 December 2003, 16 management companies had submitted their application for approval to the CSSF in order to subject to the provisions of Chapter 13. At the end of 2003, three entities have been registered on the official list of management companies under Chapter 13 of the law of 20 December 2002 as amended, i.e.:

- BNP Paribas Asset Management Luxembourg, whose sole purpose is the management of undertakings for collective investment;

- LRI Fund Management Company S.A., whose purpose is the management of undertakings for collective investment, the management of investment portfolios on a discretionary client-by-client basis, as well as investment advice;

- Union Investment Luxembourg S.A., whose purpose is the management of undertakings for collective investment, the management of investment portfolios on a discretionary client-by-client basis, as well as the safekeeping and administration of units/shares of UCIs.

On the whole, the CSSF noted that one year following the coming into force of the law of 20 December 2002 as amended, a high number of market players took up the challenge to comply with the new legal provisions.

6.2. Overall situation

As at 31 December 2003, 284 management companies were active in the Luxembourg financial centre, among which three comply with the provisions of Chapter 13 of the law of 20 December 2002 as amended. 148 manage UCITS exclusively and 42 manage UCITS as well as other UCIs.

Of the remaining management companies, 54 exclusively manage UCIs subject to Part II of the law of 30 March 1988 as amended and/or subject to Part II of the law of 20 December 2002 as amended, 37 management companies manage exclusively UCIs subject to the law of 19 July 1991 on undertakings for collective investment whose securities are not intended to be placed with the public and three management companies manage UCIs subject to Part II of the law of 30 March 1988 as amended and/or Part II of the law of 20 December 2002 a amended, as well as UCIs subject to the law of 19 July 1991.

Distribution of management companies (MCs)	*Number*
MCs subject to Chapter 13 of the law of 2002	3
MCs subject to Chapter 14 of the law of 2002	281
Total	**284**
of which	
MCs managing exclusively UCITS subject to Part I of the law	148
MCs managing UCITS subject to Part I of the law as well as other UCIs	42
MCs managing UCIs subject to Part II of the law	54
MCs managing UCIs subject to Part II of the law and UCIs subject to the law of 1991	3
MCs managing UCIs subject to the law of 1991	37

According to the preceding table, 190 management companies manage at least one UCITS subject to Part I of the law of 1988 and/or the law of 2002 as at 31 December 2003.

The law of 20 December 2002 as amended provides that the management companies approved before 13 February 2004 that manage at 13 February 2004 a UCITS subject to Part I of the law of 1988 and/or of the law of 2002, can benefit from the so-called grandfathering clause, under the terms of which they must comply with the requirements laid down in Chapter 13 of the law of 2002 only at 13 February 2007 at the latest.

However, this is not the case for management companies managing exclusively UCIs under Part II of the law of 1988 and/or the law of 2002 on 13 February 2004. Consequently, should these management companies wish to manage UCITS under Part I of the law of 2002 after 13 February 2004, they must comply with the provisions of Chapter 13 of the law of 2002.

The following table shows a breakdown of management companies managing only one UCITS or UCI as at 31 December 2003.

Management companies (MCs) managing only one UCITS/UCI	*Number*
MCs managing only one UCITS subject to Part I of the law	143
MCs managing only one UCI subject to Part II of the law	54
MCs managing only one UCI subject to the law of 1991	37

6.3. Prudential supervisory practice

6.3.1. Notification procedure for management companies

The law of 20 December 2002 as amended introduces a European passport for management companies complying with the amended Directive 85/611/EEC. Under this European passport, management companies may perform, under the freedom to provide services, the activity, for which they have been authorised in their home Member State, in a Member State of the European Union other than their home Member State. They can also establish a branch in a Member State of the European Union other than their home Member State.

Articles 88 and 89 of the law of 20 December 2002 as amended provide for a notification procedure for Luxembourg management companies wishing to establish a branch within the territory of another Member State or wishing to carry on business within the territory of another Member State of the European Union under the freedom to provide services. Under the terms of the aforementioned articles, these management companies must communicate certain information to the CSSF.

A management company wishing to establish a branch within the territory of another Member State must provide the following information:

a) the Member State within the territory of which the management company plans to establish a branch;
b) a programme of operations setting out the envisaged activities and services, as well as the organisational structure of the branch;
c) the address in the host Member State from which documents may be obtained;
d) the name of the persons responsible for the management of the branch.

A management company wishing to carry on business within the territory of another Member State of the European Union under the freedom to provide services, must provide the following information:

a) the Member State within the territory of which the management company intends to operate;
b) a programme of operations stating the envisaged activities and services.

The CSSF forwards the information to the competent authorities of the host Member State.

The notification procedure for management companies as provided for by article 89 is an innovation introduced by the law of 20 December 2002 as amended and is not to be mistaken for the notification procedure for UCITS as laid down by the provisions of article 55 of this law, which has been taken over from the law of 30 March 1988 as amended and which provides that a UCITS wishing to market its units in another Member State of the European Union, must inform the CSSF thereof, as well as the competent authorities of this Member State.

The notification procedure for management companies comes on top of the notification procedure for undertakings for collective investment (UCITS) benefiting from the European passport.

6.3.2. Application of the law of 20 December 2002 relating to UCIs as amended

The legal provisions governing management companies under Chapter 13 of the law of 20 December 2002 as amended being relatively recent, they give rise to certain interpretation issues. Hereinafter are some of these questions allowing to explain the CSSF's position.

- **Means to be put into place by a management company under Chapter 13 of the law of 20 December 2002 concerning undertakings for collective investment as amended in order to take account of the provisions of article 42(1) as regards the use of a risk-management process**

Article 42(1) of the law of 20 December 2002 as amended provides that the management companies under Chapter 13 of this law are required to manage the risks associated with their investment portfolios and to use a risk-management process. Consequently, the setting up of a risk-management process is an additional structural element which must be taken into account in order to verify that a management company complies with the legal requirements laid down in the law of 2002. As the legal texts do not specify under which form this risk-management process must be set up, the CSSF takes up the following position.

In order to carry out the management functions provided for by Annexe II of the law of 2002, the CSSF considers that a management company must have appropriate means allowing it to adequately monitor the risks inherent in the investment portfolios. It must, in principle, set up its own risk-management department.

Nevertheless, it can also delegate, under its own responsibility, the risk control to a qualified third party. In this case, the CSSF considers that a management company under Chapter 13 of the law of 20 December 2002 as amended must not necessarily have the technical means in relation to risk management, but must employ one or several persons qualified and experienced to verify that risk-management processes used are appropriate for the various UCITS under management. Moreover, the person(s) must be able to interpret and control the results generated, and be able to intervene in case of problems and propose corrective measures.

The risk-management process must be adapted to the investment policy of the UCITS managed.

In short, a management company must have the means to ensure permanent monitoring of risks inherent in investment portfolios under its management.

- **Possibility of the board of directors of an investment company having designated a management company to directly delegate one of the functions mentioned in Annexe II of the law of 20 December 2002 concerning undertakings for collective investment as amended**

Article 27 of the law of 2002 provides, inter alia, that investment companies, which have not designated a management company under Chapter 13 of this law must meet a series of criteria as regards the "substance" of these investment companies. The investment companies that have designated a management company under Chapter 13 of the law are not obliged to fulfil these criteria, as they are met by the management company.

The law however does not give any specific explanations as to the meaning of the terms "designate a management company".

As regards investment companies that have designated a management company, the following question arises: does the delegation of one or several of the three functions provided under Annexe II to the law of 20 December 2002 as amended, i.e. investment management, administration and marketing, necessarily have to pass through the management company or is the board of directors allowed to directly delegate one of these functions to a third party?

In this context, the CSSF's interpretation is as follows: an entity may only be considered as a management company if its corporate purpose includes at least the three functions included in the activity of collective portfolio management of Annexe II of the law of 2002.

The CSSF considers that the terms "designate a management company" are intended for situations where an investment company delegates all three management functions of Annexe II of the law of 2002 to a management company. In this case, the board of directors of the investment company cannot directly delegate one of these functions to a third company.

- **Possibility of a management company governed by Chapter 13 of the law of 20 December 2002 concerning undertakings for collective investment as amended, to perform the activity of receipt and transmission of orders, which is defined as commission agent under the law of 5 April 1993 on the financial sector as amended**

This point is connected with the question asked by certain professionals of the financial sector (PFS) that transformed into management companies under Chapter 13 of the law of 20 December 2002 as amended. Indeed, these management companies asked for permission to continue with their activities, including those performed as commission agent, for which they had been granted approval under their PFS status. Therefore, the question arose as to whether the activity of commission agent is governed by the provisions of Chapter 13.

The CSSF considers that a management company under Chapter 13 of the law of 2002 can act as commission agent on the sole condition that the mandates fall either under collective management, or under investment portfolio management on a discretionary basis, as this activity is necessary to carry on these mandates.

- **Collective management and investment portfolio management activities of a management company under Chapter 13 of the law of 20 December 2002 concerning undertakings for collective investment as amended**

As a management company under Chapter 13 of the law of 20 December 2002 as amended can carry on, besides collective management activities, investment portfolio management activities on a discretionary client-by-client basis, the question arose as to whether the latter activity can take precedence in terms of volume over collective management and whether a certain balance, in terms of volume, between collective management and investment portfolio management on a discretionary client-by-client basis should be imposed.

This question is of particular interest as the requirements in terms of initial capital imposed on management companies under Chapter 13 of the law of 20 December 2002 as amended can be less restrictive as the requirements concerning the initial capital for private portfolio managers according to the law of 5 April 1993 on the financial sector as amended.

The CSSF considers that situations of misuse must be avoided in this regard. Circular CSSF 03/108 therefore specifies that where a management company under Chapter 13 of the law of 2002 as amended provides investment portfolio management on a discretionary client-by-client basis, specific conditions must be fulfilled.

Insofar as the services provided by these management companies as regards client-by-client management are the same as those provided by private portfolio managers falling within the scope of article 24 B) of the law of 5 April 1993 on the financial sector as amended, the same prudential rules are to be applied, in principle.

Moreover, circular CSSF 03/108 defines that where a management company of UCITS provides services of investment portfolio management on a discretionary client-by-client basis, the provisions of circular CSSF 00/12 defining the capital ratios pursuant to article 56 of the law of 5 April 1993 on the financial sector as amended are applicable.

7. Prudential supervisory practice

7.1. Prudential supervision

7.1.1. Standards to be observed by UCIs

One of the fundamental functions of the CSSF when supervising UCIs is to ensure application of the laws and regulations relating to UCIs. The aim of supervision is to ensure adequate protection of investors as well as stability and security in the UCI sector.

7.1.2. Instruments of prudential supervision

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

- examination of the periodic financial information which UCIs must submit to the CSSF on a monthly and annual basis;
- analysis of annual and semi-annual reports which UCIs must publish for their investors;
- analysis of the management letters issued by the external auditor, which must be communicated immediately to the CSSF;
- analysis of the statements made on the basis of the circular relating to protection of investors in the event of a miscalculation of net asset value (NAV) and correction for the consequences of non-compliance with investment rules applicable to UCIs;
- on-site inspections carried out by agents of the CSSF.

7.1.3. Auditing

- **Auditing of semi-annual and annual reports**

The result of the examination of semi-annual and annual reports by the CSSF shows that these reports are in general prepared in accordance with the applicable legal rules. During 2003, the CSSF had to intervene with several UCI service providers due to the following factors:

- publication deadline was not met by several funds subject to Part II of the law of 30 March 1988 as amended and by UCIs that were put into liquidation;
- non-compliance of the financial report with the fund's investment policy or lack of required information;
- representation of the promoter on the board of directors;
- absence of the indication that the subscription can only be made on the basis of the UCI's prospectus;
- exchange rate not indicated;
- incorrect indication of the UCI's or compartment's denomination;
- high fees;
- incorrect breakdown of the securities portfolio.

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

In accordance with circular IML 97/136 and pursuant to article 94(1) of the law of 30 March 1988 as amended and article 118 of the law of 20 December 2002 as amended, 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 time limit to transmit the monthly financial information is twenty days following the reference date, which is in principle the last day of each month. As regards yearly financial information, the date of reference is the date of the close of the financial year and the time limit is four months.

As far as monthly financial information is concerned, the CSSF considers that UCIs must, on the one hand, scrupulously observe the imparted deadline to submit table O1.1. and, on the other hand, pay due attention when drawing up this table so as to ensure that the format and content are correct. To this end, the CSSF called to order the UCIs that did not meet these conditions, leading the central administrations in charge to review their procedures to make sure that the files are transmitted within the time limit and to improve the quality of this reporting. For information, the format and content of about 7,500 files, representing around 15,000 types of units/shares, are controlled each month.

- **On-site inspections**

During 2003, the CSSF carried out six on-site inspections at the premises of providers of services to UCIs.

The purpose of two on-site inspections was to notably assess the functioning of the central administration and of the UCI depositary bank, as well as the anti-money laundering procedures. Two on-site inspections mainly aimed to assess the functioning of the UCI's central administration and the procedures set up in the fight against money laundering. The sole purpose of another inspection was the assessment of the functioning of the UCI's central administration and another inspection concerned the assessment of the anti-money laundering procedures.

The providers of services that have been inspected by the CSSF carry out the functions of central administration and/or depositary bank for more than 500 UCIs, so that the inspections made by the CSSF in 2003 concerning the organisation of the central administration and depositary bank functions covered a large number of UCIs.

- **Specific audits**

In 2003, the CSSF required that a management company of UCIs charged an external auditor to undertake a specific audit. This audit was aimed at verifying the organisation of the management company in the fields of fund management, risk management and assessment, and compliance.

- **Survey on late trading and market timing**

The CSSF sent a circular letter to 425 service providers established in Luxembourg and operating for Luxembourg UCIs, mainly central administrations, depositary banks, registrar and transfer agents, management companies and distributors of units/shares of investment funds, in November 2003 and February 2004 respectively, inviting them to answer a set of questions relating to late trading and market timing practices.

The CSSF wished to know, by means of this survey, whether the entities surveyed had set up specific procedures to rule out any late trading and market timing practices. The CSSF enquired about the results obtained thanks to these procedures and asked those entities that have noted cases of late trading or market timing in the past, to give an account of these cases and to indicate at the same time the name of the UCI(s) concerned, the measures taken against the natural and legal persons involved, as well as the financial impact of these practices on the UCI and its investors.

The vast majority of the entities surveyed co-operated with the CSSF by providing extensive information. Even if the CSSF has not finalised its survey to date, it can already state that considering the responses received the situation is overall under control, even though supplementary information will be required in certain isolated cases. Moreover, it is not ruled out that the CSSF will carry out on-site inspections at certain entities' premises to verify the information provided.

The CSSF is satisfied to note that the entities surveyed have taken or are taking the necessary additional measures of protection.

After the professionals of the financial sector have been consulted, the CSSF has decided to publish a circular intended to provide the latter with appropriate guidelines. This circular will notably serve as a reference for their future decisions and choices. The CSSF will take into account the specificities of the Luxembourg investment fund industry. Indeed, many Luxembourg funds are invested as well as distributed across all the time zones and marketed through intermediaries subject to a foreign supervisory authority.

As a conclusion, the CSSF stresses that the protection and fair treatment of the investors has always been its absolute priority. This will therefore be the *leitmotiv* of the future circular, whose purpose will be to avoid that investors are financially harmed when the above-mentioned improper practices are used.

- **Meetings**

In 2003, 142 meetings were held between representatives of the CSSF and intermediaries of the UCIs. These meetings concerned the presentation of new UCI projects, restructurings of UCIs but also the application of the laws and regulations of UCIs

7.2. Application of the law of 20 December 2002 concerning UCIs as amended

During 2003, a series of inquiries concerning the interpretation of the law of 20 December 2002 concerning UCIs as amended were submitted to the CSSF.

Many requests for information concerned the application of the transitional provisions of the law of 20 December 2002 as amended, while others were related to the adjustments of the investment policy relating to the transition under this law, the wording of the articles of association of an investment company under Part I of this law or the content of the simplified prospectus.

The CSSF also gave an opinion concerning certain aspects of the investment policy applicable to UCITS under Part I of the law of 20 December 2002 as amended.

7.2.1. Transitional provisions of the law of 20 December 2002 as amended

Until 13 February 2007, the Luxembourg UCI sector is governed by two laws, namely the law of 30 March 1988 as amended and the law of 20 December 2002 as amended.

Within the scope of the enforcement of the law of 20 December 2002 as amended and the transition under this law of UCIs previously subject to the law of 30 March 1988 as amended, the CSSF handled some twenty requests concerning the application of the transitional provisions of the law of 2002 during 2003.

The law of 2002 provides that UCIs subject to Part II of the law of 1988 will be *ipso jure* subject to the law of 2002 as from 13 February 2004.

One question that arose concerned amendments to the articles of association to be made by UCIs having adopted a company structure that are *ipso jure* subject to the law of 2002 as from 13 February 2004. The CSSF considered that where the articles of association do not need to be amended, except where the reference to the law of 30 March 1988 as amended should be replaced by a reference to the law of 20 December 2002 as amended, these UCIs do not need to modify their articles of association before 13 February 2004. It is understood that the UCIs concerned will replace the references to the law of 20 December 2002 as amended on the next occasion, such as for instance after the ordinary general meeting.

The CSSF stressed that in any case, the UCIs subject to the law of 20 December 2002 as amended must update their prospectus so that it mentions that they are subject to this law. When the conclusion is reached that the prospectus does not need an amendment other than the replacement of the reference to the law of 30 March 1988 as amended by a reference to the law

of 20 December 2002 as amended, this modification can be made by means of an addendum specifying that the references to the law of 30 March 1988 as amended are to be replaced by references to the law of 20 December 2002 as amended.

Moreover, the CSSF stressed that there should be no inconsistencies between the UCI's prospectus and its constituting documents.

7.2.2. Modifications to the investment policy

The CSSF's position is that the modifications to the investment policy are to be accompanied by a notice of one month, during which investors can request the redemption of their units/shares free of charge.

A UCI, which extends its investment policy must consequently accompany the modification of its investment policy by a notice of one month during which investors must be able to request the redemption of their units/shares free of charge.

This principle also applies to the modifications or extensions of the investment policy under Part I of the law of 20 December 2002 as amended if substantial modifications in accordance with Part I of the law of 30 March 1988 as amended are concerned.

The modifications to the investment policy become effective only after the expiry of the one month's notice.

However, the CSSF considers that modifications that do not constitute an extension of the investment policy and which are carried out with the sole purpose of complying with the provisions of the law of 20 December 2002 as amended must not be accompanied by a one month's notice.

7.2.3. Information of the simplified prospectus and the full prospectus concerning the historical performance of the UCI and the profile of the typical investor

Schedule A annexed to the law of 30 March 1988 as amended and schedule A annexed to the law of 20 December 2002 as amended contain information relating to the full prospectus of the UCIs, while the schedule C annexed to the law of 20 December 2002 as amended contains information on the content of the simplified prospectus of UCIs.

The law of 2002 supplemented Schedule A annexed to the law of 1988 with the points 5 and 6.

In this context, the question arose as to whether it is sufficient to insert information concerning the historical performance and the profile of the typical investor of the UCI solely in the simplified prospectus and not in the full prospectus.

As point 5.1. of schedule A of the law of 20 December 2002 as amended stipulates that the information concerning the UCI's historical performance can be attached to the prospectus, the CSSF considers that the information concerning the historical performance must only be included in the simplified prospectus.

On the other hand, the information concerning the profile of the typical investor must be included in the simplified prospectus as well as in the full prospectus. Indeed, point 5.2. of schedule A and schedule C of the law of 2002 require that the full prospectus and the simplified prospectus contain the profile of the typical investor for which the UCI is designed.

7.2.4. Regulated market

On several occasions, the CSSF was led to decide on the interpretation of the term "regulated market" defined in point 20) of article 1 and in article 41(1) of the law of 20 December 2002 as amended.

The CSSF considers that the market regulated by ISMA (International Securities Market Association) can be regarded as a regulated market as defined under article 41(1). On the other hand, the American TRACE (Trade Reporting and Compliance Engine) system is not a regulated market as such as defined under article 41(1), but the OTC Fixed Income market, to which the TRACE system is linked, can be considered as a regulated market as defined by the law in question.

In the context of the EU enlargement, the CSSF considers that the official stock exchanges of the countries who are to join the EU on 1 May 2004 are regulated markets as defined in article 41(1) of the law of 20 December 2002 as amended.

7.2.5. Use of credit default swaps (CDS)

As far as the use of credit default swaps (CDS) by UCITS under Part I is concerned, the CSSF considers that the use of these instruments is subject to the following conditions:

- the counterparties to the CDS must be first-class financial institutions specialised in this type of transactions;
- the prospectuses of the UCITS must provide a detailed description of the functioning and the risks linked to CDS and also indicate the assessment process which must be duly approved by the external auditor of the UCITS, in order to ensure adequate investor information.

Moreover, the following rules must be complied with where CDS contracts are concluded with a purpose other than hedging:

- the CDS must be used in the exclusive interest of investors by letting presume an interesting return compared to the risks incurred by the UCITS;
- the maximum limit in terms of inherent commitments to CDS must not exceed 20% of net assets of the UCITS. Moreover, the total commitments of the CDS and the total commitments of the other techniques and instruments shall not, at any moment, exceed the total value of the UCITS' net assets;
- the general investment restrictions (10% of the net assets in one issuer, etc.) must apply to the CDS issuer and to the CDS' final debtor risk ("underlying");
- the use of CDS must fit the investment and the risk profiles of the UCITS concerned;
- UCITS must ensure that they guarantee adequate permanent coverage of commitments linked to the CDS and must always be in a position to honour the investors' redemption requests;
- the CDS selected by the managers of UCITS must be sufficiently liquid so as to allow the UCITS to sell/settle the contracts in question at the defined theoretical prices.

7.3. Voluntary liquidations

As regards the liquidation of UCIs, the CSSF and the *Caisse de Consignation* came to the conclusion that the liquidation of a UCI or a compartment of an umbrella fund should in principle be closed within a time limit of nine months at the most.

Where this time limit cannot be met due to exceptional reasons, the UCI concerned can submit a duly justified application for exemption to the CSSF.

Under the terms of article 83 of the law of 30 March 1988 as amended and article 107 of the law of 20 December 2002 as amended, in the event of a voluntary or compulsory liquidation of a UCI, the sums and assets payable in respect of units whose holders failed to present themselves at the time of the closure of the liquidation, must be paid to the *Caisse de Consignation* to be held for the benefit of the persons entitled thereto.

At the time of the payment to the *Caisse de Consignation* of the sums and assets payable in respect of units whose holders failed to present themselves, the UCI can decide whether all the correspondence and payments made to the *Caisse de Consignation* must be made through the UCI. By means of this decision, the UCI can maintain the contact with his clients with a view of offering other investment products.

7.4. Circular CSSF 02/77

7.4.1. Statements made in 2003 on the basis of CSSF Circular 02/77

Circular CSSF 02/77 of 27 November 2002 concerning the protection of investors in case of NAV calculation error and correction of the consequences resulting from non-compliance with the investment rules applicable to undertakings for collective investment repealed circular CSSF 2000/8.

In 2003, the CSSF recorded 788 statements on the basis of circular CSSF 02/77, against 830 statements in 2002, representing a decrease of 5%.

Among these statements, 280 cases (348 cases in 2002) concerned NAV calculation errors and 508 cases (482 cases in 2002) non-compliance with investment rules, including 70 cases (61 cases in 2002) of non-compliance with investment policy. It is noteworthy that in absolute terms, the cases of NAV calculation errors decreased substantially as compared to 2002, i.e. a decrease of 20%, while the cases concerning non-compliance with investment rules increased by 5%.

The fact that the number of cases of NAV calculation errors in absolute terms continued to decrease can be explained by the continuous efforts of the central administrations of UCIs to improve their work procedures.

192 of the 280 cases of NVA calculation errors and 242 of the 508 cases of non-compliance with investment rules could not be closed at 31 December 2003, as the CSSF is still awaiting further information or the report(s) of the external auditor or the management letters following the application of the simplified procedure as foreseen by circular CSSF 02/77.

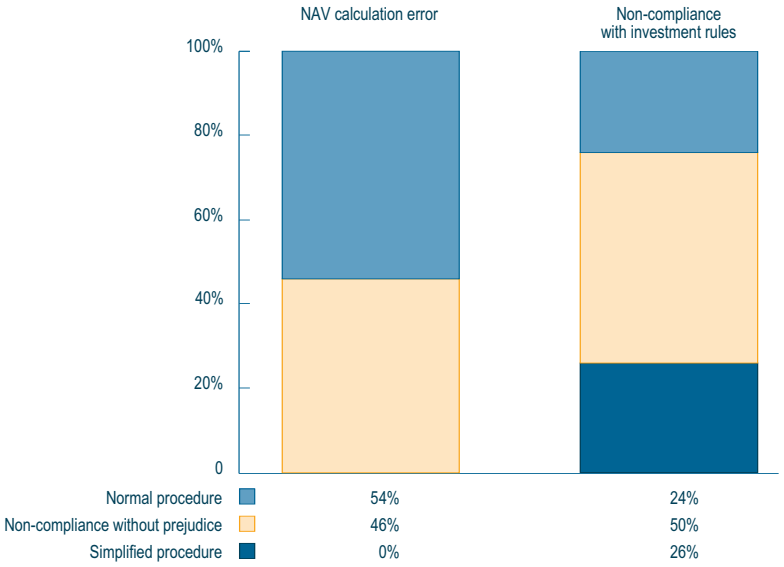
Indeed, circular CSSF 02/77 introduced a simplified procedure for cases of NAV calculation error or non-compliance with investment rules that entail losses for the UCI, where the indemnification amount does not exceed EUR 25,000 and the amount to be reimbursed to an investor does not exceed EUR 2,500.

In this event, no corrective action plan needs to be submitted to the CSSF, but the central administration must notify the occurrence of the calculation error or non-compliance to the CSSF and take the measures necessary to correct the calculation error or non-compliance and arrange the indemnification of the damages occurred. In the course of his annual audit, the external auditor of the UCI must review the correction process. The external auditor must in his report state whether, in his opinion, the process of correction is or is not appropriate and reasonable.

This procedure constituted a substantial change to the circular CSSF 2000/8. Thus, in 2003, 129 cases of the 280 cases of NAV calculation errors, and 131 of the 508 cases of non-compliance with the investment rules could apply the simplified procedure.

The following graph plots the proportion of the cases of simplified procedure compared to the total number of statements.

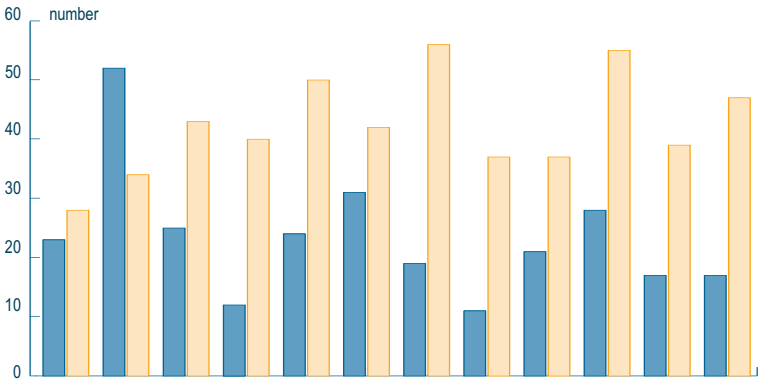
Simplified procedure



Thus, 46% of the statements of NAV calculation errors fall within the scope of the simplified procedure. As regards the cases of non-compliance of investment rules, 26% of the cases meet the criteria of the simplified procedure and 50% of cases could have been regularised without harming the investors.

The following graph sets out in detail the statements made during 2003.

Notified errors in 2003



	Jan.	Feb	Mar.	Apr.	May	June	July	Aug.	Sep.	Oct.	Nov.	Dec.
NAV calculation errors	23	52	25	12	24	31	19	11	21	28	17	17
Non-compliance with investment rules	28	34	43	40	50	42	56	37	37	55	39	47

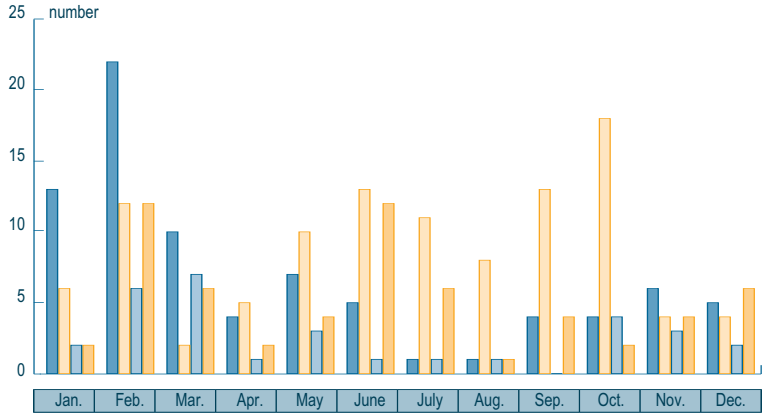
There was a higher number of statements during the months of February, May, June, July and October 2003.

With regard, more particularly, to statements made in relation to non-compliance with investment rules, a significant increase in number was observed for the months of May, July and October 2003.

NAV calculation errors are due to four different causes: pricing errors, booking errors, errors in the calculation of costs and accruals and other errors, for example, in the valuation of swaps and futures.

The following graph plots the different cases of NAV calculation errors recorded in 2003.

Reasons for NAV calculation errors in 2003



	Jan.	Feb.	Mar.	Apr.	May	June	July	Aug.	Sep.	Oct.	Nov.	Dec.
Pricing errors	13	22	10	4	7	5	1	1	4	4	6	5
Booking errors	6	12	2	5	10	13	11	8	13	18	4	4
Errors in costs and accruals	2	6	7	1	3	1	1	1	0	4	3	2
Others	2	12	6	2	4	12	6	1	4	2	4	6

In 2003, 29% of NAV calculation errors were due to pricing errors, 32% to booking errors and 17% to calculation errors in costs and accruals. Among the other causes of error were problems linked to securities operations, representing 4% of cases reported and errors in the valuation of swaps and futures accounting for 6% of the NAV calculation errors.

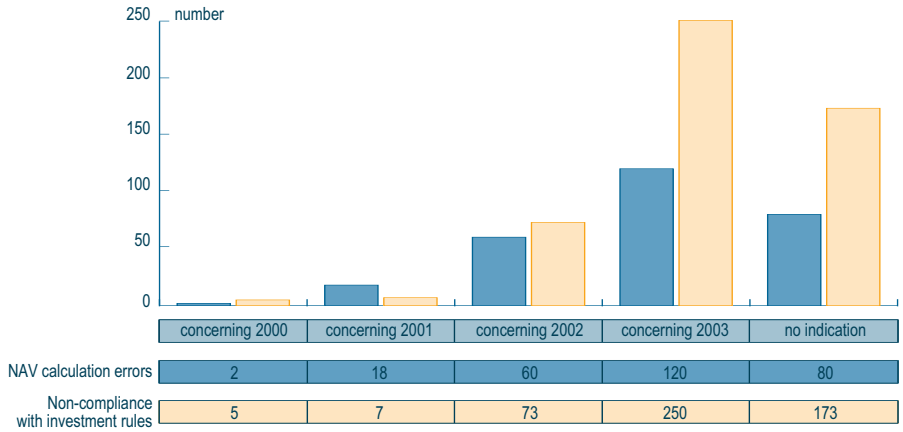
The following table shows the development of the cases of NAV calculation errors since the coming into force of circular CSSF 2000/8 of 15 March 2000 repealed by circular CSSF 02/77 of 27 November 2002.

Development of the causes of NAV calculation errors over the last four years

Over the last four years, booking errors and errors in the valuation of securities held by UCIs were the main causes for NAV calculation errors. The number of errors relating to the determination of costs and accruals continues to rise. Moreover, it is particularly noteworthy that the number of errors due to transactions on securities decreased substantially.

It should be noted that statements made during 2003 do not relate exclusively to errors and instances of non-compliance that occurred during 2003. Thus, they may also relate to errors or instances of non-compliance detected in 2003, but which relate to errors or instances of non-compliance that occurred before the start of the year, as shown in the graph below.

Statements made during 2003



Out of 788 statements made in 2003, 1% and 3% respectively were related to errors or instances of non-compliance that had occurred in 2000 or 2001. 17% concerned errors or instances of non-compliance which have occurred in 2002 and 47% of statements related to errors or instances of non-compliance that had actually occurred in 2003.

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

The table below sets out the amounts of compensation notified in 2002 and 2003. It has to be noted that it is based on data available to the CSSF as at 31 December 2002 and 31 December 2003 respectively, while the amount of compensation had not yet been notified in certain cases.

	Compensation following NAV miscalculation			
	Investors		*UCI/Subfund*	
	2002	*2003*	*2002*	*2003*
EUR	1,327,002.72	758,417.22	2,521,755.19	1,164,859.50
USD	2,467,574.06	1,599,307.08	942,618.93	1,388,746.56
JPY	6,281,672.68	6,322,973.00	543,104.00	1,240,052.83
GBP	-	722.28	-	-
CHF	7,797.38	-	9,688.37	-
Other currencies*	38.09	-	3,961.39	808.25
Total (in EUR**)	3,735,892.66	2,072,540.61	3,435,598.79	2,274,412.65

	Compensation following non-compliance with investment rules			
	Investors		*UCI/Subfund*	
	2002	*2003*	*2002*	*2003*
EUR	389,419.10	73,356.74	1,386,888.57	320,566.54
USD	44,979.23	28,328.94	356,229.72	774,209.75
JPY	-	-	-	1.234,205.00
GBP	-	1,171.29	1,299.50	182.81
CHF	-	1,337.84	22,110.15	6,300.00
Other currencies*	220.16	-	866.07	225.08
Total (in EUR**)	432,529.75	98,307.89	1,744,662.65	947,227.15

* converted in EUR at the exchange rate applying on 31 December 2003 and 31 December 2002 respectively
** exchange rate as at 31 December 2003 and 31 December 2002 respectively

With regard to the 508 instances of non-compliance with investment rules, 255 have been regularised resulting in a profit, while 80 regularisations led to a loss. In 173 instances of non-compliance, the amount realised in the context of regularising operations has not yet been communicated.

As compared to 2002, the amounts of compensation paid following NAV calculation errors continued to decrease. The most important fall (-77%) has been recorded for compensation paid to investors due to instances of non-compliance with investment rules. This development can be explained notably as follows:

- control of investment rules has been reinforced, resulting in a faster detection of instances of non-compliance and shorter periods of non-compliance;
- fewer movements on subscriptions and redemptions of units/shares in the periods during which NAV was incorrect; consequently the amounts of compensation paid to investors and/or UCIs can be not very important even if the period of non-compliance lasts several weeks.

7.4.3. Management letters

Chapter P of Circular IML 91/75 dated 21 January 1991 states that UCIs must automatically and immediately communicate to the CSSF the management letters issued by external auditors in the context of the audits which the latter are obliged to undertake pursuant to Article 89 of the law of 30 March 1988 as amended.

The analysis below sets out data for the year 2002, since these are more pertinent.

The majority of management letters, namely 71.3%, are management letters that contain no recommendations, i.e. the external auditor has not detected any irregularities in the management of the UCIs. 28.7% are management letters with recommendations by which the external auditors have reported irregularities of various types.

With regard to management letters with recommendations, the irregularities determined by external auditors may be broken down into four main categories: overstepping of statutory or regulatory limits, NAV calculation errors, non-compliance with investment policy and problems in the organisation of UCIs.

During the course of 2002, 60% of management letters described instances of exceeding investment limits whilst 40% of irregularities came under the other aforementioned categories.

In this context, it should be noted that some major errors or instances of non-compliance considered "active" that have been reported in management letters, have also been the subject of a statement in accordance with circular CSSF 2000/8 or circular CSSF 02/77.

Moreover, numerous instances of overstepping investment limits reported in management letters could be considered as "passive." With regard to NAV calculation errors, some did not exceed the materiality thresholds laid down in the aforementioned circular.

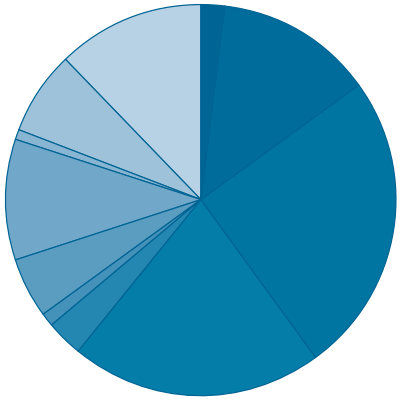
Certain management letters (8%) also contained details concerning the simplified procedure.

UCIs governed by Part I of the law of 30 March 1988 as amended represented 62.1% of Luxembourg UCIs. Insofar as statutory restrictions applying to them are tighter than those applicable to UCIs falling within the scope of Part II, it may be useful to analyse the nature of the limits which they exceed.

The following diagram sets out a breakdown of the statutory limits most frequently exceeded by UCIs governed by Part I of the law of 30 March 1988 as amended.

Nature of limits exceeded by UCIs governed by Part I of the law of 1988 as amended

art. 40(2)	2%
art. 40(4)	13%
art. 42(1) - 10%	25%
art. 42(1) - 40%	21%
art. 42(2)	3%
art. 42(3)	1%
art. 43(1)	5%
art. 44	10%
art. 45	1%
art. 47(2)	7%
chapter H circular IML 91/75	12%



The management letters mainly revealed cases where the statutory limits were exceeded as defined in Article 42(1) of the law of 30 March 1988 as amended, i.e. in 46% of cases. This article stipulates that an undertaking for collective investment in transferable securities (UCITS) cannot invest more than 10% of its assets in transferable securities of the same issuer and that the total value of transferable securities held by the UCITS of issuers in which it invests more than 5% of its assets must not exceed 40% of the value of the assets of the UCITS. Even though these limits are still frequently exceeded, a decrease of 8% as compared to 2001 has to be noted.

Compared with 2001, there has been an increase of 3% in cases of overstepping the limit set by Articles 40(4) and 44 and chapter H of circular IML 91/75. With regard to the other limits, the percentage of cases recorded has remained relatively constant.

CHAPTER IV

SUPERVISION OF PENSION FUNDS

1. Developments in the pension funds sector in 2003
2. Developments in the legal framework

1. Developments in the pension funds sector in 2003

1.1. Pension funds

During 2003, the CSSF authorised three pension funds subject to the law of 8 June 1999 as amended: two pension savings associations (assep) and one pension savings company with variable capital (sepcav):

- ERNST & YOUNG – LOMBARD INTERNATIONAL PENSION SCHEME, constituted in the legal form of a multiple compartment sepcav, was created on the initiative of Ernst & Young S.A., Ernst & Young Tax Advisory Services S.à r.l., Ernst & Young Business Advisory Services S.à r.l., Ernst & Young Resources S.à r.l., Ernst & Young Luxembourg S.A. and Monnet Professional Services S.à r.l.. Its purpose is to organise a pension fund for the employees of the Ernst & Young group in Luxembourg.

- FONDS DE PENSION DU GROUPE SIEMENS A LUXEMBOURG, constituted in the legal form of an assep, was created on the initiative of Groupe Siemens à Luxembourg with the purpose of organising a pension fund for its employees.

- LUXEMBOURG PENSION FUND, constituted in the legal form of a multiple compartment assep, has been created on the initiative of Banque de Luxembourg S.A. and its purpose is to organise a multi-employer pension fund.

The authorisation of these new pension funds raises the number of pension funds subject to the law of 8 June 1999 as amended to ten as at 31 December 2003.

It has to be noted that the growth rate of the pension fund sector is very slow. Half a dozen applications for approval are currently being processed, half of which being pension funds reserved for Luxembourg employers, the others being pension funds designed for international groups.

The impending creation of a single internal market for institutions for occupational retirement provision will hopefully facilitate the setting-up of pan-European pension funds in the medium term. The CSSF expects activities to continue their slow but ongoing pace in 2004.

1.2. Liability managers

Following the registration during 2003 of BÂLOISE VIE Luxembourg S.A., FORTIS LUXEMBOURG-VIE S.A. and HEWITT BACON & WOODROW LIMITED, United Kingdom, on the official list of professionals authorised to act as liability managers for pension funds subject to the law of 8 June 1999 as amended, the number of liability managers of pension funds approved by the CSSF amounted to eleven as at 31 December 2003.

2. Developments in the legal framework

In 2003, no changes have been made to the Luxembourg legal framework regarding sepcavs and asseps.

On an international level, the year 2003 was marked by the adoption of Directive 2003/41/EC of the European Parliament and of the Council of 3 June 2003 on the activities and supervision of institutions for occupational retirement provision, published in the Official Journal of the European Union of 23 September 2003 No. L 235.

The purpose of the Directive is to:

- create a harmonised prudential framework for the taking-up and pursuit of activities of institutions for occupational retirement provision;

- allow institutions for occupational retirement provision to freely provide their services to companies located in other Member States thanks to the mutual recognition of prudential standards and co-operation mechanisms between competent authorities of the home (where the institution is located) and host (where the company paying contributions is located) Member States.

While the original proposal of the European Commission dates back to October 2000, the Ecofin Council was able to reach an agreement on 13 May 2003 on the Directive on the activities and supervision of institutions for occupational retirement provision as it had been adopted on 12 March 2003 at second reading by the European Parliament. Indeed, the Council accepted all thirteen amendments voted by the European Parliament.

The amendments of the European Parliament notably aimed at emphasising the important role of the institutions for occupational retirement provision to ensure financial cover for retirement and to strengthen the requirements as regards information for members and beneficiaries. They also provide that the European Commission examines the opportuneness to extend the optional application of the Directive to occupational retirement activities performed by other regulated financial institutions. As regards prudential requirements applicable to institutions for occupational retirement provision, the amendments of the European Parliament left the provisions of the Council's common position unchanged.

As soon as the Directive was adopted in June 2003, the works to transpose the Directive into national law began in order to adapt the legal framework applicable to pension funds governed by the law of 8 June 1999 creating pension funds in the form of pension savings companies with variable capital (sepcav) or pension savings associations (assep) as amended to the provisions of Directive 2003/41/EC.

The deadline for the transposition of the Directive into national law is set to 24 months from the date of its publication in the Official Journal of the European Union. Hence, the necessary legislative, regulatory and administrative provisions to comply with the Directive must come into effect on 23 September 2005 at the latest.

2.1. Prudential framework applicable to institutions for occupational retirement provision

The prudential framework introduced by the Directive is very similar to the approach adopted by the law of 8 June 1999 as amended. It imposes a permanent prudential supervision and requires that the institutions for occupational retirement provision hold sufficient assets to cover their commitments. The Directive introduces a certain number of mostly qualitative rules for the calculation of technical provisions, as well as for the definition of investment rules. It also introduces a requirement for additional assets where the institution itself, and not the sponsoring undertaking or a financial institution, covers the biometric risks or guarantees a performance or certain benefits.

The approach of the Directive for the **calculation of technical provisions** is of a qualitative nature. Technical provisions should be calculated on the basis of recognised actuarial methods and certified by an actuary. The minimum amount of technical provisions should be sufficient for both ongoing benefits to continue to be paid to beneficiaries and to reflect the commitments that arise out of members' accrued pension rights. The economic and actuarial assumptions shall also be chosen prudently, taking account, if applicable, of an appropriate margin for adverse deviation. The interest rate shall be carefully determined by taking into account the return of the corresponding assets held by the institution, as well as the future investment return and/or the yields of high-quality or government bonds. The biometric tables shall be appropriately chosen with regard to the main characteristics of the pension scheme.

The Directive also adopts a mainly qualitative approach to the **investment rules** and which provides that the management of the assets must meet principles of security, quality, liquidity, profitability and diversification. The assets must be invested prudently and in accordance with the commitments made by each fund. The sole quantitative limit concerns the self-investment in the sponsoring undertaking (employer). The Directive sets a ceiling of 5% of the portfolio for investments in the sponsoring undertaking, as well as a ceiling of 10% of the portfolio for investments in the group to which this undertaking belongs, to avoid that the bankruptcy of the sponsoring undertaking has the double effect of depriving the employees of their jobs and jeopardising their pension rights.

The Member States have the possibility to submit the institutions for occupational retirement provision established within their jurisdiction to more detailed investment rules, but must allow these institutions in any case to invest at least 70% of their technical provisions or of their portfolio in shares and corporate bonds and at least 30% in assets denominated in currencies other than those in which the liabilities are expressed.

Finally, the Directive allows the host Member State to require the home Member State to apply certain quantitative rules to assets held by cross-border pension schemes, on the condition that the host Member State applies the same or more stringent rules to its own institutions for occupational retirement provision. These quantitative rules concern investments in assets that are not admitted to trading on a regulated market, investments in assets from the same undertaking or the same group of undertakings and assets denominated in currencies other than those in which the liabilities are expressed.

As regards **minimum funding requirements**, the Directive provides, as a general rule, that the technical provisions be fully covered at any moment by appropriate assets. However, as institutions for occupational retirement provision hold very long-term investments and have low liquidity risks, the Member States can authorise them, for a limited period of time, to depart from this obligation of full funding. Any deviation must be accompanied by a proper plan to restore full funding of the technical provisions. In case of cross-border activities on the territory of another Member State, the technical provisions must be fully funded at any time.

2.2. Freedom to provide services in other EU Member States

The Directive introduces the right for institutions for occupational retirement provision to freely provide their services to undertakings located in other Member States; it also obliges Member States to authorise their undertakings to sponsor institutions for occupational retirement provision set up in other Member States.

It provides a legal basis for notification and co-operation mechanisms between competent authorities regarding cross-border management of pension schemes by the institutions for occupational retirement provision.

Whereas the institutions for occupational retirement provision currently operate mainly in the Member State where they are established, an institution for occupational retirement provision can, following the implementation of the Directive, manage the schemes of companies established in other Member States by applying the prudential regulations of the Member State where it is established. The Directive provides that the social and labour legislation of the host Member States applicable to the relationship between the sponsoring undertaking that contributes to the institution for occupational retirement provision and the members will continue to apply.

Consequently, Luxembourg pension funds will be able to freely provide their services to sponsoring undertakings in other Member States in future and the other Member States must allow their undertakings to use sepcavs and asseps to manage their pension schemes.

CHAPTER V

SUPERVISION OF THE OTHER PROFESSIONALS OF THE FINANCIAL SECTOR

1. Developments in 2003 of the other professionals of the financial sector (PFS) subject to the permanent supervision of the CSSF
2. Prudential supervisory practice
3. Developments in the regulatory framework

1. Developments in 2003 of the other professionals of the financial sector (PFS) subject to the permanent supervision of the CSSF

This section and the published official statistics only examine PSF subject to the prudential supervision of the CSSF, i.e.:

- Luxembourg-registered PFS (activities conducted by these establishments in another EU Member State, either by means of the establishment of a branch or by free provision of services, are also subject to the prudential supervision of the CSSF);

- branches of investment firms originating from countries outside the EU;

- branches of PFS other than investment firms originating from a EU Member State or from a country outside the EU.

Branches established in Luxembourg by investment firms originating from another EU Member State fall under the supervision of their home state.

The law of 2 August 2003 amending the law of 5 April 1993 on the financial sector subjects the entire financial sector to a prudential supervision. Thus, PFS governed by the general provisions of the law of 5 April 1993 on the financial sector as amended, as well as the professionals carrying out an activity of debt recovery and those executing cash-exchange transactions, are henceforth also under the supervision of the CSSF.

1.1. Developments in the number of the other professionals of the financial sector

The year 2003 is characterised by a slight decrease in the number of PFS subject to the permanent supervision of the CSSF as compared to the year 2002, the number of PFS having indeed dropped from 145 entities at the end of 2002 to 142 entities as at 31 December 2003. This decrease is consistent with the overall slowdown of activities in the financial sector. The number of newly approved companies in 2003 falls slightly as compared to the number of entities that had been approved in the previous year. Eleven companies have been approved in 2003 as PFS (against ten in 2002), while fourteen entities renounced their status during the same period.

Developments in the number of PFS

Categories	1995	1996	1997	1998	1999	2000	2001	2002	2003
Investment firms									
Commission agents				4	7	10	14	15	17
(Brokers and commission agents)	14	14	14	/	/	/	/	/	/
Private portfolio managers	33	36	34	37	38	46	51	51	48
Professionals acting for their own account	18	18	20	15	17	14	17	16	16
Distributors of units/shares of investment funds	19	20	18	22	25	35	43	45	47
Underwriters				1	2	4	4	3	3
(Underwriters and market makers)	3	3	3	/	/	/	/	/	/
Professional custodians of securities	3	3	3	1	1	3	4	3	3
Registrar and transfer agents									1
PFS other than investment firms									
Financial advisors	6	6	7	9	10	9	10	9	9
Brokers				10	8	7	6	6	5
Market makers				1	2	2	2	2	2
PFS performing a connected or complementary activity of the financial sector									
Domiciliation agents of companies					1	14	32	36	34
Client communication agents									2
IT systems and communication networks operators of the financial sector									1
Institutions authorised to conduct all the PFS activities permitted by article 28 of the Law of 15 December 2000 on postal services and financial postal services							1	1	1
Total[1]	**78**	**82**	**80**	**83**	**90**	**113**	**145**	**145**	**142**

[1] The total in the table is not equal to the arithmetic sum of all the categories mentioned because an institution may be included in several categories.

Note on PFS registered on the official list:
As the official table of PFS posted on the CSSF Internet site, this table, under the company domiciliation agent heading, only includes companies that have been approved exclusively as company domiciliation agents under article 29 of the law of 5 April 1993 on the financial sector as amended. Entities authorised to exercise, in addition to the status of domiciliation agent, another PFS activity covered by Chapter 2 of Part 1 of the aforementioned law are included in this category, since approval obtained as other professional of the financial sector also authorises the provision of company domiciliation services in accordance with the law of 31 May 1999 on company domiciliation.

This table does not yet include the PFS that do not fall under a specific category and that are subject to the general provisions of the law of 5 April 1993 as amended, as the companies concerned have not yet taken the necessary steps to comply with the provisions introduced by the law of 2 August 2003 and whose time limit to comply expires on 31 March 2004. It has to be noted that the number of these entities has not changed in 2003.

The number of domiciliation agents of companies and private portfolio managers decreased, if only slightly, as opposed to the positive development in the previous years. No authorisation as new private portfolio manager has been granted in 2003.

The categories of registrar and transfer agents, client communication agents and IT systems and communication networks operators of the financial sector have been introduced by the law of 2 August 2003 amending the law of 5 April 1993 on the financial sector, which came into effect on 1 October 2003.

Moreover, the law introduced the following new categories:
- professionals performing credit offering;
- professionals performing securities lending;
- professionals performing money transfer services;
- administrators of collective savings funds;
- management companies of non-coordinated UCIs;
- administrative agents of the financial sector;
- professionals performing services of setting up and of management of companies.

As at 31 December 2003, no authorisation has been granted for any of the new categories, except for the companies registered on the official list in a category fully empowered to carry out the activities of a newly created category.

Breakdown of PFS by geographic origin

	1995	1996	1997	1998	1999	2000	2001	2002	2003
Belgium	26	29	27	25	24	21	22	22	18
France	9	11	10	10	10	11	14	13	9
United Kingdom	8	9	10	9	8	8	9	10	11
Switzerland	6	5	6	4	4	7	11	10	10
Luxembourg	8	8	11	12	17	22	31	31	32
Germany	8	6	6	6	7	11	11	10	10
United States	5	6	3	4	3	4	8	8	8
Netherlands	1	2	2	3	3	7	12	15	15
Others	7	6	5	10	14	22	27	26	29[2]
Total	**78**	**82**	**80**	**83**	**90**	**113**	**145**	**145**	**142**

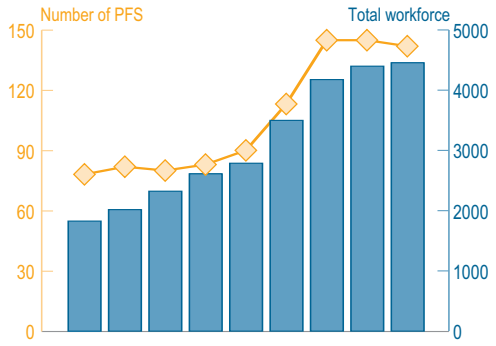
[2] Including Italy (3 entities), Sweden (3 entities), Denmark (4 entities).

PFS originating from Belgium and France each decreased by four entities, which can be connected with the fall in the number of private portfolio managers. It is noteworthy that PFS originating from Luxembourg remained the most numerous.

1.2. Development in employment of the other professionals of the financial sector

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

Year	Number of PFS	Total workforce
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



The analysis of employment in 2003 reveals a rather weak growth of the total workforce as compared to the previous years. Indeed, employment increases only 1.28% as compared to 31 December 2002. However, it has to be noted that the employment of other professionals of the financial sector developed positively although the number of PFS slightly decreased compared to the previous year.

Overall, the increase in employment from 4,399 persons as at 31 December 2002 to 4,455 persons as at 31 December 2003 can be explained on the one hand by newly approved PFS, which employ noticeably more personnel than those entities having renounced their status in 2003, and on the other hand by an increase in personnel employed by entities active in the distribution of units/shares of investment funds.

The year 2003 can be subdivided into two contrasting periods in terms of development in numbers.

Indeed, the total workforce fell during the first half of 2003 to 4,243 persons as at 30 June 2003 against 4,399 persons at the end of the previous year. This decrease is essentially due to certain institutions with a high number of staff which changed their legal status into that of management company of UCIs.

A reversal of the situation took place during the second half of 2003. Thus, the workforce employed by the other professionals of the financial sector increased from 4,243 persons as at 30 June 2003 to 4,455 persons at the end of the year. This positive development partly results from the authorisation of new establishments, but also from the increase in employment of certain entities active in the distribution of units/shares of investment funds.

1.3. Changes in 2003 in the official list of PFS

1.3.1. Luxembourg-registered PFS approved in 2003

- ***Investment firms***

According to chapter 2, section 2 of Part I of the law of 5 April 1993 on the financial sector as amended, the following are considered as investment firms: companies acting on a professional basis as commission agents (article 24A), private portfolio managers (article 24B), professionals acting for their own account (article 24C), distributors of units/shares of investment funds (article 24D), underwriters (article 24E), professional custodians of securities or other financial instruments (article 24F) or registrar and transfer agents (article 24G). An application for authorisation may relate to one or more of the categories mentioned.

The following institutions were approved as investment firms in 2003:

Name of PFS	Category
Barclays International Independent Financial Advisory Services S.A.	Commission agent
E. Oppenheimer & Son (Luxembourg) Ltd	Commission agent[3]
European Fund Services S.A.	Registrar and transfer agent, commission agent and distributor of units/shares of investment funds[3]
IKB CorporateLab S.A.	Professional acting for his own account
Nextra Distribution Services S.A.	Distributor of units/shares of investment funds

Five entities were approved as investment firms in 2003, including one entity that applied for approval for three different investment firm statuses, i.e. as commission agent, distributor of units/shares of investment funds and registrar and transfer agent.

Two entities were also approved as domiciliation agents of companies and one entity as IT systems and communication networks operator of the financial sector and are therefore listed as PFS carrying out an activity connected or complementary to the financial sector.

Combining several statuses allows a company to offer a broader range of services to its clients and to better adapt to temporary economic difficulties.

- ***PFS other than investment firms***

According to the provisions of articles 25 to 28-8 of the law of 5 April 1993 on the financial sector as amended, financial advisors (article 25), brokers (article 26), market makers (article 27), operators of payment or securities settlement systems (article 28-1), persons performing cash-exchange transactions (article 28-2), debt recovery (article 28-3), professionals performing credit offering (article 28-4), professionals performing securities lending (article 28-5), professionals performing money transfer services (article 28-6), administrators of collective savings funds (article 28-7) and management companies of non-coordinated UCIs (article 28-8) constitute PFS other than investment firms.

[3] Also refer to the table of PFS performing an activity connected or complementary to the financial sector.

Only one entity was approved as PFS other than investment firms in 2003:

Name of PFS	Category
Bellatrix Investments S.A.	Financial advisor

It has to be noted that as at 31 December 2003, no application for approval has been requested for PFS categories other than investment firms newly created by the law of 2 August 2003.

Definition of the activity of independent intermediaries
The CSSF considers that the introduction, by a natural or legal person residing in Luxembourg, of customers to a professional of the financial sector, has to be considered as establishing a relationship between both parties with a view to agree on a specific financial transaction. The activity carried out by the interemdiary in or from Luxembourg therefore requires an authorisation as broker as laid down in article 26 of the law of 5 April 1993 on the financial sector as amended.

- ***PFS performing a connected or complementary activity to the financial sector***

According to the provisions of articles 29 to 29-4 of the law of 5 April 1993 on the financial sector as amended, domiciliation agents of companies (article 29), client communication agents (article 29-1), administrative agents of the financial sector (article 29-2), IT systems and communication networks operators of the financial sector (article 29-3) and professionals performing services of setting up and of management of companies (article 29-4) are PFS performing a connected or complementary activity to the financial sector.

Name of PFS	Category
AIB Administrative Services Luxembourg S.à.r.l.	Domiciliation agent of companies
E. Oppenheimer & Son (Luxembourg) Ltd	Domiciliation agent of companies[4]
European Fund Services S.A.	Domiciliation agent of companies and IT systems and communication networks operator of the financial sector[4]
Lettershop S.A.	Client communication agent
LGT Trust & Consulting S.A.	Domiciliation agent of companies
Victor Buck Services S.A.	Client communication agent

[4] Also refer to the table of investment firms.

In 2003, four entities were authorised as domiciliation agents of companies.

As far as the new statuses introduced by the law of 2 August 2003 are concerned, three entities were approved as client communication agents, one of them being listed on the official list of investment firms as registrar and transfer agent fully empowered to carry on the activities of administrative agent of the financial sector and client communication agent. One entity was authorised to act as IT systems and communication networks operator of the financial sector.

The relatively weak number of entities having submitted an application the be authorised to carry on one of the activities introduced by the law of 2 August 2003 is, on the one hand, due to the fact that the law came into force only on 1 October 2003, and on the other hand to the fact that the time limit to comply with the law granted to persons who carried on, when the law came into force, an activity subject to a new status, only expires on 31 March 2004.

Interpretation of the concept of financial advisor
The definition of the activities of financial advisors has been specified so that the persons, who, on an individual basis, provide general financial advice, also fall under the scope of article 25 of the law on the financial sector. Until now, article 25 only concerned the persons who provided, on an individual basis, advice on specific financial transactions.

1.3.2. PFS that renounced their status in 2003

Ten entities, including five investment firms, renounced their PFS status in 2003. Three PFS have merged with their parent company or another entity of the group to which they belong. Besides the liquidation of one entity, the other renouncements were all due to discontinuation of activities or change in activities no longer requiring an authorisation as PFS, as the activities no longer fall under the scope of the law of 5 April 1993 on the financial secto as amended.

Moreover, the Minister responsible for the CSSF has withdrawn the approval of one entity upon the CSSF's request, as the PFS concerned no longer fulfilled the necessary conditions of approval.

Name of PFS	Category	Reason for renouncement
BBL Trust Services Luxembourg	Domiciliation agent of companies	Merger with ING Trust (Luxembourg) S.A.
Beta Europa Management S.A.	Professional acting for his own account	Ceased its PFS activities
BNP Fund Administration S.A.	Distributor of units/shares of investment funds	Ceased its PFS activities
Crédit Lyonnais Asset Management (Luxembourg) S.A.	Commission agent and distributor of units/shares of investment funds	Ceased its PFS activities
Cogent Investment Operations Luxembourg S.A.	Domiciliation agent of companies	Merger by take-over with BNP Paribas Fund Services
Degroof, Thierry, Portabella & Associés S.A.	Private portfolio manager and distributor of units/shares of investment funds	Merger with Banque Degroof Luxembourg S.A.

F.G.P. (Luxembourg) S.A.	Financial advisor	Ceased its PFS activities
Graham Turner Trust Services (Luxembourg) S.A.	Domiciliation agent of companies	Ceased its PFS activities
Havaux Gestion (Luxembourg) S.A.	Private portfolio manager	Voluntary liquidation
Infigest S.A.	Domiciliation agent of companies	Ceased its PFS activities
LISSA-Luxembourg Investment Strategies S.A.	Commission agent	Withdrawal of approval

1.3.3. Changes in category in 2003

The analysis of changes in the categories of the professionals of the financial sector in 2003 confirms the diversification of market activities. Most of the requested changes relate to the adoption of an additional status with a view to expanding the business covered.

Name of PFS	Category (before change)	Category (after change)
Alternative Leaders S.A.	Private portfolio manager	Private portfolio manager and distributor of units/shares of investment funds not authorised to accept and effect payments
European Fund Services S.A.	Commission agent, distributor of units/shares of investment funds not authorised to accept and effect payments and domiciliation agent of companies	Commission agent and distributor of units/shares of investment funds not authorised to accept and effect payments, domiciliation agent of companies, IT systems and communication networks operator of the financial sector and registrar and transfer agent
Fidessa Asset Management S.A.	Private portfolio manager	Private portfolio manager and distributor of units/shares of investment funds not authorised to accept and effect payments
Franklin Templeton International Services S.A.	Distributor of units/shares of investment funds authorised to accept and effect payments	Distributor of units/shares of investment funds authorised to accept and effect payments and commission agent
Keytrade Luxembourg S.A.	Broker	Commission agent and auxiliary service point 7 of section C of annexe II of the law of 5 April 1993 on the financial sector as amended
Kredietrust Luxembourg S.A.	Private portfolio manager	Private portfolio manager and distributor of units/shares of investment funds authorised to accept and effect payments

1.4. Development in the balance sheet totals and results

Development in the balance sheet total of PFS

CATEGORIES	Balance sheet total in EUR		
	2001	2002	2003[5]
Investment firms			
Commission agents	101 666 465	147 610 385	165 509 334
Private portfolio managers	866 060 509	823 033 277	903 461 433
Professionals acting for their own account	261 465 164	195 589 363	270 166 720
Distributors of units/shares of investment funds	810 254 091	778 601 009	919 379 123
Underwriters	139 269 208	55 453 654	107 130 510
Professional custodians of securities or other financial instruments	818 743 262	847 861 986	998 633 250
Registrar and transfer agents	/	/	1 595 044
PFS other than investment firms			
Financial advisors	8 327 976	8 548 297	11 303 419
Brokers	53 352 363	45 163 287	43 161 613
Market makers	17 406 945	17 721 824	17 578 705
PFS performing a connected or complementary activity to the financial sector			
Domiciliation agents of companies	72 508 986	82 607 292	108 516 585
Client communication agents	/	/	3 587 059
IT systems and communication networks operators of the financial sector	/	/	1 595 044
Institutions authorised to conduct all the PFS activities permitted by article 28 of the law of 15 December 2000 on postal services and financial postal services	/	/	/
Total	**2 316 353 170**	**2 292 287 619**	**2 546 754 660**

[5] Provisional figures.

Development in the net results of PFS

CATEGORIES	Net results in EUR		
	2001	2002	2003[6]
Investment firms			
Commission agents	5 836 317	1 195 685	6 151 947
Private portfolio managers	149 394 686	151 487 146	152 201 330
Professionals acting for their own account	17 481 305	26 831 928	26 284 405
Distributor of units/shares of investment funds	76 656 488	106 542 893	95 158 301
Underwriters	4 320 486	1 938 609	2 567 253
Professional custodians of securities or other financial instruments	51 089 607	82 936 378	142 812 697
Registrar and transfer agents	/	/	- 484 488
PFS other than investment firms			
Financial advisors	743 640	1 251 178	1 365 051
Brokers	18 339 295	18 056 064	16 298 578
Market makers	984 879	422 867	239 971
PFS performing a connected or complementary activity to the financial sector			
Domiciliation agents of companies	7 706 452	10 032 141	8 321 390
Client communication agents	/	/	833 489
IT systems and communication networks operators of the financial sector	/	/	- 484 488
Institutions authorised to conduct all the PFS activities permitted by article 28 of the law of 15 December 2000 on postal services and financial postal services	/	/	/
Total	**283 518 190**	**320 234 143**	**365 917 699**

[6] Provisional figures.

Comment on the tables

Since the same company may operate in several sectors, the total does not reflect the arithmetical sum of headings under the different PFS categories. For professionals of the financial sector authorised to conduct business as defined in articles 24A to 24D, 24G, 25, 26, 29-1 and 29-2 of the law of 5 April 1993 as amended, the balance sheet total and the net results respectively are recorded only once in the total in the category for which the capital requirements are the most stringent. If the professional conducts additional business outside of the above-mentioned categories, as covered in section 2 of chapter 2 of the aforementioned law, the balance sheet total and total results respectively are aggregated for each category but are not included in the grand total to avoid double counting.

The balance sheet total posted by PFS established in Luxembourg increased during 2003 to EUR 2,546 million, compared to EUR 2,292 million at the end of 2002, representing a net increase of 11.11%. This positive development was mainly due to the development of a few large-sized entities which were able to benefit from the recovery of the stock markets.

PFS net results at 31 December 2003 were also higher than in the previous year, amounting to EUR 365 million as against EUR 320 million at 31 December 2002, representing a growth of 14.27%. Considering the decrease in the total number of authorised PFS, the net results in 2003 thus recorded a notable growth compared to the previous year. This development, which is largely attributable to the increase in the results of commission agents and professional custodians of securities, is consistent with the general improvement of the international economic situation and the recovery of stock markets.

The tables on the development of the balance sheet total and net results reveal that the different categories of PFS posted divergent results in 2003. Certain categories recorded a fall compared to the previous year, while others were more stable or even recorded a significant increase in the balance sheet total and/or net results. Among the PFS categories that recorded a fall in their net results are the distributors of units/shares of investment funds and domiciliation agents of companies, with a decline of 10.69% and 17.06% respectively.

Commission agents

The net results of the commission agents increased substantially as compared to end of 2002. This development is due to the growth in the results of a significant player in this category.

Private portfolio managers

Despite the slight decrease in the number of private portfolio managers during the year 2003, declining from 51 to 48 entities as at 31 December 2003, this category shows a slight increase in the balance sheet total and net results.

Distributors of units/shares of investment funds

Distributors of units/shares of investment funds, the number of which increased from 45 to 47 in 2003, record a decrease in results while the balance sheet total is on the increase as compared to the previous year. A few large-sized market participants were responsible for the financial development of the category distributors of units/shares of investment funds.

Professional custodians of securities or other financial instruments

The table reveals an important increase in net results, which is essentially due to the development of a major player in the market.

Registrar and transfer agents
IT systems and communication networks operators of the financial sector

The entity that falls under these two categories is a new company, which has adopted the statuses of registrar and transfer agent and IT systems and communication networks operator of the financial sector as introduced by the law of 2 August 2003 only in December 2003. The negative net results of these categories are thus not representative.

Domiciliation agents of companies

The balance sheet total of the company domiciliation agents increased while their net results decreased, reflecting the general trend recorded for entities of this category.

1.5. Expansion of PFS at international level

- **Formation of subsidiaries in 2003**

The investment firm Hottinger & Cie, authorised as private portfolio manager, opened a subsidiary in Switzerland in 2003.

- **Freedom of establishment**

Three Luxembourg-registered investment firms established a branch in another EU Member State in accordance with the principle of freedom of establishment in 2003, namely J.P. Morgan Fleming Asset Management (Europe) S.à.r.l. which set up a branch in Germany, Nordea Investment Funds which set up a branch in Austria and SZL S.A. which set up in Belgium by means of a branch.

The company Carl Kiem, on the other hand, closed its branch in Belgium on 31 December 2003.

The following table shows all the Luxembourg investment firms, which are represented by means of a branch in one or several EU Member States as at 31 December 2003.

Name of PFS	Category	Branch
AIG Financial Advisor Services (Europe) S.A.	Distributor of units/shares of investment funds	Germany Italy
Creutz & Partners, Global Asset Management S.A.	Private portfolio manager	Germany
J.P. Morgan Fleming Asset Management (Europe) S.à R.L.	Private portfolio manager and distributor of units/shares of investment funds	Sweden Austria Netherlands Germany
Le Foyer, Patrimonium & Associés S.A.	Private portfolio manager and distributor of units/shares of investment funds	Belgium
Moventum S.A.	Private portfolio manager and distributor of units/shares of investment funds	Germany
Nordea Investment Funds S.A.	Distributor of units/shares of investment funds	Austria
SZL S.A.	Professional acting for his own account	Belgium

SUPERVISION OF THE OTHER PROFESSIONALS OF THE FINANCIAL SECTOR

At 31 December 2003, the number of branches established in Luxembourg by investment firms originating from another EU Member State amounts to four, which is a decrease compared to end of last year, where the number stood at five entities.

A branch originating from the United Kingdom, i.e. GNI Fund Management Limited, stopped its activities in Luxembourg in 2003.

Name of branch	Country of origin
Compagnie de Gestion Privée	Belgium
Morgan Stanley Investment Management Limited	United Kingdom
PFPC International Limited	Ireland
Prudential-Bache International Limited	United Kingdom

- **Freedom to provide services**

In 2003, fourteen Luxembourg-registered investment firms applied to pursue business in one or several EU Member States under the principle of freedom to provide services. The upward trend in preceding years is *de facto* confirmed. It needs to be added that the majority of investment firms concerned pursue business in several other EU countries by means of a notification.

Notifications to freely provide services in Luxembourg from investment firms situated in other EU Member States decreased in 2003, confirming the trend that crystallised in 2002. Indeed, the number of notifications received by the CSSF amounted to 68 as against 105 in 2002.

The geographical breakdown of investment firms that submitted a notification in 2003 shows that British investment firms continue to introduce the most notifications to freely provide services in Luxembourg, followed by the French investment firms.

Country of origin	Number of entities having submitted a notification to freely provide services in 2002	Number of entities having submitted a notification to freely provide services in 2003
Germany	4	1
Austria	4	2
Belgium	4	1
Spain	3	3
Finland	/	1
France	7	13
Greece	2	/
Ireland	11	3
Italy	/	/
Norway	2	/
Netherlands	7	6
United Kingdom	59	37
Sweden	2	1
Total	**105**	**68**

While the geographical breakdown shows a slight decrease for the majority of countries as compared to the previous year, the number of entities originating from France increased by six entities.

The United Kingdom and Ireland recorded a substantial decrease in the number of entities having introduced a notification to freely provide services in Luxembourg, standing at only 37 entities as against 59 for the United Kingdom and at 3 entities as against 11 for Ireland. This decrease in the number of notifications from these two countries is the main reason for the drop in the total number of notifications in 2003 as compared to the previous year.

At 31 December 2003, 965 investment firms of Community origin were authorised to freely provide services on Luxembourg territory.

2. Prudential supervisory practice

2.1. Prudential supervision instruments

Prudential supervision is exercised by the CSSF by means of four types of instruments:

- financial information submitted periodically to the CSSF enabling the continuous monitoring of the activities of PFS and of inherent risks, and the periodic supervision of the capital adequacy ratio as laid down in article 56 of the law of 5 April 1993 on the financial sector as amended;

- the report drawn up annually by the external auditors (including a certificate concerning anti-money laundering and a certificate concerning compliance with CSSF Circular 2000/15);

- internal audit reports relating to inspections carried out during the year, and the management's report on the state of the internal auditing of the PFS;

- on-site inspections carried out by the CSSF.

2.2. On-site inspections

In 2003, the CSSF carried out on-site inspections at the premises of four professionals of the financial sector.

The purpose of these on-site inspections was to control more particularly the functioning of the PFS concerned and to ascertain, among other things, that an adequate administrative and accounting structure is set up.

The CSSF attaches particular importance to this instrument of permanent supervision, which allows a global and direct view of the situation and functioning of the PFS in practice.

Thus, an on-site inspection at the premises of one professional of the financial sector in 2003 led the CSSF to require the entity concerned to renounce its PFS activities due to non-compliance with certain legal provisions. The on-site inspection at the premises of another entity led to CSSF to require the entity concerned to charge an external auditor with controlling a particular aspect of the PFS activities.

2.3. Meetings

A total of 95 meetings concerning PFS activities were held in 2003 at the CSSF's premises. Half of these meetings related to applications for approval as PFS, submitted by firms newly incorporated or to be created, or from existing entities that intend to conduct business in the financial sector that requires prior authorisation.

The remainder of the meetings held with representatives of PFS covered the following areas in particular:

- planned changes in business;
- presentation of the general context and business of the company concerned;
- courtesy visits.

2.4. Specific audits

Article 54(2) of the law of 5 April 1993 on the financial sector as amended specifies that the CSSF can ask external auditors to carry out a specific audit on a financial professional, covering one or several specific aspects of the business or functioning of the entity concerned. The ensuing costs are to be borne by the professional concerned. The CSSF made formally use of this right in one case in 2003.

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 as amended and more particularly by chapter 3bis 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 by the law.

At 31 December 2003, the CSSF had carried out supervision on a consolidated basis on 20 investment firms falling under the above-mentioned law. An in-depth study of the financial groups to which most of the PFS investment firms belong was 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. Many companies that are supervised on a consolidated basis belong to major groups operating in the financial sector and whose ultimate parent company is usually a credit institution.

The following PFS were subject to supervision by the CSSF on a consolidated basis at 31 December 2003:

- ABN Amro Investment Funds S.A.
- Atag Asset Management (Luxembourg) S.A.
- BNP Paribas Fund Services
- Brianfid-Lux S.A.
- Capital @ Work International S.A.
- Citco (Luxembourg) S.A.
- Clearstream International S.A.
- Corluy Luxembourg S.A.
- Crédit Lyonnais Management Services (Luxembourg) S.A.
- Dewaay Luxembourg S.A.
- Dexia Asset Management Luxembourg S.A.
- Foyer Asset Management S.A.
- Fund-Market Research & Development S.A.
- Hottinger & Cie

- Interinvest S.à r.l.
- Kredietrust S.A.
- Le Foyer, Patrimonium & Associés S.A.
- Petercam (Luxembourg) S.A.
- Premium Select Lux S.A.
- UBS Fund Services (Luxembourg) S.A.

3. Developments in the regulatory framework

Circular CSSF 03/113 on practical rules concerning the task of external auditors of investment firms

Circular CSSF 03/113 of 21 October 2003 defines the scope of the auditing mandate of yearly accounting documents, as well as the content of the audit report, as provided for by Article 54 (1) of the law of 5 April 1993 on the financial sector as amended. It applies to all the investment firms and to the branches of non-EU investment firms.

The long-form audit report introduced by the circular, as it exists already for credit institutions, is an important source of information for the management of the financial professional, as well as for the CSSF in its supervisory mission.

The provisions of the circular have to be observed for yearly accounts of the financial years closing after 31 December 2003.

Interpretation of the legal condition for educational qualifications to be held by managers of domiciliation agents of companies (article 29(2) of the law of 5 April 1993 on the financial sector as amended)

The CSSF considers that the requirement concerning the proof of a completed university education in law, economics or business management by the managers of domiciliation agents of companies is fulfilled by any final university degree in these areas, no matter how many years of study this degree awards.

CHAPTER VI

SUPERVISION OF SECURITIES MARKETS

1. Reporting of transactions on financial assets
2. Investigations conducted by the CSSF in its supervision of securities markets
3. Supervisory practice

1. Reporting of transactions on financial assets

1.1. The reporting requirements

The project of the reporting on transactions on financial assets having been finalised in 2002, more attention was paid to the supervision of reporting of transactions on financial assets by investment firms during 2003.

The year 2002 having been marked by the publication of the updated version of the *Recueil d'instructions* and the identification and rectifications of the most frequent mistakes made by the investment firms, stress was laid in 2003 on compliance with the requirements laid down in circular CSSF 99/7 on reporting to the CSSF in accordance with the law of 23 December 1998 on the supervision of securities markets.

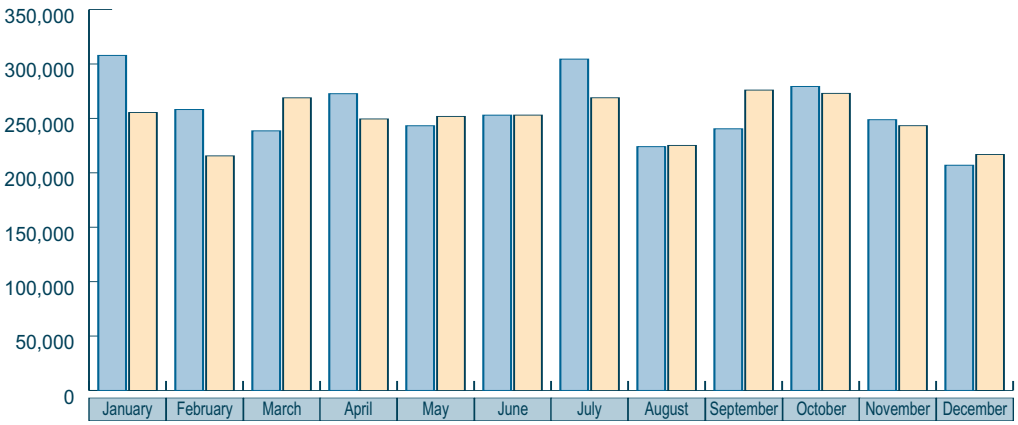
In this context and within the scope of its daily supervisory mission, the CSSF addressed a total of 84 letters covering the following subjects to the investment firms:

Subject	Number
Mailing of the *Recueil* to new firms	7
Various authorisations (reporting via fax, exemptions, deferrals)	8
Reporting irregularities (erroneous quotes, technical issues, quotes deviating from the market, block transactions)	32
Request for explanations	14
Code of ethics	8
Reminders	8
Various	7
Total	**84**

1.2. Development in the number of trades reported

The number of trades reported in 2003 amounted to 2,997,199, representing a decrease of 2.60% as compared to 2002, when the number of trades reported amounted to 3,077,255.

Monthly volume of trades reported



	January	February	March	April	May	June	July	August	September	October	November	December
2002	307,833	258,108	238,550	272,658	243,208	252,958	304,441	224,041	240,440	279,311	248,762	206,945
2003	255,351	215,545	268,896	249,447	251,811	253,014	268,930	225,159	276,001	272,951	243,282	216,812

Breakdown of transactions by type of instrument

Type of instrument	Number of trades reported (as a % of total)	
	2002	2003
Shares	62.12 %	62.19 %
Bonds	34.13 %	33.34 %
Futures	1.27 %	0.99 %
Options	1.20 %	1.77 %
Warrants	1.14 %	1.37 %
Bonds cum warrant	0.14 %	0.34 %

The reported data allows to monitor the trends of the European and more particularly the Luxembourg market. The main purpose of the supervision of the securities markets is to prevent and detect infringements of financial and stock market laws and regulations. In this context, weekly internal reports, as well as specific internal reports, based on the trades reported, are drawn up. These *ex post* analyses of transactions on financial assets are likely to be used as a starting point for enquiries of the CSSF.

2. Investigations conducted by the CSSF in its supervision of securities markets

A distinction should be drawn between investigations conducted into breaches of stock exchange regulations and investigations into non-compliance with the rules of conduct in the financial sector as laid down in circular CSSF 2000/15 of 2 August 2000.

2.1. Investigations into breaches of stock exchange regulations

The CSSF is the administrative authority competent to ensure that the provisions of the law of 3 May 1991 on insider dealing are applied. Its aim is twofold: ensure fair and equal treatment of investors, as well as protection against the illegal use of insider information.

In its supervision of securities markets, the CSSF either initiates enquiries itself or conducts them in response to a request for assistance from a foreign administrative authority within the framework of international co-operation.

2.1.1. Enquiries initiated by the CSSF

- **Enquiries concerning insider dealing**

An enquiry initiated by the CSSF in 2002 into a possible infringement of the law of 3 May 1991 on insider dealing has been closed in 2003 with no further action taken, considering the evidence and information received.

During 2003, the CSSF opened three enquiries into a possible breach of the law of 3 May 1991 on insider dealing. Two enquiries are still in progress. Based on the evidence and information collected in relation to the third enquiry, the CSSF concluded that there were no infringements of the aforementioned law.

- **Enquiries into price manipulation**

The CSSF conducted investigations regarding an enquiry into a possible price manipulation of securities of an international group whose bonds are listed on the Luxembourg Stock Exchange. Based on the analysis of the information received, the CSSF could not conclude that

the price of the listed securities had been manipulated by any fraudulent means and has closed this case without taking any further action.

The CSSF continued its investigations regarding an enquiry opened in 2001 within the scope of its general mission of supervising the securities markets. The purpose of these specific investigations is to verify whether the prices of a security officially listed on the Luxembourg Stock Exchange had been manipulated upwards. Based on the information received, the CSSF could not conclude that the price of the listed security had been manipulated by any fraudulent means and has closed this part of the case without taking any further action.

2.1.2. Enquiries conducted by the CSSF at the request of a foreign administrative authority

- **Enquiries concerning insider dealing**

In 2003, the CSSF processed 51 requests for assistance relating to enquiries into insider dealing (against 55 in 2002), one of which having been filed by an administrative authority outside the European Economic Area.

The CSSF handled all these enquiries with the necessary diligence befitting co-operation between authorities and no major issues relating to the involved financial intermediaries have been raised.

- **Enquiries into price manipulation, fraudulent public offers, breaches of the requirement to report major shareholdings and other breaches of the law**

The CSSF received three applications for assistance from foreign authorities (one of which from an administrative authority outside the European Economic Area) regarding price manipulation, two applications (one of which from an administrative authority outside the European Economic Area) regarding fraudulent public offers of securities, five applications (two of which from an administrative authority outside the European Economic Area) regarding breaches of the requirement to report major shareholdings, two applications regarding non-compliance with the rules of conduct, two requests (one of which from an administrative authority outside the European Economic Area) regarding illegal practice of activity of the financial sector, one application regarding false information in the prospectus published in relation with a capital increase and one request regarding breaches of the stock market legislation.

The CSSF responded to all these requests within the scope of its legal competence. The CSSF could not respond favourably to one application concerning a request regarding accounting information on a company affiliated to a company listed in a non-EEA country, as the requested information falls outside the competence of the CSSF.

2.2. Enquiries into non-compliance with the rules of conduct in the financial sector

Circular CSSF 2000/15 concerning the rules of conduct of the professionals of the financial sector aims to ensure investor protection and market integrity. In this context, the CSSF intervened eight times in 2003 with financial institutions members of the Luxembourg Stock Exchange to make them aware of their duties as regards deontology, notably to ensure compliance with the rules of conduct.

The CSSF's interventions were mainly motivated by the will to protect investors. The decision to open an investigation or to intervene with a professional of the financial sector is based on analytical reports of daily trading activity on the Luxembourg Stock Exchange, as well as on the analysis of trades reported to the CSSF. The CSSF then analyses this information and decides on the appropriateness of an intervention.

3. Supervisory practice

In accordance with the law of 23 December 1998 on the supervision of securities markets as amended, the CSSF supervises stock exchanges and carries out supervisory functions related to public offers and listed Luxembourg companies.

3.1. Supervision of stock exchanges

The establishment of a stock exchange in Luxembourg is subject to a concession to be granted by a grand-ducal decree. The only stock exchange currently licensed under Luxembourg law is the *Société de la Bourse de Luxembourg* (Luxembourg Stock Exchange). The CSSF monitors the proper functioning of the securities market, as well as the proper application of the related regulations. The CSSF also attends the meetings of the Luxembourg Stock Exchange authorities.

3.1.1. Regulatory changes

In its 2002 Annual Report, the CSSF indicated that a high number of application files received in 2002 were related to structured issues, whose proceeds are entirely or partly invested in funds not subject to a permanent supervision in their home country. This trend has been confirmed in 2003.

In this context, it must be stressed that the CSSF's decision not to agree to the listing of structured financial instruments linked to foreign UCIs which are not subject to a supervision in their home country, is based on the decision of the Government in Council of 4 March 1988 concerning the admission to the Luxembourg Stock Exchange of foreign UCIs not subject to a supervision abroad. In accordance with this decision, the aforementioned UCIs could not be admitted to trading on the Luxembourg Stock Exchange.

Taking account of the market trends and the legislative development in this field at national and international level, the Government in Council decided on 19 December 2003 to revoke the decision of 4 March 1988. Indeed, the Government considered that the restrictive interpretation of article 70 of the law of 30 March 1988 on UCIs as amended is no longer consistent with the national and international developments in this area. In particular, the Government took into consideration that it is no longer possible to generalise the principle according to which a public stock exchange listing is a public offer or exposure and that the Luxembourg Stock Exchange must be allowed to list foreign UCIs and products linked to such UCIs without being hindered by an approach outdated in other financial centres.

The decision of the Government in Council of 19 December 2003 thus allows the CSSF to agree to the listing of the aforementioned financial instruments. The legislative texts relating to the conditions for approval and the contents of the prospectus applicable to this category of financial instrument are being adapted to this new situation.

3.1.2. The market ensured by the Luxembourg Stock Exchange and its members

The CSSF is kept informed of market activities and related issues on a daily basis through an activity report provided by the Luxembourg Stock Exchange.

As far as market activities are concerned, turnover fell by 54.43% as compared to 2002 to reach EUR 792.84 million. Total turnover of variable income securities represented 52.11% of trading compared to 47.89% for bonds.

At the end of 2003, the Luxembourg Stock Exchange counted 71 members (against 76 in 2002), including 17 cross members.

Considering that turnover decreased in 2003, the year was nevertheless marked by intense activity in new admissions to the Luxembourg Stock Exchange. 8,246 new securities (against 7,513 in 2002) were admitted, representing an increase of about 10% in relation to the number of quotation lines, compared to an increase of 4% in 2002. The total number of admissions as at 31 December 2003 amounted to 29,102 securities (against 26,486 in 2002), composed of 21,285 bonds, 268 shares, 1,795 warrants and rights and 5,754 undertakings for collective investment and compartments.

3.2. Documentation relating to public offers and listings

Under the supervision of the CSSF, the Luxembourg Stock Exchange is entrusted with the examination of prospectuses, pursuant to the Grand-Ducal regulation of 28 December 1990 on the requirements for the drawing up, scrutinising and distribution of the prospectus to be published where transferable securities are offered to the public or of listing particulars to be published for the admission of transferable securities to official stock exchange listing. Under the Grand-Ducal regulation, the Luxembourg Stock Exchange approves the prospectuses to be published where transferable securities are admitted to official listing and where public offers of transferable securities are followed by a listing on the Luxembourg Stock Exchange. Prospectuses relating to public offers of transferable securities not followed by a listing are approved by the CSSF.

In 2003, twenty-five public offers of transferable securities were made in Luxembourg, seventeen of which were public exchange offers in relation to securities listed on the Luxembourg Stock Exchange. The CSSF approved the documentation relating to seven public offers that were not the subject of an application for admission to official listing on the Luxembourg Stock Exchange.

The criteria applied by the CSSF regarding the supervision of the specific task of approval of prospectuses carried out by the Luxembourg Stock Exchange are based on close co-operation between the Stock Exchange and the supervisory authority.

In 2003, the Luxembourg Stock Exchange submitted around thirty application files drawn up for the purpose of the due examination of the public offer prospectus or listing particulars to the CSSF in order to obtain the CSSF's view on these issues. In addition, the Stock Exchange referred twenty-seven applications for an exemption from specific regulatory provisions concerning prospectuses to the CSSF. Seventeen of these were duly justified and thus granted.

As regards co-operation with foreign authorities concerning mutual recognition of prospectuses, the CSSF issued certificates of approval relating to 59 public offers or admission to the official stock exchange listing made simultaneously or within short interval in several Member States of the European Economic Area.

3.3. Luxembourg companies listed on the Luxembourg Stock Exchange

3.3.1. Financial information disclosed by listed companies

The law of 23 December 1998 on the supervision of securities markets as amended lays down the principle of monitoring the disclosure of financial information by companies admitted to the official listing on the Luxembourg Stock Exchange. The number of Luxembourg companies whose shares are listed amounted to 45 on 31 December 2003.

- **The IAS Regulation**

The IAS Regulation of the European Parliament and of the Council of 19 July 2002 introduces the obligation for companies, the securities of which are traded on a regulated market, to draw up their consolidated financial statements in accordance with IAS standards.

Continuing the work initiated in 2002, the CSSF explored and analysed the responses received to its letter sent to the Luxembourg companies whose shares are listed on the Luxembourg Stock Exchange, enquiring about the progress made by these companies (first concerned by the regulation) to adapt to these standards planned for 2005.

In order to assess the extent of the implementation of the second stage of the IAS regulation and in the context of the CSSF's participation in the CESRFin group, the CSSF started an analysis of the Luxembourg-registered companies of which only non-equity securities are listed.

- **The control of financial information**

The CSSF verifies all the financial data submitted to it, in particular the annual and half-yearly reports published by Luxembourg companies whose shares and parts are listed on a Luxembourg stock exchange. The CSSF can ask an independent external auditor to prepare a written report on individual and consolidated annual accounts of these companies.

Due to the difficulties encountered by certain listed companies concerning their transition to IAS/IFRS standards, the CSSF took a prudent approach in formulating observations and questions following the examination of the annual reports. The CSSF intervened several times as regards financial information submitted in 2003.

The CSSF intervened firmly with one company after having observed infringements of the requirements of continuous financial information, disclosure requirements of major shareholdings and the legal accounting requirements. Following a meeting with representatives of the company and several exchanges of letters, the CSSF communicated its grievances to the Luxembourg Stock Exchange, which decided to withdraw the securities from the official listing, and the CSSF transmitted the case to the Public Prosecutor in connection with the suspicions of infringements of the Luxembourg law.

While reviewing the accounts of another Luxembourg-registered company whose securities are admitted to the official listing of the Luxembourg Stock Exchange, the CSSF considered that the non-consolidated accounts did not reflect the economic reality and as a consequence, required the company to draw up consolidated accounts, integrating all the group's companies whose risks and profits it takes into account. The CSSF intervened with the persons in charge of the company in this respect.

The CSSF gave a negative response to a question relating to the application of article 9 of the IAS regulation, as it considers that the company must apply the IAS/IFRS standards as of 2005, since the latter does currently only provide a reconciliation with the accounting rules that apply in the United States.

3.3.2. Information on major shareholdings

The CSSF systematically checks compliance with the law of 4 December 1992 on the information to be published when a major holding in a listed company is acquired or disposed of, notably by considering attendance registers of ordinary and extraordinary meetings, as well as any other source of information.

The CSSF intervened more specifically in one case where the transparency of the transactions was not given. Following several exchanges of letters, details of the transactions have been reported in accordance with the legal provisions.

CHAPTER VII

SUPERVISION OF INFORMATION SYSTEMS

1. Activities in 2003
2. International co-operation

1. Activities in 2003

1.1. Meetings and on-site inspections

In 2003, IT audit participated in 114 meetings and 3 on-site inspections on subjects covering the functioning and security of the supervised entities' IT systems. A little bit more than half of the meetings were held with providers of services, consultants or law firms.

IT audit has also contributed to several seminars or conferences, national meetings held within the framework of projects, such as the setting up of a national certification authority, and to press articles.

As from September 2003, IT audit was greatly solicited by companies seeking information on the legislative changes that took place in August 2003. Indeed, the law of 2 August 2003, amending the law of 5 April 1993 on the financial sector, has, inter alia, introduced three new categories of professionals of the financial sector (PFS) defined under articles 29-1, 29-2 and 29-3 of the law of 5 April 1993, which gave rise to questions falling more particularly under the competence of IT audit. The activities covered by these PFS, considered as connected to the financial sector, do not exclusively rely on the provision of financial services anymore, but on the provision of outsourcing services relating to financial activities. The following statuses are concerned:

- Client communication agents whose services notably include printing of statements of account or confirmations of financial transactions, as well as archiving of documents. As communication can also take place in electronic form, holders of this status are allowed to operate consultative websites.

- Administrative agents allowed to contribute to the business processes of financial institutions and whose services are similar to back office functions.

- IT systems and communication networks operators of the financial sector who intervene on the IT systems of financial institutions, but which are not allowed to intervene within the business lines.

The reader is invited to refer to Chapter I, which provides further information on the specificities of these activities.

With respect to these new activities, IT audit takes account of the concentration risk and verifies the professionalism of the activities, so as to ensure that the quality of the outsourced services meets the same criteria as those required for financial institutions which have recourse to these services.

Particular stress is laid on the segregation of environments and data. Indeed, a service provider entrusted with the work of several financial institutions must at any time be able to distinguish for whom he is providing a service. He must also be able to ensure perfect impermeability between the entities concerned, so as to guarantee perfect confidentiality of the entrusted data.

Where a company or group creates a new PFS entity and partially transfers staff to this new structure, IT audit verifies that the access rights to premises and systems, which must be reserved to staff of the PFS, are strictly complied with. Indeed, transferring personnel always entails difficulties as regards the management of these changes, in particular where the PFS occupies premises adjacent to those of the company it originates from. It is not always easy or natural for transferred employees to consider their former colleagues, whom they possibly meet every day because of the closeness of the premises, as external parties according to circular IML 96/126. The circular notably defines certain practices that must be complied with as regards access to the production environment and professional secrecy.

Considering the origin of the providers of connected services, who do not necessarily have a "corporate culture" similar to that of an entity subject to the supervision of the CSSF, IT audit intends to insist on the educational aspect rather than on the coercive aspect of supervision. The purpose is to convey the basic mechanisms governing a "sound and prudent" management of the activity to the new PFS. Stress will be laid on the perenniality of the activities, the drawing up of procedures, the four-eye principle, as well as on segregation, integrity and confidentiality of the processed data.

1.2. The GRIF research project

On 30 June 2003, the CSSF signed a co-operation agreement with the *Centre de Recherche Public Henri Tudor* (CRP-HT). The aim of the agreement is to carry out an applied research project, named *Gestion des Risques Informatiques dans le Secteur Financier: nouvelles approches méthodologiques* (GRIF project, IT risk management in the financial sector: new methodological approaches).

This project, which is co-financed by the CRP-HT and the CSSF, has been set up in the context of the international harmonisation of banking supervision as defined by the New Basel Accord ("Basel II") and more particularly of the supervisory mission of the CSSF under "pillar 2", which requires that the supervisory authority reviews and assesses capital adequacy and the internal rating process of credit institutions.

The main objective of the CSSF and the CRP-HT consists in studying new methodological approaches allowing to assess IT-related risks, preferably in a quantitative manner. The findings in this highly specific field of research aim to formalise and quantify the consideration of IT risks within the global operational risks of financial institutions. The knowledge shared is diverse and the project team consists of both CRP-HT researchers and CSSF agents, so as to optimally cover the areas of statistics, mathematics, IT, documentary research, project management, IT systems audit, prudential supervision and systems security and finance.

The GRIF project, in its initial stage, will stretch over two years and consists of four parts. The first part aims to create an "IT and finance" sectorial competence unit, directed towards risk management and IT security. The second part covers the production of a new methodological tool, while the third part consists in validating the results through consultation of local players. The fourth and last part concerns a study on the perpetuation and development of skills, e.g. by widening the partnership with the financial, institutional and IT sectors.

At the end of 2003, the multidisciplinary research team closed the stage consisting in levelling up the participants' knowledge. Thus, each member has a more precise view of the concepts of Basel II, as well as of those of IT risk management. The works on the agenda during the next stage consist in analysing the main components to be taken into consideration as regards IT risk. It is possible that a UML representation (Unified Modeling Language) will allow to better formalise this model: resources used, characteristics of these resources, weaknesses and associated risks, etc. This type of model could lead to a language or formalism shared by institutions which carry out their own risk assessment within the scope of AMA (Advanced Measurement Approach) and by the CSSF, which must validate their approach.

2. International co-operation

IT audit participates in the works of the Electronic Banking Group (EBG) of the Basel Committee. The EBG was instituted in November 1999 with the aim of reflecting on the prudential consequences of electronic banking activities, mainly through the Internet.

The first document entitled "Electronic Banking Group Initiatives and White Papers" has been presented in November 2000 and defined the initiative taken by the Basel Committee on banking supervision.

The document entitled "Risk Management Principles for Electronic Banking" had been drawn up in May 2001 and published in its final version in July 2003. It sets out the main points to comply with in order to ensure adequate risk control as regards e-banking: effective management by the Board of directors and the senior management of the financial institutions, security controls (non-repudiation, authentication, etc.), legal and reputational risk management.

Furthermore, the report "Management and Supervision of Cross-Border Electronic Banking Activities", published for the first time in October 2002, which, on the one hand, identifies the responsibilities of the institutions when setting up a cross-border activity via Internet and, on the other hand, specifies the supervisory modes of the relevant authorities, i.e. the authority responsible for the supervision of the institution offering the service concerned and the authority of the host country in which the service is offered, has been published in its final version in July 2003. This document shows the limits of such a co-operation between authorities, in particular when the home country does not provide for any supervision and the services are provided without any physical presence in a host country requiring that the services provided be supervised.

None of the final versions of these documents has been fundamentally changed. The modifications essentially concern the presentation order of certain footnotes.

During the year 2003, the EBG continued to act as an exchange platform, allowing members to better understand the current challenges as regards e-banking services. These information exchanges, notably in the field of cyber-criminality, show that certain continents, in particular Asia, are subject to a new wave of fake web sites, aiming either to mislead users in order to intercept their identification data on real websites or to intercept credit card numbers, or to illegally collect deposits of the public, whereas the credit institution does not exist. The EBG intends to discuss the subject of the security of electronic financial services in 2004, subject to the approval of the Basel Committee. The stakes represented by outsourcing should also be examined.

CHAPTER VIII

MEANS OF SANCTION AVAILABLE TO THE CSSF

1. Means of intervention available to the CSSF
2. Sanctions imposed in 2003

1. Means of intervention available to the CSSF

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 a sector of activities of the establishment concerned.

In addition, the CSSF has the right to:

- impose or ask the Minister of Treasury and Budget to impose disciplinary fines on the persons in charge of the administration or management of the establishments concerned;

- under certain conditions, request the District Court responsible for commercial affairs to have payments suspended and place an establishment under controlled administration;

- ask the Minister of Treasury and Budget to refuse or 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 or withdraw registration from the official list of undertakings for collective investment, pension funds or management companies (Chapter 13 of the law of 20 December 2002 as amended), 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;

- in extreme cases and under precise conditions laid down by law, request the District Court responsible for commercial affairs to order the winding up and liquidation of an undertaking.

Moreover, the CSSF informs the Public Prosecutor of any situation 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 company domiciliation without belonging to any of the professions entitled by the law of 31 May 1999 governing the domiciliation of companies as amended to carry on this activity;

- 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 as amended, 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. Sanctions imposed in 2003

2.1. Credit institutions

In 2003, the CSSF did not have to formally use its right of injunction and suspension conferred on it by law.

However, the CSSF required the departure of six managers and directors. In two cases, the legislation concerning money laundering was seriously infringed. The other cases concerned unprofessional and deontological incorrect behaviour relating to the granting of a credit which resulted in a loss for the bank.

The CSSF filed one complaint with the Public Prosecutor's Office for illegal banking activities and one complaint for violation of article 52(2) of the law of 5 April 1993 on the financial sector as amended.

2.2. The other professionals of the financial sector (PFS)

In 2003, the CSSF did not have to formally use its right of suspension conferred on it by law.

However, it used its right of injunction on three occasions. The imposed injunctions concerned situations of non-compliance with legal provisions regarding daily management according to article 19 of the law of 5 April 1993 on the financial sector as amended.

During 2003, the CSSF also imposed disciplinary fines of EUR 1,500 each on persons responsible for the daily management of three PFS. These were imposed on account of refusal to transmit information in accordance with article 54 of the aforementioned law, i.e. closing documents for the financial year ending 31 December 2001.

The CSSF also requested in one particular case that the Minister of Treasury and Budget withdraws the ministerial authorisation, as the PFS concerned did no longer fulfil the necessary conditions for the authorisation to be maintained.

Following an on-site inspection at the premises of one professional of the financial sector acting as domiciliation agent of companies, the CSSF had to require the PFS concerned to cease all activities of the financial sector due to non-compliance with certain legal provisions.

In 2003, the CSSF filed twelve complaints with the Public Prosecutor's Office for illegal domiciliation activities of companies not authorised thereto. The CSSF also lodged five complaints with the Public Prosecutor's Office for illegal activity of the financial sector, including two cases where the companies concerned collected third-party funds without being authorised thereto.

2.3. Undertakings for collective investment

In 2003, the CSSF decided to require one UCI not to accept any new requests for subscription. This measure became necessary due to the fact that legal proceedings had been instituted against the promoter of the Luxembourg UCI in its home country. These proceedings, entailing a payment and transfer prohibition of the promoter, led to its liquidation. The Luxembourg UCI has finally also been put into liquidation.

The CSSF has observed serious deficiencies for one UCI as regards the transmission and the quality of financial information to be reported to the CSSF in accordance with circular IML 97/136 of 13 June 1997 concerning the financial information for the CSSF and Statec. Indeed, the financial information reported by this UCI was incomplete, incorrect or false and, despite several reminders concerning the provisions of the aforementioned circular, the CSSF did not note any improvement in the transmission and the quality of the monthly financial information of the UCI concerned. The CSSF has therefore decided, by virtue of article 84 of the law of 30 March 1988 on UCIs as amended, to impose a disciplinary fine on each of the UCI's directors for non-compliance with the provisions of circular IML 97/136.

Moreover, following certain events relating to the manager of two UCIs, the latter was led to resign his post at both UCIs, since the CSSF considered that he no longer fulfilled the criteria of good reputation requested by law.

CHAPTER IX

CUSTOMER COMPLAINTS

1. Complaints in 2003
2. Analysis of complaints handled in 2003
3. FIN-NET network: the cross-border out-of-court complaints network for financial services

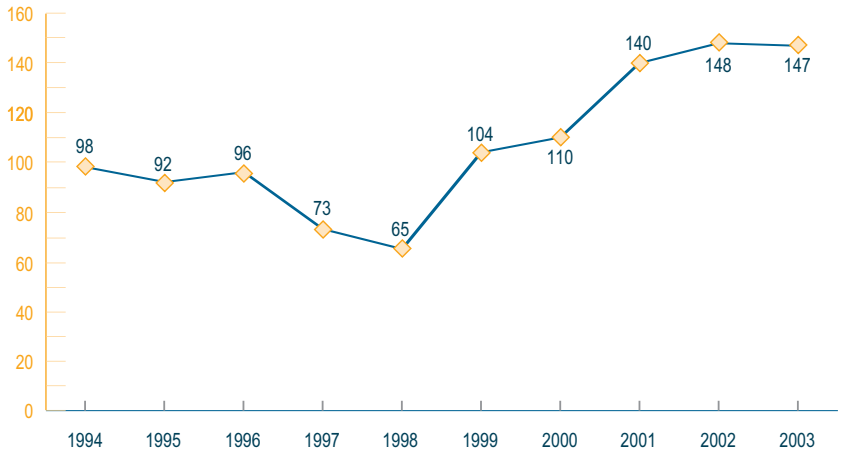
1. Complaints in 2003

The law of 5 April 1993 on the financial sector as amended confers on the CSSF the task of mediating between the customers and the institutions it supervises. Under the terms of article 58, the CSSF is competent to receive complaints from clients of the persons subject to its supervision and to take action vis-à-vis these persons with a view to reaching an amicable settlement of the disputes.

Within the CSSF these disputes are handled by the General Secretariat.

The analysis of the new complaints handled by the CSSF in 2003 reveal for the first time a certain stabilisation.

Number of complaints received



Among the 147 complaints received in 2003 by the CSSF, 137 were lodged by natural persons and 10 by legal persons. 24 plaintiffs contacted the CSSF through a lawyer or a representative. The majority of complaints concerned banks (136), while 11 complaints concerned PFS. Furthermore, the department for the supervision of UCIs handled 19 complaints against UCIs; these complaints are not included in the statistics of the General Secretariat.

Number of complaints handled in 2003

Number of complaints received in 2003	147
Files from 2002	63
Total files handled in 2003	210

Geographic breakdown[1] of the 210 complaints handled in 2003

Belgium	55	United Kingdom	2
Germany	48	Spain	2
Luxembourg	46	Portugal	1
France	20	Finland	1
Netherlands	3	Denmark	1
Sweden	3	Greece	1
Italy	3	Others	24

These figures confirm that the Luxembourg financial centre attracts clients from all over the world, but mainly from Belgium and Germany.

[1] *According to the home country of the plaintiff.*

Among the 210 complaints handled in 2003, 157 were closed, with the following outcome or reason for closing:

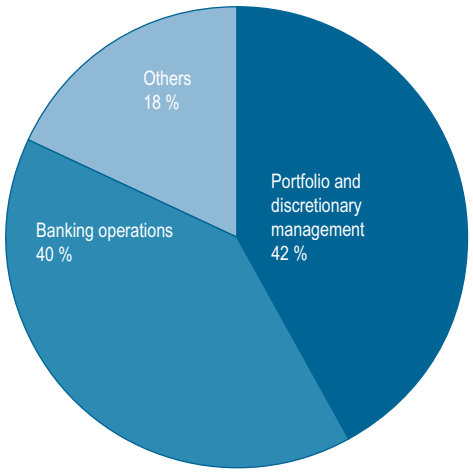
Closed files:		157
Article 58 non applicable	1	
Referral to a court	3	
Withdrawal by client	23	
Amicable settlement	13	
Justified or partly justified complaints	11	
Unjustified complaints	42	
Irreconcilable positions	52	
Other	12	
Files reported into 2004:		53

It has to be noted that 24 of the 53 files reported into 2004 were settled by 1 March 2004.

For 52 cases of the closed files, no amicable settlement could be reached, as the positions of the parties were irreconcilable and contradictory. As the CSSF does not act as judge or arbitrator making the sentence compulsory, but its role being limited to finding an amicable settlement to the case, the failure of discussions between the bank or another professional of the financial sector and the client puts an end to the CSSF's intervention. The category of files closed for other reasons includes twelve complaints for which the CSSF considers that the clients have not exhausted all the recourse available with the professionals. As a consequence, the clients were invited to address the professionals concerned and keep the CSSF informed, for a possible later intervention, of the results of their complaint. In the above-mentioned cases, it seems that the clients were able to solve their dispute with the professionals without requiring the intervention of the CSSF.

The analysis of complaints according to their object reveals that those relating to portfolio management (securities) still take the top position, followed by the category of banking operations of all kinds. The complaints relating to cross-border transfers alone represent nine cases.

Breakdown of complaints according to their object



Portfolio and discretionary management		88[2]
Non-execution of orders	11	
Fees and commissions	12	
Incomplete customer information	19	
Non-professional management	32	
Non-fulfilment of agreement	7	
Request of documents	1	
Other	19	
Banking operations		85
Non-execution of orders	18	
Fees and commissions	21	
Incomplete customer information	9	
General conditions	1	
Non-fulfilment of agreement	1	
Request of documents	4	
Cross-border transfers	9	
Others	26	
Others	37	

While 66% of the complaints were related to portfolio management in 2002, there has been a substantial decrease in complaints in this field for the first time with only 41.9%; the slight recovery of stock markets, in particular as from the second quarter 2003, certainly contributed to this development.

2. Analysis of complaints handled in 2003

2.1. Discretionary management

As far as investment is concerned, the discretionary management mandates are at the root of many complaints, the clients blaming the professional of the financial sector for poor management of their portfolio as soon as they record losses. However, it has been noted that in most cases, the decrease in the portfolio value is rather due to the fall of stock markets than to poor management by the portfolio manager.

The concept of the discretionary management mandate as such is simple: the client charges the professional with the management of his portfolio in a discretionary manner, without needing the client's prior agreement for the transactions executed. The client does not actively participate in the management of his portfolio. The situation is less clear where the client himself gives precise instructions the manager then executes. This type of situation often results in the client blaming the professional, as soon as things turn bad, for poor management within the scope of the discretionary management mandate.

Many problems could be avoided if the professionals were more rigorous in the fulfilment of their discretionary management mandate and/or if the clients refrained, within the scope of a discretionary management mandate, from giving instructions to the professional to buy or sell a specific financial product, knowing that it is difficult to reconcile these practices with the principles of a discretionary management agreement.

Within the scope of the disputes submitted to the CSSF, the question arose as to whether the professional who received such instructions within the context of a discretionary management is obliged to execute them.

[2] *Certain files can appear in several sub-categories.*

It must be referred to the terms of the agreement binding the parties in order to be able to answer this question and the relating disputes. The solution is easy if the agreement expressly provides for this possibility: the professional is obliged to execute the customer's orders. However, if the agreement only stipulates that the professional has discretionary power without needing to obtain prior authorisation by the client, the professional must take all the prudent steps he deems necessary to execute these orders. However, if the professional follows the client's orders, he must stick to this way of proceeding and cannot, in the future, ignore the client's orders. In this case, the discretionary management agreement must be interpreted in the light of the common intention of the parties, instead of keeping strictly to the literal sense of the terms and conditions.

It must also be noted that within the scope of the information requirement, the professional is obliged to inform the client of the incompatibility between the signature of a discretionary management agreement on the one hand, and the instructions given directly by the client on the other hand. The professional must, if necessary, direct the client towards a better-suited formula, such as an advice agreement, allowing the client to manage his portfolio himself by placing buying and selling orders.

2.2. Advice management

Notwithstanding the existence of an advice management agreement, clients sometimes give their manager a free hand to execute transactions on securities without their consent, or even without being aware thereof. This practice, based on a trust relationship between the client and the manager, is very common and works as long as the client ratifies the transactions afterwards, tacitly or in writing. However, problems become inevitable when the latter disputes a transaction that was detrimental to him, by invoking the absence of his instructions and of a discretionary management mandate. Other complaints stem from the attempt of one of the parties to establish the existence of a tacit discretionary management mandate.

The reverse side of this practice is that a simple trust relationship between the client and the manager can result in a dependence of the client vis-à-vis his manager, who manages the client's portfolio *de facto* in the absence of any discretionary management mandate.

In this context, the CSSF has dealt with a complaint where problems arose from the moment the portfolio manager left the bank. As the bank is not obliged to notify the client of the departure of the manager, the client was unaware thereof. It was only when he vainly tried to contact his account manager that he became aware that his portfolio was not actively managed anymore. The bank stated that it was not aware of the manager's practices and denied that a discretionary management mandate had existed. The client was unable to prove the contrary, nor to submit concrete elements to establish the existence of a tacit mandate between himself and the manager, so that the CSSF could not conclude that the bank acted wrongly. The CSSF can only recommend that both parties be prudent and vigilant and clearly set the obligations by which they are bound, which is in their own interest. Thus, where the bank regularly executes orders for the account of its client without prior instruction of the latter, it is highly recommended that they sign a discretionary management agreement.

The majority of the clients benefiting from an advice management agreement and those who give their instructions independently from the bank's advice, require that their funds be rapidly invested on the stock market and therefore often use not very formalised means to transmit their orders, such as telephone, fax or e-mail. However, these clients would be well-advised to conscientiously keep records of their orders and not to hesitate to request, if necessary, a written confirmation of the orders given, allowing them to complain to the professional within a short period of time, with supporting documents to prove their claim. Indeed, any tangible element likely to support the position of the parties will afterwards make it easier not only to prove the arguments discussed in the complaint letter, but also to find an amicable settlement, as it will allow to establish the truth.

In one case submitted to the CSSF, the client claims to have given a written order by fax to buy four securities, specifying a month's deadline. However, he noticed several months later that two of these securities had been bought after the deadline. The bank denies having received the fax in question. It confirms that the orders are encoded without indication of deadline, except otherwise specified by the client, and invoked that according to its general terms and conditions, the orders are systematically validated until the end of the civil year during which they have been encoded. While the bank maintains that it never received the fax concerned, the client transmitted copies of the faxes sent to the bank and his detailed telephone bills, proving that not only a fax had been sent to the bank at the said date, but also that the bank had received this fax together with a certain number of other faxes (not disputed by the bank) referring directly to the fax in question. The bank however maintains that the client must have given oral unlimited orders; but it does not have any elements whatsoever to prove its points, such as telephone recordings or transcriptions. Moreover, the bank considers that in the absence of any dispute by the client within the given time limit, only the notes are sufficient prove of the orders given by the client, according to its general terms and conditions. However, as the client thought that the order had expired after the month in question, the client was not aware that his order was still valid. In this dispute, the documents provided by the client as proof are very important. The bank, however, does not have any arguments in the presence of the client's instructions, which were clear and had been reiterated many times by fax. Following our reasoned opinion, the client was entirely compensated for the loss sustained by the acquisition of the securities.

2.3. Information on risks

The CSSF is also contacted by clients complaining that they were only insufficiently warned of the risks inherent in the purchase of one or several financial products. They often become aware of the risks only after having sustained substantial losses.

The professionals of the financial sector are bound by the obligation to inform the clients on all the risks inherent in a financial product and to give useful advise by taking into consideration their investment profile (financial situation, targets, experience, etc.). It is important that they provide sufficient and complete information to the clients and make sure that the latter are fully aware of the scope of their commitment. This obligation is all the more important as many clients are only fairly experienced in this field and are not used to such transactions. The professional must therefore inform the clients on the risks inherent in the transactions they envisage, so as to allow them to invest with full knowledge of the facts. On the other hand, the clients are also obliged to take the initiative to seek information on the products they are interested in, as they are the ones who decide.

A significant number of clients blame their bank for having bought too speculative securities within the scope of a discretionary management mandate.

The following case demonstrates how essential it is that the professional ensures that the client chooses the adequate profile from the beginning, even though this is often difficult, as the client's requirements are often unclear or ambiguous. A dispute concerned the fact that the client had decided on a discretionary management with a dynamic management profile and claimed afterwards that he had laid down the condition that the bank should withdraw his portfolio from the market in case of a loss of a maximum of 15% of the total investment. He sustained that at no moment had he been advised of the risks inherent in an active management of a 100% share investment. However, a clause of the signed agreement stipulated that he had been made aware of the risks. The bank explained that on the basis of the elements and evidence of managers and account managers, the client had never expressed the wish to have his losses limited to 15% and that such a limitation was in direct contradiction with a dynamic profile. As the CSSF did not have any element at its disposal proving the client's claims, and considering that the latter even refused several times to change his investment profile, the bank could not be blamed for any incorrect behaviour.

It has to be stressed that as far as stock market matters are concerned, even the best-informed clients having a thorough knowledge of the risks, should seek more information on the technical nature of the products in which they wish to invest.

In one case submitted to the CSSF, it seems that the client was unaware of the fact that European-type bonds cannot be realised before their maturity date and can be subject to margin calls. However, the documents relating to transactions on bonds stated that the client had been made aware that the risks inherent in leveraged derivatives were unlimited. He could thus not reproach the bank with selling shares of his portfolio in order to increase his cover and with closing the short positions following his inability to provide further funds.

2.4. Third-party management agreement

A less widespread management formula is the third-party management agreement, which consists in giving a management mandate to a person of one's choice, charged with managing his portfolio on one's behalf and for one's account, and not to a professional of the financial sector.

The CSSF handled a case where the professional, although only a third party to this mandate, found himself involved in this matter, as the mandate had been given to one of his employees (client's personal friend). However, the client blames the professional for the drop in the value of his portfolio, claiming that the portfolio management had not been made in a non-speculative perspective and that the parity of the shares and bonds had not been respected. In principle, the professional should not consider himself as a third party to this agreement, as the latter had been signed with one of his employees. However, in this particular case, the professional was able to prove that the client gave this mandate knowingly to his friend *intuitu personae* and that no contract had bound him to the company, as he had refused to sign an agreement with the latter. The CSSF can only disapprove of this type of practices, which result in ambiguous situations.

2.5. Fees and commissions

Another category of complaints concerns fees charged by banks and which are deemed excessive. In this respect, it should be pointed out that the CSSF does not, in principle, interfere in the determination of the price list of the professionals, which is of the sole remit and responsibility of the latter. Indeed, the CSSF does only interfere with a professional with respect to prices, if the latter failed to apply the prices communicated to the client or failed to inform him about the existence of fees and commissions beforehand.

Given the fact that a substantial number of complaints concerned problems relating to the fees charged by the banks, of which the clients claim they had not been informed beforehand, the CSSF advises the professionals to make their clients aware that the price list is available (should it not be handed out anyway) and to inform them of any subsequent change thereto.

The clients must not however adopt a purely passive attitude: they must be reminded that they are themselves obliged to seek information.

Among the cases concerning fees and commissions, the following are of particular interest.

A client bought units of funds at issuance price. The prospectus stated that the maximum loss that could be incurred could not exceed 3% of the invested capital. At maturity date, this was the case. The client then complained that he was reimbursed less than the guaranteed minimum and that the bank had charged a commission for the order transmission, as well as account charges. The client blames the bank for not having informed him beforehand of the annual deduction of account charges through the sale of fund units held (leading to a lesser refund) and demands to be refunded. The bank specifies that a distinction has to made

between the operations consisting in investment in funds and the keeping of funds acquired by the client. Indeed, the latter had opened a deposit account with the bank to this end. By doing this, he had expressly signed and acknowledged that he had been informed of the general terms and conditions, which provide for annual account fees to be charged for the management of the deposit account, and that all the fees and commissions would be fixed according to the prices applied within the bank. The terms and conditions also provide that the bank is entitled to cover the account costs through the sale of fund units or parts of fund units respectively, up to the amount of charges.

In a certain number of cases, clients of the same bank were surprised by the changes made to the price list. While the bank had managed the clients' deposit accounts for free for many years, the clients received a letter in December 2002, informing them about the new terms and conditions of the bank applicable as of January 2003 and providing for the introduction of advice fees. However, the letter did not specify that this new bimonthly fee applied to all the holders of deposit accounts, even if they did not enjoy advice from the bank to manage their portfolio. The clients who did not feel concerned by this new fee, did not deem it necessary to terminate their relationship on the grounds of the fee being too high in relation to the funds deposited. It was only when the fees were eventually charged that the client became aware that they were compulsory for all the account holders. The bank agreed to reimburse the clients and to rectify the general terms and conditions in order to make them more transparent.

2.6. Obligation of the client to seek information

Besides the obligation of the professional to inform and advise the clients, the clients have to seek information themselves, making use, where applicable, of the sources at their disposal.

In one case, the client reproaches the bank for not having informed him, not even by means of documents, of the high risk inherent in the investment in an investment fund and claims to be reimbursed of the loss incurred following the acquisition of the fund units. The bank informed the CSSF that, at the launch of the new sicavs, it had sent a notice thereon to the clients, inviting them to contact one of the advisers or the commercial secretariat in order to obtain further information on the product. According to the bank, the notice sent to the clients was not in the least intended to provide comprehensive information (notably on risks), but only aimed to inform the clients about the existence of this product, specifying that adequate information was available upon request. The bank was not able to pronounce on what had been discussed on the phone, but stressed that according to general practice, the marketing people assess the different aspects of the proposed financial products with the clients. The bank admits that the publication rating the fund's risk as very high had only been made available to clients on express request and that it did not have any evidence proving that the client had made such a request. After having examined the explanations provided by both parties, the CSSF concluded that the bank had given the opportunity to the client to obtain further information; however, the latter had never made use of this possibility.

Moreover, the clients are obliged to keep themselves informed about the development of their portfolio through statements of account and wealth and other means made available by the professional and must, where applicable, regularly check their mail held by the professional. Indeed, the professionals are only obliged to inform the clients of important losses in certain determined cases.

This is illustrated by the following case where a client, whose portfolio had sustained a loss exceeding 10%, considered that the bank should have notified him thereof. However, the CSSF informed the client that circular CSSF 2000/15 did not apply in this case, as article 5.10 of the circular only applies to substantial losses sustained in relation to the investments made for the client within the scope of the discretionary portfolio management. In that case, the professional is indeed obliged to immediately inform the client of the negative development of his portfolio. As this dispute did not lie within the scope of a discretionary management

mandate, this article did not apply. Moreover, the client was permanently in touch with his account manager with whom he discussed the content and the performance of his portfolio. He could therefore not have been unaware of his portfolio's negative development. A client is thus obliged to request himself information from the bank on the state of his wealth; the managers of the banks are in charge of assisting and advising him.

2.7. Cross-border credit transfers

Under the scope of article 41-10 of the law of 5 April 1993 on the financial sector as amended, the CSSF had to deal with a certain number of disputes relating to provisions of directive 97/5/EC of the European Parliament and of the Council of 27 January 1997 on cross-border credit transfers (hereinafter the "Directive") transposed into Luxembourg legislation by the law of 29 April 1999 amending the law of 5 April 1993 on the financial sector as amended, as well as of Regulation (EC) No 2560/2001 of the European Parliament and of the Council of the 19 December 2001 on cross-border payments in euro (hereinafter the "Regulation").

Under the terms of article 7 point 1 of the Directive: *"The originator's institution, any intermediary institution and the beneficiary's institution, after the date of acceptance of the cross-border credit transfer order, shall each be obliged to execute that credit transfer for the full amount thereof unless the originator has specified that the costs of the cross-border credit transfer are to be borne wholly or partly by the beneficiary".*

The Directive foresees the option OUR (all charges to the originator of a payment) as default option in order to avoid double charging and to ensure the arrival of the full amount transferred on the account of the beneficiary.

The CSSF has noted that certain banks apply, if they do not leave the choice to the originator of the sharing of costs, the principle of shared costs (hereinafter "SHARE"), according to which the originator as well as the beneficiary each bear the costs charged by their respective bank. Other banks however levy the entire charges on the originator (hereinafter "OUR"), in case no choice is given, and also those levied by the beneficiary's bank.

The Regulation sets out, from 1 July 2003, the principle of equal charges for cross-border transactions within the European Union and for domestic transactions. Thus, a credit transfer up to EUR 12,500 indicating the beneficiary's IBAN code (International Bank Account Number) and the BIC code (Bank Identifier Code) of the beneficiary's bank, has to be handled like domestic credit transfers.

Costs for domestic credit transfers, which, until that date, had been free of charge, have been introduced in Luxembourg.

The purpose of the Regulation is to ensure equal charges for any credit transfers, domestic or international, as soon as the conditions described above are fulfilled. Indeed, the introduction of the IBAN and BIC codes aims to reduce the transfer costs through the automated processing of credit transfers. If these codes are not indicated, the banks can levy additional charges in order to compensate for manual manipulations needed to execute the credit transfer.

Since the implementation of the Regulation, the CSSF has received a certain number of complaints related to the fact that banks levied intermediary bank charges on top of the transfer charges. The banks justify these deductions by explaining that intermediary institutions are levying these charges. Thus, Luxembourg banks claim they only levy on the customer those charges that the other institutions charged on themselves.

The intermediary bank charges levied by Luxembourg banks stem from the distinction made since the transposition of the Directive depending on whether the cross-border credit transfers are executed according to the option chosen by the originator: BEN (all charges to the beneficiary), OUR (all charges to the originator) or SHARE (shared costs between originator and

beneficiary). With the coming into force of the Regulation, the SHARE option became, within the scope of the execution of a cross-border credit transfer, a condition to be fulfilled in order to apply the same charges as those applied for a domestic transfer, as only this option allows to automatically route the transfer orders through the settlement systems (Straight Through Processing, hereinafter "STP").

This can be explained by the fact that with the Regulation, concrete measures to simplify the technical processing of cross-border credit transfers in euro became necessary. The European banks, in conjunction with the European Payments Council, have thus drafted the Credeuro Convention, which defines the characteristics of a standard credit transfer to be processed through STP, thus guaranteeing an efficient and low-cost execution with an execution time of a maximum three days.

A basic credit transfer must contain the IBAN and BIC codes, must be of up to an amount of EUR 12,500, the bank of the originator and that of the beneficiary must be located in a EU Member State and the mode of cost sharing must be SHARE (shared costs). If these criteria are fulfilled, the account of the beneficiary will be credited with the full amount (less domestic charges deducted, if applicable, by the beneficiary bank).

A second convention, the Interbank Convention on Payments (ICP), aims to supplement the new regime and covers the charging principles by laying down new pan-European rules relating to the standard charging procedure between banks for cross-border STP credit transfers falling under the scope of the Regulation.

This Convention lays down two main principles:

- the use of the SHARE charging option as a standard for the execution of a basic credit transfer. The originator and the beneficiary will only be charged for the costs levied by their own bank (and not for any intermediary bank charges);

- the elimination of any deduction by intermediary banks of any charges or replacement of these intermediary charges by interbank charges (levied on the banks). Consequently, the full amount will always be credited to the beneficiary.

The banks remain free to propose the charging option BEN and OUR, which give rise to extra costs, as these services do not fall under the scope of the ICP. The CSSF considers it essential that the Luxembourg banks better inform their customers about the fact that the options BEN (costs borne by the beneficiary) and OUR (costs borne by the originator) entail extra costs, as well as about the reasons of these costs. The banks must also inform their clients that the choice of the SHARE mode allows in principle to ensure that the amount ordered is fully credited to the beneficiary of the transfer, as in the majority of countries, the banks do not charge any costs for receipt of the funds.

2.8. Banking operations

In one case, a client handed in five securities for collection and got a receipt mentioning "five securities worth 10,000". Another bank, which is the principal paying agent for this issue informed the first bank that they were not worth 10,000, but 50,000, and that consequently, the client's account has been credited with the corresponding amount. The receipt has been changed following the correction communicated by the principal paying agent. Almost ten months later, the latter informed the bank that it noted, after having checked the issue, that it were five securities of 10,000 and not five securities of 50,000 and requested the immediate refund by the bank of the excess payment made to the client. The bank then debited the client's account despite the opposition of the latter. The bank insists that this way to proceed is covered by the general terms and conditions relating to transfers, which provide that the client authorises the bank to reverse any transaction whose execution has been called into question.

The bank, under the threat of legal proceedings by the principal paying agent, justifies the fact of having debited the client's account, by providing a judgement of the court of appeal, which declared as justified the recovery of payments made by mistake, as the payment had been executed following a material mistake on the number of deposited securities.

In another case, a client claimed to have submitted a certain number of securities for redemption. One month later, the bank informed the client that a mistake, which had been made when the securities had been counted, has been noted during the course of an internal control and that the agency had counted a significantly higher number of securities than the securities that had actually been deposited. The bank demands the refund of the payment made by mistake to the client on the grounds of the payment conditions signed by the client, which mention an "under reserve" clause, allowing the bank to claim, without time limit, the amount of the securities that have been counted and cannot be collected. The bank reserves the right to reverse the amounts paid, under reserve, on the client's account, or, failing that, demand the amounts in question directly from the client. As the client contests this position, without however specifying the number of securities he had actually deposited, the bank required him to provide a proof of the number of securities deposited. However, the client considers that he must not produce such a proof, as the receipt of the deposit should serve as proof. But the receipt is not an indisputable proof. The bank thus applied the under reserve clause correctly. The CSSF considered that the bank did not make any mistake while debiting the client's account, given the absence of proof regarding the number of securities actually deposited by the client, and the presentation by the bank of a copy of the securities deposited. The bank is thus entitled to reverse the amounts paid to the client, even though it made a material mistake.

3. FIN-NET network, the cross-border out-of-court complaints network for financial services

The FIN-NET network was established by the European Commission and gathers the bodies responsible for the out-of-court settlement of cross-border disputes relating to financial services within the European Economic Area, among which the CSSF. Two meetings were held in Brussels (3 March 2003 and 4 November 2003) under the aegis of the European Commission. These meetings notably covered the exchange of experience within the framework of the network's functioning and recent developments within the field of out-of-court settlement of disputes, as well as in the more vast area of financial services in the European Union.

The number of complaints submitted to the CSSF by bodies responsible for the out-of-court settlement of disputes of other Member States remained very low and amounted to two in 2003. This is due to the fact that the Luxembourg financial centre is at the heart of Europe and its for the most part foreign customers, who do not hesitate to directly turn to the CSSF without addressing the Fin-net. Thus, among the 210 complaints handled in 2003, 147 originate from another Member State of the European Union. The number of complaints transmitted by the CSSF to the competent authority within the Fin-net network amounted to six.

CHAPTER X

INTERNATIONAL CO-OPERATION: CSSF INVOLVEMENT IN INTERNATIONAL GROUPS

1. Co-operation within European institutions
2. Multilateral co-operation

Article 3 of the law of 23 December 1998 creating a *Commission de surveillance du secteur financier* as amended appointed it, inter alia, to deal with and participate in the negotiations concerning problems involving the financial sector, at both European Union and international level. In accordance therewith, the CSSF participates in the work of the following bodies.

1. Co-operation within European institutions

1.1. Groups attached to the European Commission

1.1.1. The Banking Advisory Committee

The Banking Advisory Committee was established by article 11 of the first banking co-ordination directive (Directive 77/780/EEC). It is made up of decision makers of the highest level in the banking supervisory and regulatory authorities of each Member State. It was chaired by Mrs Tumpel-Gugerell of the Austrian Central Bank until June 2003. Mr Roldan of the Spanish Central Bank was elected as interim chairman until December 2003. Mr Guill, Luxembourg Treasury Director, was elected chairman on 10 December 2003. The Committee's mission is to assist the European Commission in the proper implementation of directives and in the preparation of new proposals for directives. In addition to this consultative function, the Committee assumes a regulatory role in the comitology procedure as part of the executive power of the European Commission. The Committee is not entitled to examine specific problems concerning individual credit institutions.

During 2003, the Committee was informed several times by the European Commission on developments in the new supervisory and regulatory architecture as far as banking is concerned.

Following the publication on 5 November 2003 of the proposal for a directive aiming notably at reforming the Banking Advisory Committee into a level two committee within the framework of the implementation of the Lamfalussy process concerning banking supervision, the representatives of supervisory authorities and central banks will not participate in the works of the Banking Advisory Committee as from 2004. Indeed, the latter will constitute the members of the Committee of European Banking Supervisors, which is the level three committee within the scope of the Lamfalussy structure as regards banking supervision.

As far as the works accomplished in 2003 are concerned, the Committee has been kept informed as in the past on the development of the prudential supervisory systems and the legislative framework of the applicant countries for membership in the EU.

The Committee continued to discuss the review of the regulations concerning own funds, initiated in 1998 concurrently with the work of the Basel Committee on Banking Supervision. The members of the Committee regularly discussed the progress reports provided by the technical subgroup and its working parties. The Committee discussed the question of the most appropriate legislative approach with regard to capital adequacy and the question of prudential supervisory convergence.

The European Commission regularly submitted verbal reports to the Committee on the progress of the action plan concerning financial services.

The Committee continued to follow the development of the banking sector's solvency in Member States, by means of the annual report prepared by the contact group. Additionally, the Committee examined the report developed by the contact group on outsourcing of banking services.

In 2003, the Committee assumed only once its regulatory function within the framework of the implementing powers of the European Commission in the application of the comitology procedure.

1.1.2. The Committee of European Banking Supervisors

The Committee of European Banking Supervisors (CEBS) has been established by the European Commission Decision 2004/5/EC of 5 November 2003. It is in charge of reflecting, discussing and giving advice to the European Commission in the fields of banking regulation and supervision. The Committee also cooperates with the other competent committees in banking matters, notably with the European Banking Committee instituted by European Commission Decision 2004/10/EC. The CEBS is chaired by Mr José-María Roldan (Banco de España, Spain). The Vice-Chair is Mrs Danièle Nouy (Commission Bancaire, France). Mr Andrea Enria (Banca d'Italia) has been appointed General Secretary. The Chair is supported by a 'Bureau', comprising Mr Andres Ittner (Oesterreichische Nationalbank, Austria), Mr Helmut Bauer (Bundesanstalt für Finanzdienstleistungsaufsicht, Germany) and Mrs Kerstin af Jochnick (Finansinspektionen, Sweden). The Committee's Secretariat will be based in London.

CEBS took up its duties in January 2004 and held its first meeting in Barcelona on 29 January 2004. The CSSF is represented by Mr Arthur Philippe, Director.

The CEBS will fulfil the functions of Level 3 Committee for the banking sector in the application of the Lamfalussy process.

The role of the Committee is to:
- advise the European Commission either at the Commission's request, within the time limit which the Commission may lay down according to the urgency of the matter, or on the Committee's own initiative, in particular as regards the preparation of draft implementing measures in the field of banking activities;
- contribute to the consistent application of Community directives and to the convergence of Member States' supervisory practices throughout the Community;
- enhance supervisory co-operation, including the exchange of information.

The CEBS is composed of high-level representatives from the banking supervisory authorities and central banks of the European Union. The EU acceding countries will participate as observers until 1 May 2004. The European Economic Area (EEA) countries will participate as observers on a permanent basis.

1.1.3. The *Groupe de Contact*

The *Groupe de Contact*, which has been created in 1972, is at the origin of informal co-operation on Community level and comprises representatives of the banking supervisory authorities of Member States. It is chaired by Mr Keith Pooley of the FSA (United Kingdom) since 2002, year of the *Groupe's* 30th birthday.
The *Groupe*, which is a body appreciated for informal exchanges concerning the situation of individual credit institutions, particularly in the event of problems, follows the development of national regulations, discusses practical aspects of prudential supervision of credit institutions and conducts general comparative studies.
Within the new European structure of the regulation of the banking sector, the *Groupe de Contact* will henceforth also act as main working group of the Committee of European Banking Supervisors and, in that capacity, assist the Committee with a view to achieve convergence of the prudential supervisory practices in the European Union.

In 2003, the *Groupe de Contact* continued to focus on the implementation of the supervisory review process, the second pillar of the new capital adequacy framework at Community level.

Following the development of high-level principles in this field, the group started to study different elements, i.e. the capital adequacy assessment process, the evaluation process and the risk assessment system of the supervisory authorities. The results of this study will soon be submitted to the Committee of European Banking Supervisors.

The *Groupe* has also developed high-level principles in the important area of outsourcing of banking functions. As far as comparative studies are concerned, the *Groupe* conducted its annual study on the solvency of credit institutions in the European Economic Area.

1.1.4. The Contact Committee on Money-Laundering

The Contact Committee on Money-Laundering met twice in 2003. The meetings and discussions of the Committee notably focused on the revision of the Forty Recommendations of the Financial Action Task Force concerning the fight against money laundering (FATF) and on subjects the European Commission could take into account when drafting the third directive on the fight against money laundering.

1.1.5. The Contact Group on UCITS

In 2003, the Contact group on UCITS, chaired by the European Commission, met five times in Brussels. During these meetings, discussion namely concentrated on the responses of the prudential supervisory authorities to the questionnaires on UCITS tracking an index, funds of funds, monetary market instruments and deposits with credit institutions.

The report of the task force on the use in financial derivative instruments, as well as the report of the working group on the simplified prospectus have been finalised. It is planned that the European Commission issues recommendations based on the conclusions of these reports.

The task force on the use of derivative financial instruments has been set up in order to achieve a common interpretation, notably as regards the following seven points:
- limitations of leverage through the use of financial derivative instruments under articles 36 and 21(3) of the amended directive 85/611/EEC;
- definition of global exposure linked to derivative instruments under article 21(3) of the amended directive 85/611/EEC;
- definition of exposure under paragraphs 2 and 3 of article 21(3) and article 22 of the amended directive 85/611/EEC;
- definition of cover;
- identification of transactions in financial derivative instruments for hedging and application of investment restrictions;
- methodologies for assessing counterparty risk;
- use of financial derivative instruments by passively managed UCITS.

The task force on the simplified prospectus has been set up to agree on a common interpretation, notably as regards the following four points of schedule C annexed to the amended directive 85/611/EEC:
- definition and presentation of information concerning the investment strategy of the UCITS and brief assessment of the UCITS' risk profile;
- definition and presentation of the UCITS' historical performances, including the use of benchmarks;
- definition and presentation of costs (fees and commissions), including the use of a Total Expense Ratio (TER);
- other important aspects (multiple-compartment UCITS, Exchange Traded Funds, tax system).

The conclusions of the report of the task force on the simplified prospectus led to a common interpretation on the majority of the points discussed. As regards the points on which no consensus could be reached, the report concludes that several interpretations are admitted.

Moreover, the Contact Committee drew up questionnaires on the regulations applying to management companies. These questionnaires aimed at collecting the opinion of the prudential supervisory authorities on the requirements concerning the taking up of this activity, the capital requirements, the activities, the conditions to outsource functions, the European passport and conflicts of interests.

1.1.6. The Working Group on the Interpretation and Application of the Banking Directives (GTIAD)

The Group held two meetings in 2003, which concentrated on directive 2000/46/EC on the taking up, pursuit and supervision of the business of electronic money institutions. The discussions notably aimed at defining the applicability of the directive to mobile telephone operators who provide, besides services relating purely to vocal telephony, supplementary services which are likely to fall under the scope of the directive. The discussions resulted in the consensus to publish, following the agreement of the Banking Advisory Committee, a public consultative document containing possible solutions as regards the application of directive 2000/46/EC to these particular cases.

1.1.7. The expert group on payment systems

The *ad hoc* group met twice in 2003 in order to prepare notably the public consultation paper concerning a new legal framework for payments within the single market. The public consultation having been closed in mid February 2004, the group will be kept informed on the responses of the different professional and consumer representations in the coming months.

1.1.8. The Mixed Technical Group on Financial Conglomerates

The technical group, which held three meetings in 2003, focused on the problems that arose within the context of the transposition of directive 2002/87/EC on the supervision of financial conglomerates, notably as regards the interpretation of different provisions of the directive. A working subgroup started to study the scope of the equivalence of the regulations and supervision of financial conglomerates of certain third countries, while another subgroup surveyed the financial conglomerates likely to fall under the scope of the directive.

1.1.9. The Contact Committee on accounting directives

The committee met once in 2003. The discussions mainly focused on questions and answers relating to the IAS regulation and the accounting directives. The European Commission has published these questions and answers in November 2003 in the form of observations concerning certain articles of the IAS regulation, as well as the 4th and 7th directive.

1.1.10. The Accounting Regulatory Committee

The Accounting Regulatory Committee, set up by the European Commission in accordance with article 6 of the IAS regulation, held four meetings in 2003. The agenda mainly focused on the IASB standards projects and a presentation thereon by EFRAG, the European Financial Reporting Advisory Group. At the meeting of 16 July 2003, the committee adopted all the international accounting standards including related interpretations, except for the IAS 32 and 39 dealing with the accounting and disclosure of financial instruments, and the related SIC 5, 16 and 17. The IAS standards 32 and 39, which were severely criticised by the financial sector, have not been included, as they have been submitted for review by IASB, in co-operation with European accounting experts.

1.1.11. The Peer Review Group

In the context of its expansion, the European Union assesses the extent to which the legislation and prudential supervisory policies of candidate countries comply with the existing Community rules. It also verifies the implementation and application of Community rules in candidate countries. To this end, the European Commission asked the supervisory authorities of Member States, the 'peers', to assess the relevant authorities of the candidate countries. For each candidate country, six authorities competent to supervise the financial sector (banks, financial markets and insurance) and a representative of the European Commission form a peer review team that visits the country concerned in order to meet the equivalent authorities and to assess their missions and responsibilities and how they operate (authorisation, on-site inspections, ability to impose sanctions).

The European Commission requested a reduced team of supervisory authorities of Member States to assess the measures taken by the candidate countries' authorities following the recommendations given by the peer review team in 2001 and 2002.

The CSSF took part in the reduced group's Securities Team that visited Cyprus from 13 to 15 March 2003 to assess, in co-operation with its Greek equivalent, the Capital Market Commission, the progress made by Cyprus as regards the legislative framework and the supervision of securities markets. The CSSF took also part in the Securities Team of the reduced group that visited Latvia from 5 to 7 May 2003 to follow-up on the legislative framework and the supervision of the Latvian securities markets.

1.2. Groups operating at European Union Council level

The CSSF is a member of the groups working on proposals for directives concerning financial services. The groups of government experts meeting at Council level play an important role in the Community legislative process, since they format the consensus texts, referring only political difficulties to the Permanent Representatives Committee and the Council of Ministers of Finance. The groups are chaired by a representative of the Member State, which presides the Council. Greece thus presided during the first half of 2003 followed by Italy during the second half. The list of directives under negotiation at Council level and a brief description thereof can be found in chapter XI.

1.3. The Banking Supervision Committee of the European Central Bank

The Banking Supervision Committee of the European Central bank is a committee made up of representatives of the banking supervisory authorities and the central banks of Member States. It is chaired by Mr Meister, a member of the Board of Directors of Deutsche Bundesbank. The missions concerning prudential supervision conferred by the Treaty and the statutes of the European Central Bank on the ESCB (European System of Central Banks) are carried out by the Banking Supervision Committee on behalf of the ESCB. The Committee is a forum for the exchange of opinions on the supervisory policies and practice in Member States. It should also be consulted on proposals for directives and bills tabled by Member States affecting matters within its competence.

In carrying out its mandate in 2003, the Banking Supervision Committee was assisted mainly by two working groups made up of members of central banks and national supervisory authorities, namely the Working Group on Macro-Prudential Analysis and the Working Group on Developments in Banking.

In order to systematise the analysis of macroeconomic data with a view to identifying in reasonable time and as far as possible the factors likely to weaken the financial institutions as a whole and therefore the financial system, the Working Group on Macro-Prudential Analysis monitors the macroeconomic environment and reports to the Committee on trends and facts likely to be relevant to the prudential supervision of the financial sector.

Each year, the working group draws up a report on the stability of the financial sector. This report, which has been prepared under the aegis of the committee for two years now, is also discussed by the Executive board of the European Central Bank.

In 2003, the group analysed more particularly the risks stemming from the failures of small- and medium-sized companies for the banking sector. Other analyses concerned the risks of a prolonged slowdown of the European economy, the persistent imbalances in the United States and the impact of the expected development of the real estate sector. The working group also initiated a study on derivative credits and other factors shifting the credit risk of the banking sector towards other sectors.

As in the previous year, the Working Group on Developments in Banking focused during the first half of 2003 on the drawing up of its structural report. This annual report aims to identify and monitor the structural trends marking the European banking sector as a whole. The 2003 report concentrated in particular on the impact of the economic slowdown on the dynamics of globalisation, consolidation and disintermediation of banking activities in Europe. During the second half of 2003, the group concentrated, as usual, on thematic analyses. Thus, it launched a study on the development of the bank-insurance phenomenon in Europe. The final report of this study is expected to be published in the second half of 2004.

2. Multilateral co-operation

2.1. The Basel Committee on Banking Supervision

2.1.1. The new capital adequacy framework

In 2003, the Basel Committee continued to concentrate its efforts on the new capital adequacy framework, resulting in the publication of a third consultative paper (CP3) on 29 April 2003. This publication coincided with the appointment of Mr Jaime Caruana succeeding Mr William McDonough as chairman of the Committee on 1 May 2003.

- **Results of the Quantitative Impact Study (QIS3)**

The third Quantitative Impact Study (QIS3), aimed at assessing the impact of the new rules before the publication of the third consultative paper, was launched on 1 October 2002. More than 350 banks from 43 countries volunteered to participate in that exercise.

The overall results of the QIS3 are presented in the document "Quantitative Impact Study 3 - Overview of Global Results" published by the Basel Committee on 5 May 2003. Following public interest in the QIS3 results, a supplementary document ("Supplementary Information on QIS3"), which provides more detail on some areas of the results, was published on 27 May 2003.

The Committee noted that the QIS3 results were overall consistent with the objectives and thus confirmed the decision to modify certain areas of the new regime as it was foreseen in the second consultative paper.

The participation of the CSSF in the QIS3

The CSSF has been a member of the working group entrusted with overseeing the quantitative impact studies of the New Basel Accord within the Basel Committee for Banking Supervision since the first QIS exercise. As regards the third quantitative impact study, the CSSF was one of the member countries involved in the technical aspects of setting up this *ad hoc* reporting.

At national level, the CSSF held a meeting at its premises with the so-called "systemic" credit institutions on 4 July 2002, in order to set the practical modalities of the study. The CSSF then invited, by means of its circular letter of 25 October 2002, all the credit institutions under Luxembourg law to carry out this impact calculation on a voluntary basis. Several Luxembourg responses have been sent anonymously to Basel in order to be included in the overall assessment.

The CSSF's objective however exceeded that of a simple calculation and also aimed at a qualitative assessment within the context of the supervision of credit institutions. Thus, each response was thoroughly analysed by CSSF agents, often at the premises of the participating banks. These visits also enabled both supervisors and the credit institutions to perform a first gap analysis with respect to the qualitative requirements of the Accord.

The first conclusions allowed to draw up a model questionnaire, part of which has been submitted to the credit institutions by means of the CSSF's circular letter of 17 December 2003.

Quantitative results of the QIS3 for Luxembourg credit institutions

The CSSF received 18 responses to the questionnaire, covering between 50% and 55% of the balance sheet total and of the banks' own funds, as defined in the numerator of the solvency ratio of the 122 Luxembourg-registered credit institutions that must comply with the solvency ratio defined by the CSSF as of 31 December 2002. The sample included a wide range of banks, from universal banks to specialised banks. The coverage of assets included in the study exceeded in any case 80% of the exposures of the institutions' individual consolidated or sub-consolidated balance sheets.

As regards credit risk, it has to be noted that 16 banks completed the Standardised approach, 10 banks the IRB Foundation and 3 banks the IRB Advanced approach. 14 banks were in a position to complete the Standardised approach for operational risk. None of the banks provided results on the Advanced Measurement Approach.

As far as credit risk is concerned, overall results are in line with those obtained for the other European Group 2 banks. Capital requirements thus increase by 8% for the Standardised approach (7% if account is taken of the changes introduced in CP3), mainly due to the increase in requirements on bank exposures and the newly introduced capital charge for operational risk, whose impact has been directly incorporated.

Capital requirements however decrease by 22% (21% according to CP3) in the IRB Foundation approach driven by the substantial reductions in the corporate and retail asset classes. It should also be noted that additional simulations have shown that capital requirements would decrease by 11% if banks applied the explicit maturity, reflecting an average maturity clearly below 2.5 years, notably for interbank exposures.

Capital requirements for operational risk reached 6.29% for the Basic Indicator Approach, and 6.11% for the Standardised approach. Results by bank substantially diverged and depended on the distribution of activities. Indeed, the distribution of requirements across business lines largely reflected their respective weighting levels (beta factor).

- **Results of the third consultation**

On 29 April 2003, the Committee published its Third Consultative Paper (CP3) containing an outline of the new capital adequacy rules. The results of this QIS3 entailed several modifications to the preceding version, i.e. the QIS3 Technical Guidance. Furthermore, the CP3 confirmed the favourable treatments of debtors who are individuals and small- and medium-sized companies, as proposed in the latter, but not included yet in the CP2.

During this consultation period, which ended on 31 July 2003, more than 200 responses were received, the majority of which confirmed their support for the overall structure of the New Accord, as well as the need to adopt a more risk-sensitive regulatory framework.

Following the analysis of the responses, the Basel Committee published a press release on 11 October 2003 announcing its intention to solve, by the end of 2004, when the New Accord is expected to be published, the problems identified and to improve several aspects of the new framework that have been criticised. The implementation date of 31 December 2006 has been maintained.
The press release also invites the banks to comment on the new calibration proposal of the IRB approach, according to which the capital requirements would be based solely on the unexpected loss portion.

From October 2003 onwards, the Committee and its subgroups working on the Accord concentrated on the following issues:
- changing the calibration of the IRB approach which will be based solely on unexpected losses (UL);
- simplifying the treatment of securitisation under the IRB approach;
- revisiting certain aspects of the rules concerning credit risk mitigation.

- **The subgroups working on the revision of the Accord**

Working Group on Overall Capital and Quantitative Impact Study

The group stems from the merger of the Working Group on Overall Capital, entrusted with the calibration of the New Accord as a whole, with the Working Group on Quantitative Impact Study, which concentrates on the quantitative impact studies. Since the publication of the third consultative paper and the results of the third impact study, the group has been charged with verifying the impact of the provisions, as well as the coverage of expected losses under the two internal ratings-based approaches.

Working Group on Expected Loss/Unexpected Loss

This working group has been entrusted with analysing all the technical details related to the shift from the approach consisting in measuring risk-weighted assets based on expected and unexpected losses, towards a measurement based solely on unexpected losses, as mentioned in the press release of the Basel Committee of 11 October 2003.

Securitisation Group

In 2003, the Securitisation Group mainly focused on the development of methods of securitisation treatment under the IRB approach. It took into account the comments submitted by the banking sector on the third consultative round in order to draw up a new formula to calculate the capital requirements of the tranches, which are not externally rated, and to define the risk weightings applicable to the listed tranches. Furthermore, the group paid particular attention to the development of the treatment of liquidity lines under the Asset-Backed Commercial Paper programs.

Risk Management Group

In 2003, the group carried out an extensive working program with a view to implement the AMA approach. In this context, it focused in particular on taking into account the insurance policies as operational risk mitigation technique, as well as on the problem concerning the application of the AMA approach in a cross-border context (approval/acceptation by the host authorities of the advanced method as regards subsidiaries of international banking groups).

In order to respond to the concerns of the banking industry, the group prepared a document, in conjunction with the Accord Implementation Group, dealing with this issue, which has been published for consultation with the banking industry.

Furthermore, the working group published the document "Sound Practices for the Management and Supervision of Operational Risk" in February 2003. The consultation paper "Principles for the Management and Supervision of Interest Rate Risk" was published in September 2003 for a short consultation period with the industry before being finalised.

Accord Implementation Group

In August 2003, the Accord Implementation Group published, under the aegis of the Basel Committee, the document "High-level Principles for the Cross-Border Implementation of the New Accord". In order to respond to the concerns of the banking industry regarding the application of the New Accord for banking groups operating on a cross-border basis, the document sets out six guidelines governing the functioning of the cross-border application of the New Accord.

The first principle provides that the New Accord will modify neither the legal responsibilities of the national supervisory authorities as regards the regulation of banking institutions under their competence, nor the consolidated supervisory regime as already set up by the Basel Committee on banking supervision. Thus, the home country supervisor is responsible for the

implementation of the New Accord by all the banking groups on a consolidated level, while it is in the host country supervisor's interest to accept the methods and approval processes that the bank uses at a consolidated level in order to reduce the compliance burden and avoid any regulatory arbitrage.

An enhanced and pragmatic co-operation should be established between the supervisory authorities with legitimate interests. The home country supervisors should lead this coordination effort.

Another principle provides that the supervisory authorities should avoid, as far as possible, to perform redundant and uncoordinated approval and validation work in order to reduce the implementation burden on the banks and spare supervisory resources.

Transparency Group

In the beginning of 2003, the Transparency Group mainly focused on fine-tuning pillar 3 of the New Accord (market discipline) for the publication of the third consultative paper of the Committee on 29 April 2003.

From August 2003 onwards, i.e. following the end of the consultation period, the group started to study the comments received. During this period, which should lead to a refined version of the disclosure requirements, the Group actively co-operated with the banking industry.

Owing to its direct involvement in the IASB advisory group charged with the review of the IAS 30, the standard setting disclosure rules for financial activities, the Transparency Group continued its pursuit to achieve maximum harmonisation between the accounting requirements and those of pillar 3. As the IASB has decided to use general principles requiring the disclosure on main financial risks instead of detailed requirements, the risk of incompatibility has been substantially reduced.

Moreover, the Transparency Group carried out its annual survey on disclosure practices on a sample of credit institutions of Member States of the Basel Committee on Banking Supervision. The results of the study will be published as a summary report.

Subgroup on Credit Risk Mitigation

Before the publication of CP3, the Subgroup on Credit Risk Mitigation finalised certain proposals relating to the treatment of repo-style transactions, as well as to the treatment of credit derivatives. Since the end of the third consultation round, the Subgroup concentrates on revising certain aspects of the rules concerning credit risk mitigation techniques considered as unsatisfactory, with a view to publish the final version of the new capital adequacy regime.

- **New developments in January 2004**

In its press release of 15 January 2004, the Basel Committee gave an overview of the decisions taken during their meeting that day. The industry welcomed the new treatment for expected (EL) and unexpected (UL) losses proposed in October 2003 and the works on its implementation continues. Furthermore, concrete proposals have been made to simplify the treatment of securitisation under the IRB approach; a detailed technical note is being drawn up. Finally, the Committee explains its viewpoint on the implementation of the second pillar of the New Accord.

2.1.2. The other subgroups of the Basel Committee

- **Accounting Task Force**

The Accounting Task Force is in charge of following-up on the developments in the accounting and auditing areas. There are two aspects to its mandate:

- following-up on the work of accounting and auditing standards setters that are of particular interest to the financial and banking sector, notably the work of the International Accounting Standards Board (IASB) and of the various committees, including notably the International Auditing and Assurance Standards Board (IAASB), that are operating under the aegis of the International Federation of Accountants (IFAC);
- developing principles and guidelines in the areas of accounting, auditing and, more recently, compliance.

As regards the follow-up on accounting standard setters, the Task Force's main focus continued to be on the rules applying to financial instruments (IAS 32 and IAS 39 standards).

During regular contacts with representatives of the IASB, the Accounting Task Force endeavoured to raise the accounting standards setters' awareness with regard to certain issues that are of particular interest to prudential supervisors, notably the area of provisioning and the issues in relation to the introduction of the fair value option. Besides these prudential aspects, the group also concentrated on the exposure-draft of the IASB proposing a method for the accounting treatment of the portfolio hedge of interest rate risk. The Task Force also contributed to the dialogue between the IASB and the banking industry, inter alia by means of a comment letter.

The Accounting Task Force also addressed other IASB draft standards, including the "Exposure Draft 2 Share-based Payments" and the "Exposure Draft 5 Insurance Contracts". Other developments in relation to the IASB are monitored through the participation of Basel Committee representatives in the Standards Advisory Council.

Furthermore of interest in the area of accounting is the ongoing work on a study on the impact of the accounting standards IAS/IFRS on regulatory capital; the study should be finalised during 2004.

As regards auditing, it is worth pointing out that several comment letters have been sent, as well as the significant contribution to the work on reforming the IFAC's structure and the creation of its oversight body, the Public Interest Oversight Board.

The Group also received the mandate from the Basel Committee to develop principles concerning the compliance function. A consultation paper thereon has been published in October 2003. The Committee proposes a definition of the compliance function as well as guidelines, in the form of best practice principles, with a view of establishing such a function. The proposed principles deal more specifically with the responsibilities of the governing bodies, the status of the function, its independence, its roles and responsibilities, organisational aspects, cross-border issues, the relationship with the internal audit department, as well as outsourcing issues. The final version of the paper is expected to be published this year.

- **Working Group on Cross-Border Banking**

The Working Group on Cross-Border Banking, which is a joint working group of the Basel Committee and the Offshore Group of Banking Supervisors, drafted a reasoned opinion for the Basel Committee on the methodology to assess the compliance with the forty revised FATF recommendations to combat money laundering and terrorist financing.

Furthermore, the Group continued to prepare guidelines based on the "Customer due diligence for banks" document published in October 2001 and which resulted in the publication of the consultation paper "Consolidated KYC Risk Management" in August 2003. This document

stresses the importance for banks to apply the four principles governing a sound know-your-customer programme to all the entities of the banking group, namely:
- customer acceptance policy;
- customer identification;
- on-going monitoring of higher risk accounts;
- risk management.

2.1.3. Other publications

The documents "Risk Management Principles for Electronic Banking" and "Management and Supervision of Cross-Border Electronic Banking Activities", prepared by the Electronic Banking Group of the Basel Committee, have been published in their final version.

The document "Risk Management Principles for Electronic Banking", prepared in May 2001, sets out the main points to comply with to ensure adequate risk control in the field of e-banking, i.e. an effective management by the decision-taking bodies of the financial institutions, security controls (non-repudiation, authentication, etc.), as well as legal and reputational risk management.

The document "Management and Supervision of Cross-Border Electronic Banking Activities" covers risk management and the supervision of cross-border e-banking activities. The banks' responsibilities as regards the management of the risks inherent in these activities have been identified. The document draws the attention on an efficient supervision of these activities by the supervisory authority of the home country and international co-operation between supervisory authorities.

2.2. The International Organisation of Securities Commissions (IOSCO) and IOSCO task forces

2.2.1. The XXVIIIth Annual Conference of IOSCO

The regulatory authorities of the financial and futures markets and other members of the international financial community met in Seoul, South Korea from 14 to 17 October 2003 on the occasion of the XXVIIIth Annual Conference of IOSCO.

The theme of the conference, "New Challenges for Securities Markets and Regulators", was chosen in recognition that recent high-profile corporate failures, as well as other world events, have raised important regulatory challenges that securities regulators must address. Maintaining the integrity of international capital markets is a crucial part of the main mission of securities regulators, which is investor protection. Recent events have demonstrated that the integrity of capital markets fundamentally depends on the quality of financial disclosures made by issuers and on the appropriate resolution of conflicts of interests faced by professionals. Maintaining the integrity of capital markets requires that regulators prevent the use of international financial markets for any form of international financial crime.

In the context of enhancement of international co-operation, essential to achieve this goal, IOSCO announced that substantial progress has been made since the last conference, which was held in Istanbul in May 2002. Forty members of IOSCO have applied to become signatories of the Multilateral Memorandum of Understanding on co-operation and exchange of information (the "MOU"), which had been adopted unanimously in May 2002. The applicants will undergo rigorous screening review of their ability to co-operate according to the standards set by the MOU. By committing themselves to this process, they express their commitment to take part in an efficient system of information exchange with the aim of fighting against breaches of stock exchange regulations and any other form of international financial crime. Twenty-four of these candidates have already signed the MOU.

2.2.2. Groups of the International Organisation of Securities Commissions

The CSSF is a member of two IOSCO groups, i.e. the Standing Committee n. 1, dealing with subjects concerning accounting, and the Standing Committee n. 5 concerning UCITS and collective management.

- **Standing Committee n. 1**

In 2003, the Committee participated, as far as auditing is concerned, in discussions on the creation of a Public Interest Oversight Board (PIOB). Four of the PIOB's members will be appointed by IOSCO.

Furthermore, the Committee monitored in particular the development of the IAS/IFRS standards by providing comments on the related projects. It closely co-operates with the International Accounting Standards Board (IASB). IOSCO encourages IASB and the international standard-setters to continue their co-operation to come to a convergence allowing to facilitate cross-border offers and quotations and to encourage regulators to cope with the more vast issues concerning the coherence of interpretations, the implementation of the accounting standards and the sanction of non-compliance therewith.

The main obstacle to the finalisation of the project of international disclosure standards for multinational offers and listings of bonds was the diverging regulatory approaches of the members. Consequently, the project has been amended and the work will continue in 2004 in order to provide, on the basis of the standards developed in 1998 for shares, an analysis of standards and an explanation of the goals of the different approaches of the regulators.

After having conducted a study on periodic and continuous information requirements on issuers whose securities are listed, the Committee concentrated on finalising high-level standards in this field.

- **Standing Committee n° 5**

In 2003, the Committee has finalised a study on index funds and has worked on the document "Elements of International Regulatory Standards on Fees and Expenses of Investment Funds" which should be approved soon. Moreover, the Committee discussed in detail the issues arising regarding investment funds in the context of anti-money laundering measures. Finally, a new mandate given to the Committee concerns the rules applicable to the mergers between investment funds in the different member jurisdictions.

2.3. CESR and groups established within CESR

2.3.1. CESR (Committee of European Securities Regulators)

Established by the European Commission decision of 6 June 2001, CESR took over from FESCO (Forum of European Securities Commissions) in September 2001. CESR is one of the two committees proposed in the report of the Committee of Wise Men, which was endorsed by the Stockholm resolution of 23 March 2001. Composed of representatives of 17 supervisory authorities of securities markets in the European Economic Area (Member States of the European Union, Norway and Iceland), CESR is an independent body, which assists the European Commission in preparing technical measures regarding Community legislation on transferable securities, and is entrusted with ensuring harmonised and continued application of Community legislation in Member States. CESR also works towards strengthening co-operation between the supervisory authorities.

INTERNATIONAL CO-OPERATION

In 2003, CESR concentrated its activities on work related to initiatives concerning the Financial Services Action Plan. In this context, CESR notably continued to concentrate on the mandates covering the development of implementing measures within the scope of the directive on insider dealing and market manipulation and the directive concerning the prospectus to be published when securities are offered to the public or admitted to trading.

CESR also started to work on the development of implementing measures concerning the Financial Instruments Markets Directive (ISD 2) by creating three expert groups, i.e. the expert group on intermediaries' issues, the expert group on markets and the expert group on co-operation and enforcement issues. The Steering Group ensures coordination between the three groups.

The Market Participants Consultative Panel, a committee gathering eleven members who are appointed in a personal capacity, was created in June 2002 following the recommendations of the European Parliament and the Committee of Wise Men, and assists CESR in the execution of these tasks. The committee held three meetings in 2003 on aspects concerning the Lamfalussy procedure, the consultation policy and the priorities and working methods of CESR and, on the other hand, more technical issues such as the disclosure obligation of quarterly reports, the so-called pre-trade transparency obligations under ISD2, clearing and settlement in Europe, the obligation of best execution and the execution-only activity.

CESR strengthened its initiatives regarding the integration of accession countries during the year by promoting their participation as observers in these groups. CESR recognised, within the scope of European legislative process, the need to start reflecting on its role and more particularly the Lamfalussy process.

Anticipating the adoption of the legal framework relating to the extension of the Lamfalussy procedure to the regulatory principles of collective management, as decided by the ECOFIN Council on 3 December 2002, CESR initiated on 30 October 2003 a consultation on its internal organisation, the organisation during the transitional stage and the areas in which CESR wished to start working as from now. In this context, CESR established an expert group on Investment Management.

Moreover, CESR held an *ad-hoc* meeting on the amended UCITS directive (UCITS III) in 2003, in order to discuss the topics where CESR could contribute to an enhanced co-operation between prudential supervisory authorities and to the common interpretation of the amended UCITS directive. During this meeting, CESR identified the areas and priority work streams it aims to concentrate on, in a first stage, in the field of investment funds.

In particular, CESR identified four general principles guiding its work:
- any work accomplished by CESR regarding the amended UCITS directive would have to be conducted in full coherence with the EU institutional framework;
- CESR should take a global vision of the so-called buy-side, referring to collective and individual management;
- CESR should not start to work on matters where the UCITS Contact Committee is about to finish its work;
- account should be taken of the work already accomplished by IOSCO.

The following four areas have been identified as priorities:
- areas where input could be provided to the UCITS Contact Committee (delegation of functions, depositaries, scope of the European passport for management companies, money market instruments, UCITS tracking an index);
- areas where convergence of prudential supervisory practices and techniques should be achieved (elaboration of common prudential supervisory techniques by exchange of experience, notably in the area of risk management, marketing policy, fee structures, conflicts of interest);
- areas not covered by the UCITS directive (hedge funds, real-estate UCIs);
- areas where consistency with the EU legal framework and the other EU directives should be

achieved (investment services directive, e-commerce directive, distance marketing directive, impact of the International Accounting Standards).

CESR will start working in an *ad-hoc* working group and will also consult with a consultative group of market participants.

Following this meeting, CESR published a consultation paper on its role in the regulation of UCITS and asset management activities in Europe.

2.3.2. CESR expert groups

- The **Review Panel**, established by the Presidents of CESR following the decision of December 2002, is mandated to assist CESR in its task to ensure coherent and equivalent implementation of Community legislation in Member States. In 2003, the Review Panel has started its work with the scrutiny of the status of implementation of the CESR standards for Alternative Trading Systems and the rules of conduct in Member States.

- Carrying out an additional mandate regarding the directive on insider dealing and market manipulation, the **Market Abuse** expert group submitted its additional technical advice on implementing measures on 3 September 2003. The European Commission, in conjunction with the European Securities Committee and the European Parliament, will use this advice to establish implementing measures for the directive on market abuse. In accordance with the consultation policy recommended by the Committee of Wise Men and adopted by CESR, the project, published in April 2003, was submitted to professionals of the various Member States. The group has taken account of their comments (a public hearing was held and around hundred responses received) to finalise the document.

The document covers the following points:
- guidelines to determine accepted market practices according to the directive;
- definition of inside information for derivatives on commodities;
- maintenance of insider lists by issuers;
- disclosure of transactions by senior managers;
- obligation to report suspicious transactions to the regulator.

A consultative working group, composed of representatives of investors and market participants, including one representative of the Luxembourg Stock Exchange, assisted the expert group with drawing up the advice.

A mandate relating to the future work to be carried out under level 3 of the Lamfalussy procedure as regards the directive on insider dealing and market manipulation was given to CESRPOL in December 2003. CESRPOL is a permanent group within CESR, responsible for enhancing the exchange of information, coordination of surveillance and enforcement activities between CESR members.

- The **Prospectus** expert group, created in December 2001, has responded to the provisional mandates of 27 March 2002 and 7 February 2003 under the directive on the prospectus to be published when securities are offered to the public or admitted to trading, in accordance with the three deadlines that had been set: 31 July 2003, 30 September 2003 and 31 December 2003. Both mandates were formalised on 31 October 2003 following the adoption of the directive. The group took into account the 320 responses received and held three public hearings in the course of its consultation process.

The technical advice of the group covers the following six areas.

- The format of the prospectus.
  CESR elaborated details concerning the presentation of the prospectus as a single document or three separate documents (registration document, securities note, summary), as well as the presentation of a base prospectus with supplements. CESR also provides a road map for

companies, facilitating the identification of information to include in the prospectus for each type of issue.

- Minimum information to be included in the various prospectus schedules according to investor needs.
  CESR proposed schedules for shares, retail and wholesale bonds, asset backed securities, banks non-equity, certificates issued on shares, derivatives securities, programs, units issued by closed-ended investment funds, securities issued by states as well as their regional or local authorities and securities issued by supranational institutions. These schedules are supplemented by building blocks in particular cases, such as guarantees, pro forma information, underlying equity. Particular importance has been attached to the historical financial information to be included.

- Annual information.
  CESR proposed different means to publish the document that contains or mentions all information published during the year, taking account of the goals pursued by this publication and of rapid and cheap access for investors.

- Incorporation by reference.
  CESR proposed the possibility to include by reference published information such as auditing reports, financial reports and articles of incorporation. Moreover, CESR considers that the prospectus and the documents incorporated by reference must be linguistically coherent.

- Publication of the prospectus.
  CESR defined the provisions relating to the dissemination of the prospectus and proposed indications to include in the advice.

- Advertisements.
  CESR chose to allow the use of all means of advertisement without imposing a ban before the publication of the prospectus.

This advice was integrated in a first stage into a working document that was published for comments by the European Commission in November 2003, and in a second stage, in formal proposals of the European Commission on the implementing measures of directive 2003/71/EC on prospectuses, presented in January 2004 in the form of a proposal for a regulation subject to the vote of the European Securities Committee.

- Under the oversight of a **Steering Group** and with the assistance of a consultative group consisting of 23 external experts (including one representative of a Luxembourg professional of the financial sector), three expert groups responded to the provisional mandate on the directive concerning financial instruments markets (ISD 2). These mandates were published by the European Commission on 20 January 2004.

The provisional mandates cover three main areas:
- the obligations for financial intermediaries (Intermediaries group);
- the transparency rules on financial markets (Markets group);
- the requirements for reporting on transactions and co-operation within the scope of the supervision of financial markets (Co-operation and Enforcement group).

The **Intermediaries** expert group addresses the comitology provisions relating to the internal organisation of financial intermediaries with the aim of protecting the investor. Two approaches aim at reaching this goal:
- an "internal" approach covering the organisational requirements, rules of conduct of business obligations when providing investment services to clients and the management of conflicts of interest;
- an "external" approach covering best execution of client orders and client order handling rules.

The **Markets** expert group is charged with:
- establishing criteria to set up transparency rules for the admission of securities to the regulated markets and defining the means to establish to control compliance with these rules;
- elaborating technical measures relating to the pre- and post-trade transparency requirements for regulated markets and multilateral trading facilities and post-trade transparency requirements for investment firms.

The **Co-operation and Enforcement** expert group concentrates on the following two areas:
- means to be established at national level to allow for the supervision of markets, mainly by elaborating the content of information relating to transactions (on and off stock exchanges) to be reported by the financial intermediaries to the competent authority;
- co-operation between supervisory authorities of Member States by covering the exchange of information as regards securities transactions, as well as exchange of information concerning the approval and activities of financial intermediaries.

The groups started their work by identifying the areas of convergence and divergence respectively, in the current regulations through questionnaires relating to the different areas covered. The first projects had been presented to the consultative group in January 2004 to collect the advice of these market participants before elaborating a more detailed technical advice. The consultation by means of working documents is due to be launched in June 2004 so as to comply with the deadline of 31 January 2005 set by the European Commission to submit the technical advices.

2.3.3. Permanent CESR groups

- **CESRFIN**, the permanent committee on financial reporting, continued its work on international accounting standards (IAS/IFRS), auditing and financial disclosure by listed companies, considering that the transition to international accounting standards will represent a major challenge for the 7,000 European listed companies. The introduction of international standards will improve transparency and comparability of financial information. The markets and investors will need to adapt to the new way financial information is presented and their correct enforcement should remain a high priority for supervisory authorities.

In 2003, the subgroup CESRFIN-Endorsement continued to closely follow the discussions and work concerning the IAS/IFRS standards and their enforcement at community level and expressed many comments and suggestions. Within the framework of the transition of listed companies to the international accounting standards IAS/IFRS in 2005, the sub-group issued on 30 December 2003 a recommendation for the transitional stage based on three main lines:
- the information a company can disclose before 1 January 2005 to inform the investors about the impact of the new accounting principles;
- the accounting rules to be applied to interim financial reports in 2005;
- the comparability between interim and yearly financial reports for 2005.

Following the publication in March 2003 of the first standard relating to financial information and dealing with the supervision of implementation of accounting standards in Europe, the sub-committee CESRFIN-Enforcement launched a consultation process on a second standard relating to financial information in October 2003. The standard proposes principles set to enhance coordination of enforcement practices of accounting standards in Europe, notably:
- that the supervisors should take into account the existing decisions and, where practicable, discussions should take place between authorities;
- that a database providing a record of previous decisions should be made available, on a confidential basis, to the different authorities;
- that regular sessions should be held between the different bodies concerned in the decision process, thus allowing to discuss the decisions taken and to share experience.

- **CESRPOL**, responsible for enhancing the exchange of information, co-operation and co-ordination of the supervision and enforcement activities between members of CESR, held three meetings in 2003.

One of the main aspects of the activities of CESRPOL was the adoption of the format for a request for assistance and of criteria for treating these requests under the Memorandum of Understanding (MoU) of FESCO (predecessor of CESR) concluded on 26 January 1999.

Moreover, CESRPOL concentrated on updating the MoU in the light of the implementation of the Financial Services Action Plan, the priorities of the enforcement of legislative provisions in Member States, the Internet surveillance activities in order to detect unlawful financial activities, the problems with un-cooperative jurisdictions, as well as the possible impacts of the European Convention on Human Rights.

Responding to a mandate given by the group of presidents of CESR during its meeting on 11 and 12 December 2003, CESRPOL will elaborate more detailed measures relating to the defensive means against market abuse and accepted market practices in 2004, in accordance with level 3 of the Lamfalussy process. CESRPOL will regularly review the safe harbours within which prohibitions of market abuse do not apply. Furthermore, CESRPOL will analyse national and cross-border market abuses on a regular basis.

2.3.4. Joint CESR-ECB working group on compensation and securities settlement systems

On 27 September 2001, the European Central Bank (ECB) and CESR drafted the framework for co-operation between the European System of Central Banks (ESCB) and CESR as regards compensation and securities settlement systems in order to study subjects of common interests.

Following several meetings in the first half of 2003, the joint working group published a consultative report in July 2003 on the CESR website (www.cesr-eu.org). Following this publication, the working group held a public hearing at the beginning of October 2003 and received about fifty formal responses to the consultative report. These responses are dealt with as from the beginning of 2004 at the next meetings of the consultative group.

2.4. The informal groups

The Prospectus informal contact group

In 2003, the members of the informal contact group shared their points of view on three subjects, notably the prospectus itself, the public offers and the issues concerning markets in general.

As far as the prospectus itself is concerned, the discussions mainly focused on the use of a summary prospectus and the period of time needed by the competent authorities to approve prospectuses, as well as the issue of public offers without prospectus.

The development of the proposal for a directive on the prospectus to be published when securities are offered to the public or admitted to trading, as well as the proposal for a directive on takeover bids have also been discussed.

Finally, the discussions concerned the rules applicable to market makers, rating-based issues, information required in case of multiple listing in several States, of which one is not part of the European Economic Area, equivalence of information in case of multiple listings and allocation of shares by Internet and the publication of this information by the issuers on their website.

2.5. Institut Francophone de la Régulation Financière (IFREFI)

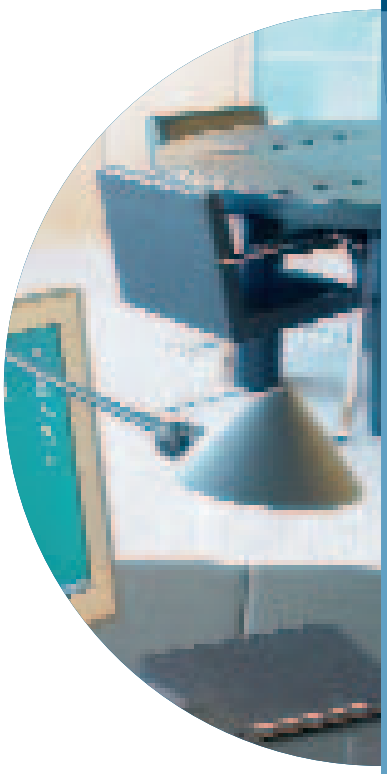
The I*nstitut Francophone de la Régulation Financière* (Francophone Institute for Financial Regulation), gathering the financial markets regulatory authorities of nine French-speaking countries (Algeria, Belgium, France, Guinea, Luxembourg, Quebec, Morocco, Switzerland and the West African Monetary Union) was created in 2002 by a charter.

IFREFI is a flexible structure of co-operation and dialogue and aims at furthering the exchange of knowledge and experience, drawing up studies and exchanging essential information relating to the financial markets between the Member States of the Institute. According to the charter, IFREFI also aims at promoting professional training by organising training seminars on specific topics.

During their annual meeting which was held in Montreal in June 2003, the presidents and representatives of the Francophone regulatory authorities discussed the current concerns of the world of finance following the failures of supervisory systems of general management and boards of directors of companies, notably corporate governance, as well as the scope of intervention of the regulators in this area.

CHAPTER XI

BANKING AND FINANCIAL LEGISLATION AND REGULATIONS



1. Directives under discussion at Council level
2. Directives adopted by the Council and the European Parliament but not yet implemented under national law
3. Laws passed in 2003
4. Circulars issued in 2003
5. Circulars in force

1. Directives under discussion at Council level

The CSSF participates in the groups examining the following proposals for Directives:

1.1. Proposal for a Directive on financial instruments markets (ISD 2)

On 19 November 2002, the European Commission, within the framework of the Financial Services Action Plan, adopted a proposal to modernise the investment services Directive following a large consultation of the sector that lasted two years. The initial designation of the Directive concerning investment services and regulated markets has been changed along the way into a Directive concerning financial instruments markets.

The Directive will increase harmonisation of national rules and give investment firms a veritable 'single passport', which will allow them to operate throughout the European Union on the basis of authorisation in their home Member State. It will also ensure that investors enjoy a high level of protection when making use of investment firms, wherever they are located in the European Union. It seeks to establish, for the first time, a comprehensive regulatory framework governing the organised execution of investor transactions by exchanges, other multilateral trading systems and investment firms.

Following the vote of the European Parliament approving the proposal at first reading, a political accord could be reached at the meeting of ECOFIN on 7 October 2003, notwithstanding the fact that five countries, including Luxembourg, voted against the proposal. The Council reached a common position on the proposal by qualified majority on 8 December 2003 and the proposal has been returned to the European Parliament for second reading.

As regards the highly controversial issue on the internalisation of orders by banks and investment firms, i.e. the execution of orders outside regulated markets, the common position subordinates the authorisation to match orders internally to a certain number of conditions. Thus, the common position limits the obligation to publish quotes to the systematic internalisers and proposes to extend the pre-trade transparency obligations to transactions whose size is not large in scale compared to the normal market size. As regards the suitability test, the common position sets out that a full suitability test must be carried out when a firm is providing investment advice, no suitability test will be performed for execution-only business and a less rigorous test for circumstances in between. The political accord also reflects a compromise on the issue of the application of the home country rule, in other words, of the areas where the activities of the investment firms should be monitored by the authorities of the Member State where they are situated and of those where the regulations of the host country where they perform the majority of their services should apply.

As a framework Directive, the Directive only sets the general obligations that the authorities of the Member States must impose. More detailed implementing measures will be laid down by the comitology procedure. The first provisional mandates have been published in January 2004 and a more detailed description can be found under point 2.3. "CESR and groups established within CESR" of Chapter X "International co-operation".

1.2. Proposal for a Directive on the harmonisation of transparency requirements with regard to information about issuers whose securities are admitted to trading on a regulated market (transparency Directive)

Following a first consultation in 2001 on the measures needed to harmonise the requirements for information that must be provided by the companies whose securities are traded on a regulated market and a second and last consultation in 2002, the European Commission presented a proposal for a Directive aiming at enhancing investor protection and transparency on 26 March 2003.

The proposal introduces minimum transparency requirements with regard to information that companies whose securities are admitted to trading on a regulated market must publish. It aims to enhance investor protection, attract investors to the European financial market and improve the efficiency, openness and integrity of European capital markets. It also aims at removing certain national barriers linked to transparency requirements, which may discourage issuers from having their securities admitted to trading on more than one regulated market in the European Union. In order to achieve these goals, the proposed Directive upgrades the current level and frequency of the mandatory financial information that issuers have to provide to the markets throughout the financial year. It will also simplify the obligations that issuers must meet regarding the use of languages and on the way information is disseminated.

During the discussions within the working groups of the Council, Luxembourg voiced concerns with respect to the disclosure requirement for quarterly reports, the requirements concerning IAS/IFRS, as well as the scope of application of the reporting of major shareholdings in listed companies.

1.3. Proposal for a Directive on takeover bids

On 16 December 2003, the European Parliament adopted the report of Mr Lehne on takeover bids, thus approving the entire informal compromise reached by the Council in November 2003. The long procedure to set up common provisions at European level regarding takeovers has achieved its goal. The text still needs to be adopted by the Council.

The text adopted by the European Parliament reflects many compromises by including a number of optional arrangements in order to take account of the substantial diversity in company law within the European Union.

The main goal of the future Directive concerns best protection of minority shareholders. In the initial proposal of the European Commission, a company that launches a takeover bid was obliged to buy the securities of minority shareholders at a "fair price", defined as being the "highest price paid for the same securities by the offeror […] over a period of between six and twelve months prior to the bid". According to the compromise reached at the Council and approved by the European Parliament, the definition of the fair price becomes more generous for the minority shareholders. If, after the bid has been made public and before the offer closes for acceptance, the offeror purchases securities at a price above the offer price, the offeror shall increase his offer to not less than the highest price paid for the securities so acquired.

The main amendments that have been adopted concern the use of defensive measures, the restrictions on votes and multiple voting rights, particularly the introduction of optional arrangements.

According to the proposal of the European Commission, the board members of the offeree companies were obliged to consult with their shareholders before taking any defensive action, such as the issue of new shares.

However, the European Parliament introduced the compromise consisting in the adoption of an amendment allowing Member States to make this provision optional, i.e. to reserve the

right not to require domestic companies to apply the provisions concerning defensive measures. But the companies will have the possibility in these Member States to apply these provisions, i.e. not to take defensive measures without obtaining permission from shareholders. Another exception: a company which has chosen to apply this rule, but would be the object of a takeover bid from a company which has not, would still have the possibility not to subject to this rule at that moment.

The multiple voting rights are another form of "defensive position". The European Parliament has adopted an amendment allowing multiple voting rights to be treated the same way as restrictions on voting rights. The companies and Member States can depart from these provisions, as is the case for defensive measures. Another amendment stipulated that where rights are being removed, equitable compensation must be provided for any loss incurred by the holders of these rights. The terms for determining such compensation will be set by Member States.

The future Directive does not address the golden shares held in major companies by certain European governments and sometimes used to block off takeover bids. They shall be the object of a separated Directive.

1.4. Proposal for a Directive in order to establish a new financial services committee organisational structure

The proposal for a Directive amending Directives 73/239/EEC, 85/611/EEC, 91/675/EEC, 93/6/EEC, 94/19/EC, 2000/12/EC, 2002/83/EC and 2002/87/EC, in order to establish a new financial services committee organisational structure aims at amending the current committee structure, established by the various sectorial financial services Directives.

Indeed, the European legislators and regulators of the banking, insurance and investment fund sectors have established a legislative and "comitology" regime that is ill-suited for an enlarged EU of 25 Member States. Even if this process were to be maintained, the present committee structure would still need to be adapted to new developments, for instance, by extending the scope of the Insurance Committee to occupational pensions. Legislators and regulators in these areas must be able to respond quickly and effectively to technological change and market developments, by adopting implementing rules on a much faster and more flexible basis.

In response to these challenges, the Council asked to reflect on the best way to improve the financial services committee architecture in April 2002. On the basis of this review, the Council invited the European Commission on 3 December 2002 to extend the committee structure applied in the securities sector to the banking, insurance and UCITS sectors. In particular, the Council invited the Commission to establish "as quickly as possible" new committees in each sector by means of Decisions.

In the securities sector, three pieces of legislation were used to implement this approach, in line with current interinstitutional practice and established precedents:

1) a Commission Decision establishing the Committee of European Securities Regulators (level 3);

2) a Commission Decision establishing the European Securities Committee (level 2) in advisory mode (level 1);

3) a European Parliament and Council Directive on market abuse subsequently establishing the European Securities Committee (level 2) as a committee assisting the Commission in the exercise of its implementing powers (level 2).

In the banking, insurance and UCITS sectors, however, the situation is complicated given the presence of committees (the Banking Consultative Committee (BCC), the Insurance Committee (IC) and the UCITS Contact Committee) established by and referred to in existing European Parliament and Council Directives, and acting in both advisory and "comitology" mode.

As a consequence, the European Commission has been careful to take an approach for the proposal for Directive, that:
- is institutionally and legally consistent with the approach used in the securities sector, and across the range of Community activities;
- avoids the risk of unnecessary complexity and duplication due to the overlap between existing and newly established committees;
- is consistent with the requests of the Council for committees to be set up as soon as possible in advisory capacity;
- is mindful of the concerns raised in the two Parliament Resolutions and gives the Parliament as co-legislator an equal right to decide on the move to a new financial services committee structure.

Thus, the Commission has concluded that the only way to reconcile these objectives in the banking and insurance fields, is by amending the provisions of existing sectoral Directives to repeal the existing committees and by establishing the new banking and insurance committees as committees assisting the Commission in the exercise of its implementing powers (level 2). At the same time, new banking and insurance committees are established in advisory mode (level 1) by two Commission Decisions. New committees of supervisors (Level 3) are established by two separate Commission Decisions.

In the UCITS field, this means amending the existing Directive to delete references to the UCITS Contact Committee and to transfer to the European Securities Committee (ESC) the role of "comitology" committee in this field, as well as the Commission Decisions relating to ESC and CESR (Committee of European Securities Regulators).

The Commission decided that the most effective and transparent means to ensure that such a simultaneous transfer takes place is to immediately adopt "suspensive" Decisions creating the new banking and insurance committees (level 1) and amending the ESC and CESR Decisions, but including clauses stipulating that these Decisions would only come into effect if and when an amending Directive of the type set out above also came into effect. This will ensure that there is no duplication of committees and that the establishment of the committees (level 1 and 2) in the banking and insurance field (and the transfer of UCITS Contact committee functions to the ESC and CESR) is dependent on the agreement of the Council and European Parliament.

Therefore, the Commission came forward with a package of seven measures:

1) a Commission Decision establishing CEBS (Level 3) with effect from 1 January 2004;

2) a Commission Decision establishing CEIOPS (Committee of European Insurance and Occupational Pensions Supervisors) (level 3) with effect from 24 November 2003;

3) the proposal for a Directive, deleting references to the BAC, IC and UCITS Contact Committee acting in an advisory mode and amending references to them acting as committees assisting the Commission in the exercise of its implementing powers to refer to the EBC, EIOPC, and ESC;

4) a Commission Decision establishing the EBC (European Banking Committee) in its advisory capacity (level 1), which will only enter into force at the same time as such an amending Directive;

5) a Commission Decision establishing the EIOPC (European Insurance and Occupational Pensions Committee) in its advisory capacity (level 1) which will only enter into force at the same time as such an amending Directive;

6) a Commission Decision amending the ESC (European Securities Committee) Decision, which will only enter into force at the same time as such an amending Directive;

7) a Commission Decision amending the CESR (Committee of European Securities Regulators) Decision which will only enter into force at the same time as such an amending Directive.

This package of measures concerning the creation of a new committee structure does not confer any new implementation powers on the European Commission.

2. Directives adopted by the Council and the European Parliament but not yet implemented under national legislation

This section presents the various Directives adopted by the Council and the European Parliament for which a draft law has been submitted to the Luxembourg Parliament (*Chambre des Députés*) or for which a preliminary draft is under discussion by committees operating within the CSSF or which are still being implemented by the CSSF.

2.1. Directive 2001/65/EC of 27 September 2001 amending Directives 78/660/EEC, 83/349/EEC and 86/635/EEC as regards the valuation rules for the annual and consolidated accounts of certain types of companies as well as of banks and other financial institutions ("Fair value Directive")

Besides prescriptions concerning the mandatory disclosure of information relating to the fair value of derivative financial instruments to be included in the annexe of the accounts, the fair value Directive introduces the IAS 39 standard "Financial instruments: recognition and measurement" as an option in the accounting Directives concerned. More detailed explanations concerning this Directive can be found in the CSSF's 2002 Annual Report.

2.2. Directive 2001/97/EC of 4 December 2001 amending Directive 91/308/EEC on the prevention of the use of the financial system for the purpose of money laundering

As the 1991 Directive did not clearly state whose Member States' authorities should receive declarations on suspicious transactions filed by the EU branches of credit and financial institutions located in other Member States, this Directive lays down that the authorities of the Member State in which the branch is located should receive such declarations. These authorities are also responsible for ensuring that branches comply with the Directive. The Directive redefines the terms "credit institution" and "financial institution" in order to clearly define these responsibilities.

In order to cover as much of the financial sector as possible, the Directive specifies that it also applies to investment firms as defined in Directive 93/22/EEC. The Directive extends the scope *ratione personae* notably to notaries and other members of legal professions when they assist their customers in various real estate or financial transactions.

Finally, the Directive calls on the Member States to take specific and adequate measures necessary to cope with the greater risk of money laundering which arises when professionals of the financial sector enter into a business relationship with a customer who has not been physically present for identification purposes.

2.3. Directive 2002/47/EC of 6 June 2002 on financial collateral arrangements

The Directive aims at improving the effectiveness of the single market for financial services. It seeks to increase the harmonisation of the EU financial market and to promote the smooth functioning of the single monetary policy within the Economic and Monetary Union. To this end, it defines a single, minimum legal framework applicable to the provision of securities and cash as collateral, through the pledging of securities or the transfer of title including repurchase agreements. The Directive aims to ensure that effective and simple regimes exist for the creation of collateral under either title transfer or pledge structures. Certain provisions of insolvency laws should not apply to collateral arrangements, notably those that inhibit the realisation of financial collateral or cast doubt on the validity of techniques such as bilateral close-out netting, the provision of top-up collateral and substitution of collateral.

The Directive also aims to limit the administrative burdens affecting the use of collateral in the financial markets, by limiting costly formalities imposed on the creation or enforcement of collateral arrangements. It ensures that agreements permitting the collateral taker to re-use the collateral for its own purposes under pledge structures are recognised as effective as for repurchase agreements.

2.4. Directive 2002/65/EC of 23 September 2002 concerning the distance marketing of consumer financial services and amending Directives 90/619/EEC, 97/7/EC and 98/27/EC

The Directive, whose purpose is to define a harmonised legal framework covering the conclusion of financial service contracts at a distance so as to establish an appropriate level of consumer protection in all Member States and thereby promote cross-border marketing of financial services and products, has been covered in detail in the CSSF's 2002 Annual Report.

2.5. Directive 2002/87/EC of 16 December 2002 on the supplementary supervision of credit institutions, insurance undertakings and investment firms in a financial conglomerate and amending Directives 73/239/EEC, 79/267/EEC, 92/49/EEC, 92/96/EEC, 93/6/EEC, 93/22/EEC, 98/78/EC and 2000/12/EC

The Directive, the purpose of which is to supplement the legislation on sectoral prudential supervision with a set of measures governing the supervision of financial conglomerates, has been covered in detail in the CSSF's 2002 Annual Report.

2.6. Directive 2003/6/EC of 28 January 2003 on insider dealing and market manipulation (market abuse)

The purpose of the Directive is to ensure the integrity of the EU financial markets and to strengthen investor confidence in these markets. The Directive has been covered more explicitly in the CSSF's 2001 Annual Report.

In accordance with the final report of the Committee of Wise Men on the regulation of European securities markets, the European Commission Services published a first set of implementing measures on 10 March 2003 in the form of three working documents, based on the advice submitted by CESR on 31 December 2002 at the close of a long consultation period[1]. The European Commission then presented formal draft proposals on the implementing measures to the European Securities Committee in July 2003.

[1] The technical advice concerned is covered more specifically in the CSSF's 2002 Annual Report under the CESR Market Abuse working group.

The technical measures were approved in the form of:

- Regulation (EC) No 2273/2003 of 22 December 2003 implementing Directive 2003/6/EC as regards exemptions for buy-back programmes and stabilisation of financial instruments;

- Directive 2003/124/EC of 22 December 2003 implementing Directive 2003/6/EC as regards the definition and public disclosure of inside information and the definition of market manipulation;

- Directive 2003/125/EC of 22 December 2003 implementing Directive 2003/6/EC as regards the fair presentation of investment recommendations and the disclosure of conflicts of interest.

The European Commission Services published on 17 November 2003 a working document on a second set of implementing measures, based on the technical advice given by CESR in September 2003. This advice is further detailed under point 2.3. of Chapter X "International co-operation".

2.7. Directive 2003/41/EC of 3 June 2003 on institutions for occupational retirement provision

The Directive is covered separately under point 2 of Chapter IV "Supervision of pension funds".

2.8. Directive 2003/51/EC of 18 June 2003 amending Directives 78/660/EEC, 83/349/EEC, 86/635/EEC and 91/647/EEC on the annual and consolidated accounts of certain types of companies, banks and other financial institutions as well as insurance undertakings (Directive "Modernisation of accounting Directives")

The Directive supplements the IAS regulations making the application of IAS standards compulsory for consolidated accounts of companies listed on a regulated market from 2005 onwards. It amends the 4th and 7th Directives, the accounting Directive for banks and other financial institutions, as well as the accounting Directive for insurance undertakings.

There are two parts to this Directive:

- As far as companies that do not fall under the IAS regulation (nor under the optional or mandatory regulations) are concerned, the proposed Directive removes all inconsistencies between accounting Directives and existing IAS standards as at 1 May 2002. Furthermore, it aims at making accounting Directives flexible enough to allow later amendments to IAS/IFRS standards. Its purpose is to preserve as far as possible equal opportunities between companies that apply IAS standards and those that do not. This principle of equality conditions a smooth transition for companies seeking admission to the listing of a regulated market.

- For all the companies, the Directive provides an update of certain points that are not covered by the IAS standards, such as the requirement to disclose an annual management report, to have accounts audited by a legal auditor and to publish an audit report.

As far as the first part is concerned, the Directive introduces the conformity with IAS standards by choice, allowing the Member States to either permit or require that all IAS options be applied by all the companies or only by certain categories.

2.9 Directive 2003/71/EC of 4 November 2003 concerning the prospectus to be published when securities are offered to the public or admitted to trading (prospectus Directive)

Based on the political accord reached by the Ministers for Finance and Economic Affairs on 5 November 2002, a common position has been adopted by the Council in March 2003 and the European Parliament has voted 21 amendments to the proposed Directive at second reading on 2 July 2003. Two of these amendments are particularly important for the Luxembourg market:

- the freedom to choose the competent supervisory authority for non-equity issuers whose denomination per unit amounts to at least EUR 1,000;

- the possibility of independent administrative authorities to delegate certain functions to other entities for eight years. The European Commission will assess the national practices after five years and decide on whether to amend this provision or not.

Following its final adoption within the framework of the co-decision procedure, the prospectus Directive has been published in the Official Journal of the European Union on 31 December 2003.

This Directive will make it easier and cheaper for companies to raise capital throughout the European Union on the basis of approval of the home competent authority in one Member State and reinforce investor protection by guaranteeing that all prospectuses, wherever they are issued in the EU, provide them with the clear and comprehensive information they need to make investment decisions.

The Directive will introduce a new single passport for issuers, which means that once approved for a public offer procedure or for admission to trading on a market regulated by the authority in one Member State, it will have to be accepted everywhere else in the European Union. In order to ensure investor protection, approval will only be granted if prospectuses meet common EU standards for what information must be disclosed and how. For investors, the Directive will raise the quality of information and ensure easy access to documents.

In accordance with the procedure decided upon following the resolution of the Stockholm European Council of March 2001 aiming at improving the decision procedure as regards securities, the first implementing measures relating to the prospectus Directive have been published in November 2003 in the form of a working document drawn up by the European Commission Services. A draft for formal proposals has been submitted to the European Securities Committee in January 2004. The implementing measures take account of the technical advice addressed by CESR to the European Commission during 2003. This technical advice is covered more specifically under point 2.3. of Chapter X "International co-operation" concerning the activities of the CESR prospectus group.

2.10 Regulation (EC) No 1606/2002 of 19 July 2002 on the application of International Accounting Standards (IAS Regulation)

The IAS Regulation provides that all EU companies, the securities (shares or bonds) of which are listed on a regulated market within the European Union, shall prepare their consolidated accounts according to the International Accounting Standards (IAS) as from the financial year 2005 (compulsory regime of the IAS Regulation). Member States have the option of also requiring or permitting the application of IAS to non-listed companies as well as for annual accounts (optional regime of the IAS Regulation).

According to the transitional provisions, Member States have the right to defer the application of compulsory provisions until 2007 for the companies of which:
- only the bonds are listed on a regulated market in the EU, or
- the securities (shares or bonds) are listed on a regulated market outside the EU, which are already applying another set of internationally accepted standards for a financial year having started before the publication of the IAS Regulation.

The Regulation has been covered more specifically in the CSSF's 2002 Annual Report.

3. Laws passed in 2003

3.1. Law of 2 August 2003 amending:

- the law of 5 April 1993 on the financial sector
- the law of 23 December 1998 creating *a commission de surveillance du secteur financier*
- the law of 31 May 1999 governing the domiciliation of companies

The law aims at ensuring that the entire financial sector is subject to a prudential supervision. It also defines new categories of PFS, which correspond to existing activities, namely credit offering, including factoring and leasing with a purchase option, as well as securities lending and borrowing activities, but also activities resulting from specialisation and outsourcing phenomena, such as administrative agents of the financial sector, client communication agents, IT systems and communication networks operators of the financial sector and professionals performing services of setting up and management of companies.

A detailed analysis of the law is covered in Chapter I "Information concerning the law of 2 August 2003".

3.2. Law transposing Directive 2001/24/EC of 4 April 2001 on the re-organisation and winding-up of credit institutions into the law of 5 April 1993 on the financial sector as amended

The law, as adopted on 17 February 2004, transposes Directive 2001/24/EC, which aims at guaranteeing the mutual recognition of national measures to re-organise and wind up credit institutions, as well as the co-operation between competent authorities in such crisis situations, into Luxembourg legislation.

The scope of the law is broader than that of Directive 2001/24/EC, as it does not only concern credit institutions, but also the investment firms that are entitled to hold third-party funds or financial instruments.

The law confirms the principle of competence of the authorities in the country of the registered office and the application of measures drawn up by the home country (principle of recognition by the Member States of the measures taken by each of them). In other words, the measures taken in a home Member State shall be fully effective in the host Member State without any further formalities. Applying the law of the home Member State allows to ensure the equal treatment of all the creditors of the bankrupt institution.

The law also defines a principle of unique insolvency, encompassing, on the one hand, all the branches of Luxembourg-registered institutions, whether they are located in the European Union or in a third country, and covering, on the other hand, the Luxembourg branches of institutions managing third-party funds, wherever their registered office is located.

4. Circulars issued in 2003

From 1 January 2003 to 1 March 2004, 44 circulars have been issued by the CSSF, 34 of which dealing with the fight against money laundering and the identification of business relationships with terrorist circles.

The following circulars are the most important, some of which being detailed in the relevant Chapters of the Annual Report:

- Circular 03/87 on the coming into force of the law of 20 December 2002 regarding undertakings for collective investment;
- Circular 03/88 on the classification of undertakings for collective investment governed by the provisions of the law of 20 December 2002 regarding undertakings for collective investment;
- Circular 03/95 on banks issuing mortgage bonds: applicable minimum requirements regarding management and control of the mortgage register, guarantees and limit of circulating mortgage bonds;
- Circular 03/100 on the publication on the Internet of CSSF instructions;
- Circular 03/108 on 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;
- Circular 03/113 on the practical rules concerning the mission of the external auditors of investment firms.

5. Circulars in force (as at 1 March 2004)

5.1. Circulars issued by the *Commissariat au Contrôle des Banques*

B	***79/2***	***of***	***07.05.1979***	European Code of Conduct on securities transactions
B	***83/6***	***of***	***16.03.1983***	Participating interest held by credit institutions

5.2. Circulars issued by the *Institut Monétaire Luxembourgeois*

IML	***84/18***	***of***	***19.07.1984***	Futures markets (law of 21 June 1984)
IML	***86/32***	***of***	***18.03.1986***	Control of the annual accounts of credit institutions
IML	***88/49***	***of***	***08.06.1988***	New legal provisions concerning controls carried out by auditors
IML	***90/67***	***of***	***07.08.1990***	Freeze of funds belonging to the States and residents of Kuwait and Iraq
IML	***90/68***	***of***	***13.09.1990***	Freeze of funds belonging to the States and residents of Kuwait and Iraq
IML	***91/75***	***of***	***21.01.1991***	Revision and recasting of rules governing Luxembourg undertakings covered by the law of 30 March 1988 on undertakings for collective investment

IML	*91/77*	*of*	*25.06.1991*	Freeze of funds belonging to the States and residents of Kuwait and Iraq
IML	*91/78*	*of*	*17.09.1991*	Terms of application of Article 60 of the amended law of 27 November 1984 regulating private portfolio managers
IML	*91/80*	*of*	*05.12.1991*	Staff numbers (PFS)
IML	*92/85*	*of*	*19.06.1992*	New compilation of instructions to banks
IML	*92/86*	*of*	*03.07.1992*	Law of 17 June 1992 concerning the accounts of credit institutions
IML	*92/87*	*of*	*21.10.1992*	Reporting to be supplied by other financial sector professionals
IML	*92/88*	*of*	*30.11.1992*	Certain periodic data to be supplied by credit institutions under Luxembourg law and by branches of banks originating from a country outside the EEC
IML	*93/92*	*of*	*03.03.1993*	Computerised transmission of periodic data
IML	*93/94*	*of*	*30.04.1993*	Entry into force for banks of the law of 5 April 1993 on the financial sector
IML	*93/95*	*of*	*04.05.1993*	Entry into force for other professionals of the financial sector of the law of 5 April 1993 on the financial sector
IML	*93/99*	*of*	*21.07.1993*	Provisions for Luxembourg credit institutions wishing to exercise banking activities in other EEC countries through the establishment of branches or under the freedom to provide services
IML	*93/100*	*of*	*21.07.1993*	Provisions for credit institutions of Community origin exercising banking activities in Luxembourg through branches or under the freedom to provide services
IML	*93/101*	*of*	*15.10.1993*	Rules concerning the organisation and internal control of the market activity of credit institutions
IML	*93/102*	*of*	*15.10.1993*	Rules concerning the organisation and internal control of the activities of brokers or commission agents exercised by other financial sector professionals
IML	*93/104*	*of*	*13.12.1993*	Definition of a liquidity ratio to be observed by credit institutions
IML	*93/105*	*of*	*13.12.1993*	Introduction of table 4.5. "Shareholder Composition"
IML	*94/109*	*of*	*08.03.1994*	Allocation of responsibilities for the establishment of equipment for transmitting computerised data to the IML
IML	*94/112*	*of*	*25.11.1994*	The fight against money laundering and prevention of the use of the financial sector for the purpose of money laundering
IML	*94/113*	*of*	*07.12.1994*	Explanations of various questions on accounting - treatment of premiums and discounts on transferable securities, repurchase agreements, spot and forward transactions, and

	definition of "multilateral development banks" A supplement to the *Recueil des instructions aux banques*
IML 95/116 of 20.02.1995	Entry into force of: - the law of 21 December 1994 amending certain legal provisions concerning the transfer of claims and pledging; - the law of 21 December 1994 concerning repurchase agreements transacted by credit institutions
IML 95/118 of 05.04.1995	Treatment of customer complaints
IML 95/119 of 21.06.1995	Rules for the management of risks linked to derivatives transactions
IML 95/120 of 28.07.1995	Central administration
IML 96/123 of 10.01.1996	Staff numbers (new table S 2.9.)
IML 96/124 of 10.01.1996	Staff numbers (new table S 2.9. for other financial sector professionals)
IML 96/125 of 30.01.1996	Supervision of credit institutions on a consolidated basis
IML 96/126 of 11.04.1996	Administrative and accounting organisation
IML 96/129 of 19.07.1996	The law of 9 May 1996 on the netting of claims in the financial sector
IML 96/130 of 29.11.1996	Calculation of a simplified ratio in application of IML Circular 96/127
IML 97/134 of 17.03.1997	Provision for the cost of migration to the euro for banking systems
IML 97/135 of 12.06.1997	Transmission of supervisory data and statistics by telecommunications media
IML 97/136 of 13.06.1997	Financial information for the IML and Statec
IML 97/137 of 31.07.1997	Updating the *Recueil des instructions aux banques* Report 1.4.: Integrated ratio / simplified ratio Report 3.2.: Details of calculation of the overall capital requirement
IML 97/138 of 25.09.1997	New collection of statistical data with a view to Economic and Monetary Union
IML 98/142 of 01.04.1998	Financial data to be supplied periodically to the IML
IML 98/143 of 01.04.1998	Internal control
IML 98/146 of 14.05.1998	Updating the *Recueil des instructions aux banques*: Report 6.4.: Consolidated integrated ratio / consolidated simplified ratio Report 7.3.: Details of calculation of the consolidated overall capital requirement

IML	*98/147*	*of*	*14.05.1998*	Provisions for EC investment firms exercising their activities in Luxembourg through branches or under the freedom to provide services
IML	*98/148*	*of*	*14.05.1998*	Provisions for Luxembourg investment firms wishing to exercise their activities in other EC countries through the establishment of branches or under the freedom to provide services
IML	*98/149*	*of*	*29.05.1998*	Updating the *Recueil des instructions aux banques*: Table S 1.2.: Simplified monthly statistical balance sheet

5.3. Circulars issued by the *Banque Centrale du Luxembourg* (until 31 December 1998)

BCL	*98/151*	*of*	*24.09.1998*	Accounting aspects of switching to the euro
BCL	*98/153*	*of*	*24.11.1998*	Supplement to IML Circular 94/112 on the fight against money laundering and prevention of the use of the financial sector for the purpose of money laundering
BCL	*98/155*	*of*	*09.12.1998*	Minimum reserve requirements

5.4. Circulars issued by the *Commissariat aux Bourses*

CAB	*90/1*	*of*	*13.12.1990*	Conditions for drafting, scrutiny and distribution of the prospectus to be published when transferable securities are offered to the public, or of listing particulars, to be published for the admission of transferable securities to official stock exchange listing
CAB	*91/2*	*of*	*01.07.1991*	Law of 3 May 1991 on insider dealing
CAB	*91/3*	*of*	*17.07.1991*	Admission to official listing on the Luxembourg stock exchange of foreign undertakings for collective investment (UCIs)
CAB	*93/4*	*of*	*04.01.1993*	Law of 4 December 1992 on reporting requirements concerning the acquisition or disposal of major holdings in a listed company
CAB	*94/5*	*of*	*30.06.1994*	Publication of forecasts in the admission prospectus for an official listing
CAB	*98/6*	*of*	*24.09.1998*	Information to be included in the prospectus for a public offering or for admission to official listing of certain debt issues whose income and/or redemption is/are linked to underlying shares
CAB	*98/7*	*of*	*15.10.1998*	Information to be shown in the prospectus for a public offering or for admission to official listing of certain categories of warrants, bonds, or issue programmes

5.5. Circulars issued by the *Commission de surveillance du secteur financier*

CSSF 99/1 of 12.01.1999	Creation of the *Commission de Surveillance du Secteur Financier* (list of Circulars in force appended)
CSSF 99/2 of 20.05.1999	Entry into force of three new laws dated 29 April 1999
CSSF 99/4 of 29.07.1999	Entry into force of the law of 8 June 1999 creating pension funds in the form of pension savings companies with variable capital (sepcav) and pension savings associations (assep)
CSSF 99/7 of 27.12.1999	Declarations to be sent to the CSSF in accordance with articles 5 and 6 of the law of 23 December 1998 on the supervision of the securities markets
CSSF 00/10 of 23.03.2000	Definition of capital ratios pursuant to article 56 of the amended law of 5 April 1993 on the financial sector (application to credit institutions)
CSSF 00/12 of 31.03.2000	Definition of capital ratios pursuant to article 56 of the amended law of 5 April 1993 on the financial sector (application to investment firms)
CSSF 00/13 of 06.06.2000	Sanctions against the Federal Republic of Yugoslavia and the Taliban in Afghanistan
CSSF 00/14 of 27.07.2000	Adoption of the law of 17 July 2000 amending certain provisions of the law of 30 March 1988 on undertakings for collective investment
CSSF 00/15 of 02.08.2000	Rules of conduct for the financial sector
CSSF 00/16 of 23.08.2000	Supplement to Circular IML 94/112 on the fight against money laundering and prevention of the use of the financial sector for the purpose of money laundering
CSSF 00/17 of 13.09.2000	Entry into force of the law of 27 July 2000 bringing into force the provisions of Directive 97/9/EC concerning investor compensation schemes under the amended law of 5 April 1993 on the financial sector
CSSF 00/18 of 20.10.2000	Bank accounts of the State of Luxembourg
CSSF 00/19 of 27.11.2000	Appointment of those in charge of certain functions
CSSF 00/20 of 30.11.2000	EC Council Regulation maintaining a freeze of funds in relation to Mr Milosevic and those persons associated with him
CSSF 00/21 of 11.12.2000	Supplement to Circulars IML 94/112 and BCL 98/153 on the fight against money laundering and prevention of the use of the financial sector for the purpose of money laundering
CSSF 00/22 of 20.12.2000	Supervision of investment firms on a consolidated basis carried out by the *Commission de Surveillance du Secteur Financier*
CSSF 01/26 of 21.03.2001	Law of 12 January 2001 implementing the provisions of Directive 98/26/EC on settlement finality in payment and securities settlement systems under the amended law of 5

	April 1993 and supplementing the law of 23 December 1998 creating a supervisory commission for the financial sector
CSSF 01/27 of 23.03.2001	Practical rules on the role of external auditors
CSSF 01/28 of 06.06.2001	Verification by banks and FSPs that the legal requirements on domiciliation are satisfied
CSSF 01/29 of 07.06.2001	Minimum content required for an agreement on the domiciliation of companies
CSSF 01/30 of 28.06.2001	Table E 1.1. "Simplified asset and liability situation" Table E 2.1. "Simplified profit and loss account" Update of references in Table B 1.5. "Liquidity ratio"
CSSF 01/31 of 04.07.2001	Supplement to Circulars CSSF 00/16 and IML 94/112 on the fight against money laundering and prevention of the use of the financial sector for the purpose of money laundering
CSSF 01/32 of 11.07.2001	Publication of information on financial instruments
CSSF 01/34 of 24.09.2001	Entry into force of a series of laws concerning the financial sector
CSSF 01/36 of 03.10.2001	Publication in the *Mémorial A* of the law of 1 August 2001 on the changeover to the euro on 1 January 2002 and amending certain legal provisions
CSSF 01/37 of 04.10.2001	Supplement to Circulars CSSF 00/16 and 00/31 and IML 94/112 on the fight against money laundering and prevention of the use of the financial sector for the purpose of money laundering
CSSF 01/40 of 14.11.2001	Specifications on the extent of the professional obligations laid down in Part II of the amended law of 5 April 1993 on the financial sector and in Circular IML 94/112 on the fight against money laundering and prevention of the use of the financial sector for the purpose of money laundering
CSSF 01/42 of 19.11.2001	Mortgage bond banks: rules on real estate valuation
CSSF 01/46 of 19.12.2001	Repeal of Circular CSSF 01/35
CSSF 01/47 of 21.12.2001	Professional obligations of domiciliation agents of companies and general recommendations Amendment to Circular CSSF 01/28
CSSF 01/48 of 20.12.2001	Supplement to Circulars CSSF 00/16, 00/31 and 01/37 and IML 94/112 on the fight against money laundering and prevention of the use of the financial sector for the purpose of money laundering
CSSF 01/49 of 20.12.2001	Update of CSSF Circular 2000/10 defining capital ratios pursuant to the amended law of 5 April 1993 on the financial sector (definition zone A)

CSSF 01/50 of 21.12.2001	Update of CSSF Circular 2000/12 defining capital ratios pursuant to the amended law of 5 April 1993 on the financial sector (definition zone A)
CSSF 02/59 of 10.05.2002	Combating terrorism
CSSF 02/61 of 04.06.2002	Identification and declaration of business relations with terrorist circles
CSSF 02/63 of 01.07.2002	Cross-border payments in euros
CSSF 02/65 of 08.07.2002	Law of 31 May 1999 governing the domiciliation of companies; precisions as regards the concept of "seat"
CSSF 02/66 of 15.07.2002	Supplement to Circulars CSSF 00/16, 01/31, 01/37, 01/48 and IML 94/112 on the fight against money laundering and the prevention of the use of the financial sector for money laundering purposes
CSSF 02/71 of 01.10.2002	Law of 3 September 1996 concerning the involuntary dispossession of bearer securities
CSSF 02/73 of 15.10.2002	Supplement to CSSF Circulars 00/16, 01/31, 01/37, 01/48, 02/66 and IML 94/112 on the fight against money laundering and the prevention of the use of the financial sector for money laundering purposes
CSSF 02/75 of 08.11.2002	Identification and declaration of business relations with terrorist circles Combating terrorism Abrogation of several CSSF Circulars
CSSF 02/76 of 11.11.2002	Restrictive measures against Burma/Myanmar
CSSF 02/77 of 27.11.2002	Protection of investors in case of miscalculation of NAV and the compensation following non-compliance with investment rules applicable to undertakings for collective investment
CSSF 02/78 of 27.11.2002	Details on the obligation of declaration with respect to money laundering and on the primary offences that could lead to money-laundering offences
CSSF 02/80 of 05.12.2002	Specific rules applicable to Luxembourg undertakings for collective investment (UCIs) which adopt alternative investment strategies
CSSF 02/81 of 06.12.2002	Practical rules regarding the tasks of external auditors of undertakings for collective investment
CSSF 02/82 of 06.12.2002	Survey on Luxembourg credit institutions' exposure with regard to derivative credits
CSSF 03/86 of 15.01.2003	Supplement to Circulars CSSF 00/16, 01/31, 01/37, 01/48, 02/66, 02/73 and IML 94/112 on the fight against money laundering and the prevention of the use of the financial sector for money laundering purposes

CSSF 03/87 of 21.01.2003	Coming into force of the law of 20 December 2002 regarding undertakings for collective investment
CSSF 03/88 of 22.01.2003	Classification of undertakings for collective investment governed by the provisions of the law of 20 December 2002 regarding UCIs
CSSF 03/90 of 03.02.2003	Restrictive measures against UNITA (União Nacional para a Independência Total de Angola)
CSSF 03/93 of 18.02.2003	Supplement to Circulars CSSF 00/16, 01/31, 01/37, 01/48, 02/66, 02/73, 03/86 and IML 94/112 on the fight against money laundering and the prevention of the use of the financial sector for money laundering purposes
CSSF 03/95 of 26.02.2003	Mortgage bonds: Applicable minimum requirements regarding management and control of mortgage register, guarantees and limit of circulating mortgage bonds
CSSF 03/97 of 28.02.2003	Publication of the simplified and complete prospectuses as well as annual and half-yearly reports of UCIs in the database of the financial centre
CSSF 03/100 of 01.04.2003	Publication on the Internet of CSSF instructions: - *Recueil des instructions aux banques* of the CSSF - Schedule of Conditions for the technical implementation of the CSSF reporting requirements – SOC/CSSF
CSSF 03/102 of 21.05.2003	1. Identification and declaration of business relations with terrorist circles 2. Freeze of funds in relation to Mr Milosevic and those persons associated with him
CSSF 03/104 of 01.07.2003	Supplement to Circulars CSSF 00/16, 01/31, 01/37, 01/48, 02/66, 02/73, 03/86, 03/93 and IML 94/112 on the fight against money laundering and the prevention of the use of the financial sector for money laundering purposes
CSSF 03/106 of 07.07.2003	Restrictive measures in respect of Burma/Myanmar
CSSF 03/108 of 30.07.2003	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
CSSF 03/110 of 29.08.2003	Restrictive measures concerning certain Iraqi assets Identification and declaration of business relations with terrorist circles
CSSF 03/111 of 17.09.2003	Identification and declaration of business relations with terrorist circles Combating terrorism
CSSF 03/113 of 21.10.2003	Practical rules concerning the mission of external auditors of investment firms

CSSF 03/114 of 22.10.2003	Restrictive measures concerning certain Iraqi assets
CSSF 03/115 of 06.11.2003	Supplement to Circulars CSSF 00/16, 01/31, 01/37, 01/48, 02/66, 02/73, 03/86, 03/93 and IML 94/112; non-cooperative countries or territories, Myanmar
CSSF 03/118 of 05.12.2003	Restrictive measures concerning certain Iraqi assets
CSSF 03/120 of 18.12.2003	Breakdown of value corrections made by the credit institutions at 31 December 2003
CSSF 03/121 of 19.12.2003	Statistics on guaranteed deposits and instruments
CSSF 03/122 of 19.12.2003	Clarifications on the simplified prospectus
CSSF 03/123 of 29.12.2003	Combating terrorism
CSSF 03/124 of 29.12.2003	Restrictive measures against Burma/Myanmar
CSSF 04/128 of 01.03.2004	Restrictive measures in respect of Zimbabwe
CSSF 04/129 of 01.03.2004	Supplement to CSSF Circulars 00/16, 01/31, 01/37, 01/48, 02/66, 02/73, 03/86, 03/93, 03/115 and IML 94/112; non-cooperative countries or territories

The amendments to Council Regulation (EC) No 881/2002 imposing certain specific restrictive measures against certain persons and entities associated with Usama bin Laden, the Al-Qaida network and the Taliban published on 4 June 2002 in Circular CSSF 02/61 are the object of the following CSSF Circulars: 02/62, 02/68, 02/70, 02/72, 02/74, 02/75, 02/79, 03/89, 03/91, 03/92, 03/96, 03/98, 03/99, 03/101, 03/102, 03/103, 03/105, 03/109, 03/110, 03/111, 03/112, 03/116, 03/117, 03/119, 04/125, 04/126, 04/127. These Circulars are not listed above.

CHAPTER XII

INTERNAL ORGANISATION OF THE CSSF

1. Functioning of the CSSF
2. Human resources
3. Information technology department
4. Staff members
5. Internal committees

1. Functioning of the CSSF

The organisation of the administration and management of the CSSF is described in detail under the sub-section *"Gouvernement et fonctionnement"* (Corporate governance and functioning) on the CSSF website (www.cssf.lu, section *"Qu'est-ce que la CSSF?"*).

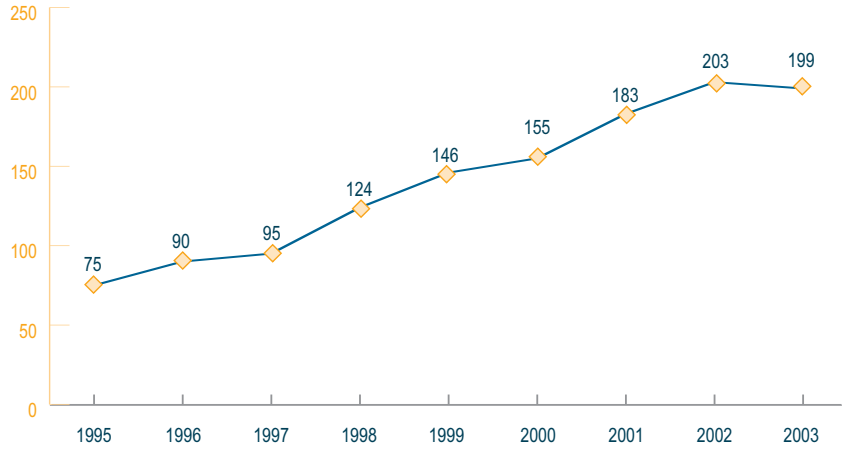
2. Human resources

While 2002 saw the recruitment of 24 agents, the year 2003 was marked by the final appointment of 43 agents in the *carrière supérieure*, 23 agents in the *carrière moyenne* and two *huissiers de salle* at the end of the training period. Thus, following the coming into force of the law of 9 November 2001 amending the law of 23 December 1998 creating a *commission de surveillance du secteur financier*, the CSSF integrated almost all the employees recruited since 1999 under the status equivalent to civil servants. The agents took specialised courses during and after their training period. Indeed, they continued taking specialised courses, notably as regards anti-money laundering measures and risk management.

Within the scope of the continuing staff training, 196 attendances have been recorded for the different courses on subjects such as criminal law and economic crime, legislation on commercial companies, anti-money laundering measures, risk management, IAS standards, specialised English for meetings and negotiations, team management and diverse IT applications.

The CSSF having concentrated in 2003 on the training of the new recruits of 2002 and their integration into the teams of the different departments, no recruitment took place during that year. As four agents left the CSSF for other government services, total staff amounted to 199 as at 31 December 2003, 175 agents of which with civil servant status and 24 agents under the status as State employee.

Movements in staff numbers



The year 2004 will be marked by a recruitment drive in two stages. The first open competition will be held in spring for the *carrière supérieure* and a second one in autumn for the *carrière moyenne*. The purpose of the recruitment drive is to replace the aforementioned departures as well as compensate for the reduction in working hours of several agents (part-time jobs, leaves for part-time work, etc.).

3. Information technology department

The activities of the IT department in 2003 focused on the introduction of the new Electronic Document Management System (DMS) system that was finalised in December 2003. The former system, which grouped the electronic mail and document management system and dated back to the IML, had not known any development in the last years. The new system, which is based on Lotus Notes and Domino.doc, allows all the CSSF departments to use a protected and centralised system to access documents. The system is perfectly integrated into the Lotus Notes messaging server set up at the end of March 2003. The shift to additional services such as scanning, workflow management or archiving is already planned.

The periodic and TAF reporting have not been subject to any major changes. Their specifications are available on the CSSF website in the heading *"Reporting légal"* (http://www.cssf.lu/fr/report/index.html). The renewal of the internal application to operate the periodic reporting is being analysed. The team of dataflow managers, who is in charge of validating the incoming reporting files, continued to guarantee the quality through their numerous interventions with financial institutions. The obligation to report the specific studies via the Librac transmission channel however encountered a few technical issues: the files were incorrectly encrypted or the names did not correspond to the CSSF's instructions.

To guarantee the update of the address lists of the supervised entities and the other contacts of the CSSF, an address server connected to the different reporting databases has been set up.

As regards IT operation, the necessary installations to set up new applications went off smoothly. In order to optimise the use of the various application servers for specific tasks, a virtual infrastructure solution allowing to run several operating systems has been installed. Thus, servers needing only little resources can share a single hardware platform. Moreover, the quick installation of a new server for testing purposes for instance, is easily feasible without acquisition of supplementary equipment.

As far as corporate governance is concerned, a committee gathering the executive board and all the heads of departments meets every two months in order to define the IT strategy and to agree on the projects and the proposed planning.

4. Staff members (as at 1 March 2004)

Executive Board

Director General	Jean-Nicolas SCHAUS
Directors	Arthur PHILIPPE | Charles KIEFFER
Executive Secretaries	Marcelle MICHELS | Monique REISDORFFER Joëlle DELOOS | Carole EICHER
Information Technology Audit	David HAGEN | Claude BERNARD | Pascal DUCARN
Internal Audit	Marie-Anne VOLTAIRE
Director General's Advisors	Marc WEITZEL | Geneviève PESCATORE
IT coordination	Pascale DAMSCHEN
Systems Security	Constant BACKES

INTERNAL ORGANISATION OF THE CSSF

General Secretariat

Head of department | Danièle BERNA-OST
Deputy head of department | Danielle MANDER
| Benoît JUNCKER | Carine CONTÉ | Natasha DELOGE
| Jean-François HEIN | Michel HEINTZ | Nadine HOLTZMER
| Iwona MASTALSKA | Christiane TRAUSCH

Department for the Supervision of banks

Head of department | Claude SIMON
Deputy head of department | Frank BISDORFF

- **Division 1 – Supervision of credit institutions 1**

  Head of division | Marc WILHELMUS
  | Marco BAUSCH | Jean LEY | Françoise DALEIDEN
  | Romain DE BORTOLI | Martine WAGNER | Gilles JANK
  | Yves SIMON | Michèle TRIERWEILER

- **Division 2 - Supervision of credit institutions 2**

  Head of division | Ed. ENGLARO
  | Isabelle LAHR | Claudine TOCK
  | Anouk DONDELINGER | Jacques STREWELER

- **Division 3 - Supervision of credit institutions 3**

  Head of division | Jean-Paul STEFFEN
  | Jean MERSCH | Joan DE RON | Alain WEIS
  | Carlos AZEVEDO PEREIRA | Gérard KIEFFER

- **Division 4 - Supervision of credit institutions 4**

  Head of division | Nico GASPARD
  | Claude MOES | Monica CECCARELLI | Steve POLFER

- **Division 5 - Supervision of credit institutions 5**

  Head of division | Patrick WAGNER
  | Jean-Louis BECKERS | Christina PINTO | Marc BORDET
  | Jean-Louis DUARTE | Marina SARMENTO

- **Division 6 – International and legal affairs division**

  Head of division | Romain STROCK
  | Guy HAAS | Nadia MANZARI

- **Special functions** | Danièle KAMPHAUS-GOEDERT | Marguy MEHLING
  | Claude REISER | Joëlle MARTINY | Davy REINARD
  | Alain HOSCHEID | Ronald KIRSCH | Patrick MAAR
  | Manuel NEU | Edouard REIMEN | Claude WAMPACH

- **Secretaries** | Michèle DELAGARDELLE | Claudine WANDERSCHEID

Department for the Supervision of undertakings for collective investment

Head of department | Simone DELCOURT
Deputy head of department | Irmine GREISCHER

- **International and legal affairs division**
  | François HENTGEN | Jean-Marc GOY | Joëlle HERTGES
- **Practical studies and specific aspects**
  | Pierre BODRY | Géraldine OLIVERA
- **IT systems** | Nico BARTHELS | Danièle CHRISTOPHORY
- **Coordination of Divisions 1 to 6**
  | Francis KOEPP
- **Division 1 – Supervision of UCIs 1**

  Head of division | Charles THILGES
  | Marc SIEBENALER | Nicole GROSBUSCH
  | Dominique HERR | Francis LIPPERT | Claude WAGNER
  | Tom EWEN | Dave REUTER
- **Division 2 - Supervision of UCIs 2**

  Head of division | Vic MARBACH
  | Martine KERGER | Géraldine APPENZELLER | Marc DECKER
  | Guy MORLAK | Marie-Rose COLOMBO | Thierry STOFFEL
  | Damien HOUEL
- **Division 3 - Supervision of UCIs 3**

  Head of division | Ralph GILLEN
  | Nathalie CUBRIC | Joël GOFFINET | Karin HOFFMANN
  | Marc RACKÉ | Son BACKES | Laurent CHARNAUT
  | Martin MANNES
- **Division 4 - Supervision of UCIs 4**

  Head of division | Angela DE CILLIA
  | Fabio ONTANO | Alain STROCK | Eric TANSON
  | Roberto MONTEBRUSCO | René SCHOTT
  | Stéphanie BONIFAS | Anne-Marie HOFFELD
  | Diane REUTER | Sabine SCHIAVO
- **Division 5 – Approval of UCIs**

  Head of division | Francis GASCHÉ
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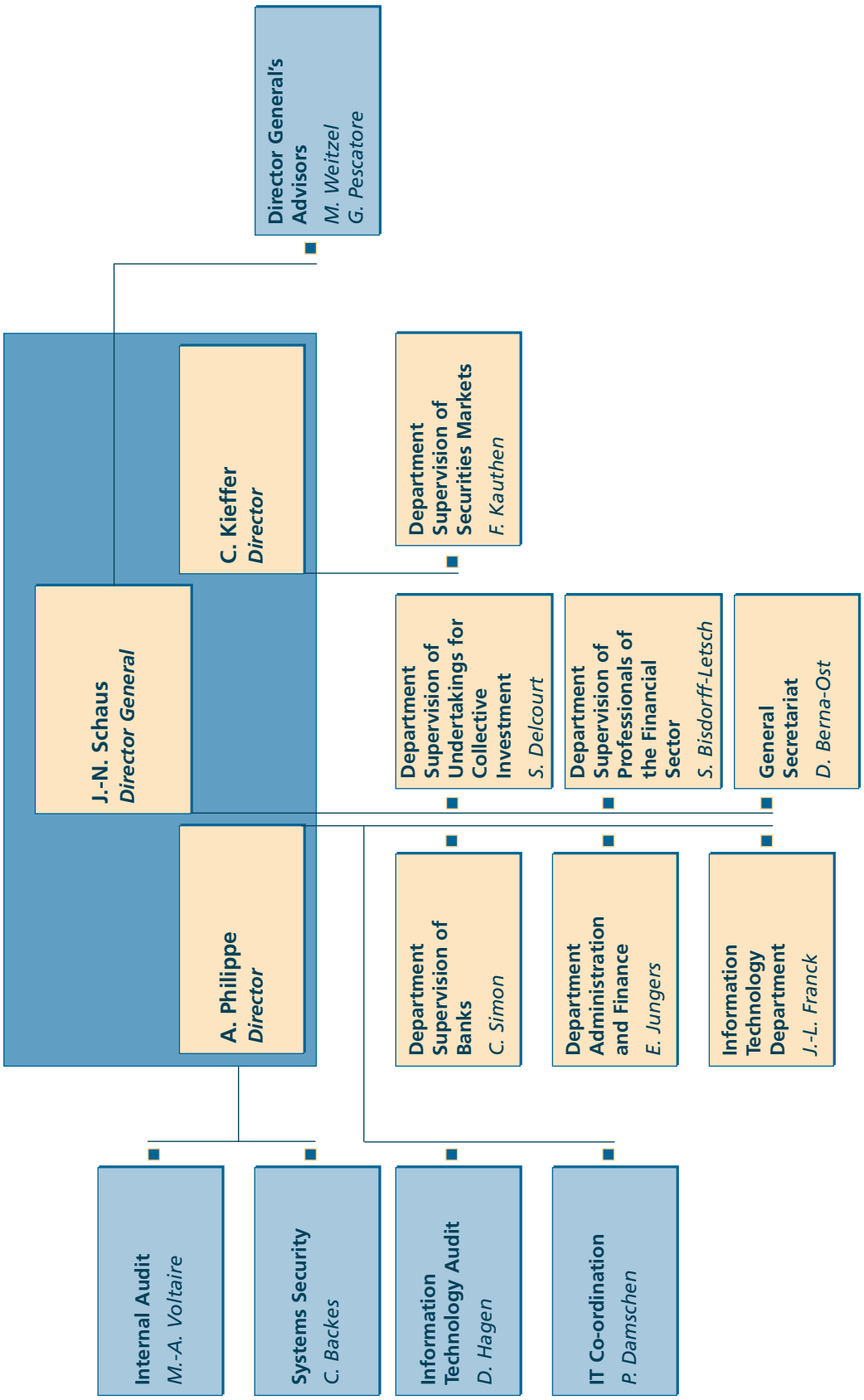
Organisation chart



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APPENDICES

1. The nature and the scope of banking secrecy
2. The CSSF in figures
3. The financial centre in figures
4. Contact telephone numbers

1. The nature and the scope of banking secrecy

Mandated by the *Comité pour le développement de la place financière* (CODEPLAFI, Committee for the development of the financial centre), the committee of legal experts (CODEJU) of the CSSF studied the implications of the concept of banking secrecy and professional secrecy in the present context.

The following note is the fruit of their reflection.

PART I: THE LEGAL NATURE OF BANKING SECRECY

A. The public order nature of banking secrecy

1) Complementarity of article 458 of the Penal code and article 41 of the banking law
2) Protected interests: coexistence of private interest and public interest

B. Consequences of the public order nature of the secrecy

PART II: THE SCOPE OF BANKING SECRECY

A. The role of the protected person's consent

1) The absence of consent is a constitutive element of the disclosure offence
2) Characteristics of the protected person's consent
   a) The protected person's interest
   b) Specific consent

B. Some practical applications

1) The right of the person concerned to direct the information
2) Circulation of information within the group
3) Disclosure to tax administrations

CONCLUSION

Every professional secrecy originates in the vulnerability of the users facing an expert to whom they expose themselves, because the latter has a technical competence, i.e. a practical power. Devoid of any own competence, the protected persons have no choice but to turn to a professional who becomes their necessary confidant.

In the light of this background, secrecy must be defined as an implicit promise without which the encounter between the user and the practitioner would most probably not take place. The confidant's authority and the user's integrity depend on the credibility of this promise. The legislator considered that the betrayal of the implicit promise of professionals, guardians of secrets by condition or profession, was contrary to public order and decided to punish the violation thereof.

The purpose of this note is to sum up the reflection of the committee of legal experts (CODEJU) relating to the question raised by the *Comité pour le développement de la place financière* (CODEPLAFI). CODEPLAFI questioned the rigidity of the public nature of banking secrecy in relation to the transmission of information that could be made upon consent or request of the protected client. CODEJU studied writings and jurisprudence in this field to define to which extent the public order nature of banking secrecy allows or prohibits the transmission of information subject to professional secrecy with the client's consent.

PART I: THE LEGAL NATURE OF BANKING SECRECY

A. The public order nature of banking secrecy

1) Complementarity of article 458 of the Penal code and article 41 of the banking law

In principle, all obligations that are sanctioned by criminal law are deemed to be of public order. Article 458 of the penal code punishes the violation of any professional secrecy and defines the regime for testimony in court.

These provisions are of public order by nature, irrespective of whether the protected interests are of public or private nature. Indeed, the legislator considers that the protection of certain private interests is of general interest and strengthens, where necessary, the legal protection by penal sanctions[1].

But beyond a criminal sanction, it is not unusual for professions subject to the duty of secrecy that the latter be specified in a detailed professional rule. The *professional* basis can be of legal or simply ethical nature.

The medical profession was the first to translate compliance with this promise into a professional rule as expressed already in the Hippocratic oath, in the form of a duty of secrecy. Thus, despite the clarity of article 458 of the penal code, which expressly refers to the medical profession, the principle of the secrecy of doctors is in fact laid down in positive law in texts specific to this profession, i.e. article 6 of the law of 29 April 1983 on the profession of doctors, dentists and veterinary surgeons[2] and to articles 35 to 38 of the medical code of ethics (ministerial decree of 21 May 1991).

The secrecy of the lawyers is laid down in article 35 of the law of 10 August 1991 on the profession of lawyers.

The secrecy of the professionals of the financial sector is laid down in article 41 of the law of 5 April 1993[3]. The anteriority of article 458 of the penal code to the professional rule of article 41 of the law on the financial sector, does not alter the intrinsic logic of these provisions. In accordance with its nature, article 458 is less specific than article 41 of the law on the financial sector, which is more modern and which defines the exceptions specific to the financial professions. Article 458 however is more specific as it defines for all the professions concerned to which extent their secrecy is an obligation or a right. But analysing the text does not allow to discern in article 41 anything other than in article 458. Both provisions shall not be read but in an absolutely complementary manner.

Article 41 of the law on the financial sector served as model for article 111-1 of the law of 6 December 1991 on the insurance sector as amended and similar reasoning applies to both texts to a large extent.

This could be sufficient to affirm the public order nature of the professional secrecy, but the secrecy does not only protect private interests.

[1] *For instance, the theft referred to under article 461 of the penal code is a provision that is clearly of general social interest while protecting the interests of private individuals.*

[2] *By the way, it is interesting to note that article 27 of this law imposes secrecy on veterinary surgeons, which proves to which extent secrecy exceeds the sole interest of the patient.*

[3] *Or in the codes of ethics such as the ABBL code of ethics.*

2) Protected interests: coexistence of private interest and public interest

The private interest is very obviously that of the protected person itself.

The general social interest protected by article 458 is of two orders:

- Firstly, the authority of the profession and the trust relationship between the guardian of the secret and the protected persons must be protected as it is in the interest of the community that the encounter between the professional and the user is unfettered, the exercise of these professions being considered as useful to the social order.

- Secondly, the protection of privacy - i.e. the modern expression of the private interests described above - is considered as an essential element of social organisation in order to balance the mass treatment of personal data. The public order nature of this second protection is also illustrated by the law of 2 August 2002 on the protection of personal data.

In order to emphasise the protected interests and to determine if the guardian of the secret and the protected person have a freedom of action as regards the application of the secrecy to their situation, the potential *contractual* nature of the banking secrecy cannot be disregarded.

One might consider that the contract between a client and a financial professional automatically contains the duty of secrecy, which would be an integral part of the relations between the parties. The judgement Hosdain and others vs. KREDIETBANK Luxembourg S.A. seems to be based on these grounds and names the public order nature of the banking secrecy as an element reinforcing the contractual obligation of the financial services provider. Furthermore, certain general conditions reinforce this viewpoint through clauses mentioning the secrecy or even allowing clients to choose a more stringent confidentiality against payment. One can also imagine that a bank considers explicitly agreeing with the clients that it has a duty of due care and not a duty to achieve a given result, in order to limit its possible contractual liability.

One should however avoid mixing up the secrecy obligation, which is of legal nature, with the contractual agreements between the parties. The financial professionals enter into deposit contracts, services contracts or mandate contracts, but the disclosure prohibition does not originate in these contracts. The secrecy does not arise from the parties' consent, which is in general the crucial element of a contract. None of the provisions mentioned (code of ethics, laws on the financial sector and insurance, medical secrecy, penal code) refers to a contract between the parties. Furthermore, secrecy also protects the persons who were in contact with a professional without having had any contractual link with the latter, as is the case for potential clients contacted, beneficial owners or proxies of an account holder, as well as for beneficiaries of insurance policies or banking operations of a client.

B. Consequences of the public order nature of the secrecy

As a consequence of the above-mentioned, the following are useful thoughts allowing to answer some questions at a later stage:

1. The banking secrecy, like the secrecy of insurance companies or any other professional secrecy, is a provision of criminal law and, as such, of public order nature. It cannot lose this characteristic unless it is completely abandoned.

2. The protection of private interests may perfectly be of public order nature. Banking secrecy is only one example among many others. But banking secrecy also protects the general social interest.

3. The public order nature and criminal nature of this provision entail that:

   a) it is of restrictive interpretation as regards the constitutive elements[4] of the violation;
   b) its application cannot be excluded by the parties of a contract in accordance with article 6 of the civil code, which defines that it shall not be departed, through particular agreements, from the laws on the public order and morality;
   c) only the law can depart from it[5].

It is the fair ordering of these few truths that poses a problem, but that also makes the professional secrecy more flexible as it may seem.

PART II: THE SCOPE OF BANKING SECRECY

A. The role of the protected person's consent

1) The absence of consent is a constitutive element of the disclosure offence

In criminal law, a violation is given when all its constitutive elements are combined. Is the consent of the protected person such as to remove one constitutive element indispensable for the violation to exist?

Many violations become legally impossible due to the sole assent of the victim, as the absence of consent is a crucial constitutive element allowing for their legal definition. This is the case *inter alia* as regards rape (article 375 PC) or forcible entry (articles 148 and 439 PC), the texts of which provide for the absence of consent.

Other violations become *de facto* impossible where the consent of the person concerned removes any meaning of the violation, as is the case for theft (article 461 PC).

One may try to reason by analogy as regards the banking secrecy. The protected person would freely define what is secret and what is not. Information which is not secret pursuant to article 458 of the penal code would also not be a secret pursuant to article 41 of the banking law. As a consequence, certain authors[6] consider that, as the information concerned is not secret, an essential constitutive element is missing.

This viewpoint is questionable, because even though the protected person does not attach any importance to the secret nature of the information, the guardian of the secret is not implicitly released from his duty of secrecy. It would be certainly unwise for him to confirm, or contradict, the client's affirmations without any further precaution.

But even where the material circumstances combine all the elements of a violation, the legal practice and theory concur on the fact that the "victim's" consent somehow influences the legal definition. As an example, assault and battery causing bodily harm incriminated under article 392 and following of the penal code are unquestionably violations of public order nature, supported by the principle of inviolability of the human person and his inalienable right to physical integrity. It would be hard to think of a situation where the public order would be more restrictive. However, the exercise of rough sports, such as boxing, is not considered illegal, as the "victim" is in a defined context, entailing that the exchange of violence takes place without interference of the penal law as long as the adversaries respect the sports context. The sportsmen are not, for that matter, supposed to renounce their physical integrity

[4] *The constitutive elements of a violation are material or psychological facts, as referred to under law, the combination of which is the condition to be defined as violation.*

[5] *There are a great number of various legal exceptions. Article 41 refers to a certain number of specific dispensations; the majority of exceptions are contained in particular laws, notably those that govern penal inquiry or prudential supervision; finally, article 458 of the penal code allows the professional to remain silent, where, such as for testimony, the duty of secrecy ceases.*

[6] *Voy. Le consentement en matière pénale, Xavier Pin, L.G.D.J. 2002, Bibliothèque des sciences criminelles T 36, p. 65 and ss.*

and it is unquestionable that the exercise of such sports takes place under the permanent protection of law and public order. The slightest deviation from the normal practice of the sport is likely to be contrary to public order and to give full authority to the incriminations of the penal code[7].

Moreover, observing the rules of the game alone does not rule out any incrimination. The "permissive consent", i.e. the consent of the "victim", beforehand, of a violation breaching his rights or interests, must also be free and informed[8]. A consent which is too general, exceeding a context of time and specific circumstances, to suffer from infringements of these rights, cannot be considered as informed.

Even if the arguments favouring a certain room for manoeuvre of the protected person exist, it is juridically very different from a conventional renunciation of the secret. For all the above-mentioned violations, the agreement according to which a person would in advance and in general renounce the protection of the law would be void, such as the contracts, in which a person would renounce its physical integrity or accept to be a victim of theft or be raped; undeniably, such agreements would breach public order and morality. A person renouncing by way of agreement the application of one of the defined articles, would not be certain that the judicial authorities would not nevertheless fully apply the criminal law. Similarly, the "beneficiaries" of such renunciation agreements would not have any right to invoke the latter and would not be safe from civil and penal prosecution instituted by the victim.

The distinction between the permissive consent and the contractual renunciation is difficult to establish, even more so as the form of the permissive consent is free and it could materialise in a contract. It is however important to draw such a distinction. Without entering into legal details, one main distinction must however be mentioned: the contractual renunciation binds the renouncing party within the conditions and time limits of the contract, while the permissive consent can be withdrawn at any moment and at the full discretion of the protected person[9].

We consider that it is always the protected person who unilaterally defines the nature of his relations with the guardian of the secret and decides if the constitutive elements are brought together. The client of a professional of the financial sector can also allow that the disclosure of information to third parties does not constitute a violation under article 41 of the banking law, without renouncing however the protection of the law.

2) Characteristics of the protected person's consent

There is no simple answer to the issue of secrecy. However, the professionals and the supervisory authorities need a minimum legal protection to broach issues raised by CODEPLAFI. They also need to solve the new problems arising in practice from the secrecy provisions. It is important to describe the criteria that must be met so that the client's attitude does not gather all the constitutive elements of an offence when a professional discloses information to third parties. The following two main criteria should be stressed:

[7] *« Given the necessities of sports and the particular context of competitions, the judges apply these incriminations in an understanding, even indulgent manner, without granting full immunity, but by cracking down only on the most severe offences and to the most dangerous behaviours. (Dalloz Civil, T X, Sports, no 74)*

[8] *Ibid. Xavier Pin*

[9] *Needless to say, if the consent materialises in a service contract whose execution requires disclosure (for instance: bank transfer), the protected person could not, by misuse of the law, unexpectedly withdraw the consent and thus bring about the penal responsibility of the confident.*

a) The protected person's interest

The secrecy is a protection that cannot be ruled out. The duty of secrecy must not however become a constraint for the protected person. The instruction or the right to disclose always emanates from the protected person, because, each time the latter is capable thereof, he defines his interests with sovereign power. The professional cannot negotiate the disclosure of information in his exclusive interest.

It is logical and in accordance with the basis of the professional secrecy that priority is given to the protected person's interest in all the considerations relating to the limits of the secrecy. Any other attitude would expose the professional to the risk of reviving the violation according to the changing moods and wishes of the protected person.

b) Specific consent

As we have seen, in order to be informed, the client's consent must take into account all the circumstances which are likely to violate his interests. Prudence imposes on the professional to assess the specificity of the consent in relation to the following criteria:

- Specificity regarding the content of the information: The "victim" must be aware of the content of the disclosure. Only the specificity of the consent regarding the information excluded from the secrecy obligation ensures that the disclosure does not exceed its intentions and does not impair his rights. This is what makes any renunciation of the secrecy on "any information whatsoever" impossible.

- Specificity regarding the addressee of the information: The addressee of the disclosed information must be known and accepted without ambiguity by the protected person. There can be no agreement allowing to disclose a specific information to "any person upon request" of the latter.

- Specificity regarding the finality: As long as the finality is not given, the consent does not exist. Where the professional is not aware of the finality motivating the client to transmit the information to a third party, the professional is well-advised to strictly set a time limit to the effects of the consent.

- Specificity of time: The client cannot give his consent for an unspecified period of time, as he cannot, at that moment, fully assess his interests in the long term. An isolated disclosure does not imply renunciation for the future.

These criteria of prudence, which are not laid down by law, are not necessarily cumulative. Thus, a specific information can be given to a specific person for a perfectly identifiable reason, but without predetermined time limit. The professional should form an opinion based on all the elements in question and decide according to the interests of the protected person. Even if the client has given his consent, the professional must always ask himself *ex ante* if the instruction received will exonerate him *ex post*[10].

[10] *A jurisprudential analysis calls for a very prudent approach, as relatively recent decisions can be found, which quote extreme positions compared to the one described above. Thus, according to a civil judgment of 4 April 2003 (no 26786), "the doctor, released from his medical secrecy by the patient, (…) is authorized to provide the information even if this information is not favourable for the client". If the Court's decision is based on article 36 of the medical code of ethics which allows, by exception, the provision of information to a specialist physician, it nevertheless disregarded the patient's interests. In a completely different direction, the judgment of the Council of the Court of Appeal of 16 May 1988 (no 54/33) on the French jurisprudence stipulates that "the beneficiary's consent cannot eliminate the breach referred to under article 458".*

B. Some practical applications

1) The right of the person concerned to direct the information

It is admitted that the protected person is the owner of the secret, which means, above all, that the financial professional cannot oppose the secrecy to his own client, nor to any person representing the latter, such as a mandatory or a sole legatee[11]. The protected person itself decides to whom it confides which information and – where the professional holds the information concerned - the protected person can also give the professional the instruction to direct the information to himself or to a third party. The person can direct the information to anyone, but it is the only one allowed to do so, as it is understood that the professional remains free to execute the instruction received or not, depending on whether he considers being freed of his duty of secrecy or not. In practice, the fact has never been contested that a banker may accept to send the statements of account of a client upon request to a third party's address.

It does not seem important in this context whether the banker who follows the instruction of the protected person acts on the basis of a mandate authorising him to represent the latter, or whether he meets this person's request in the same manner as he would if the person concerned requested him to directly communicate the information.

However, it is important to note that the injunction always emanates from the protected person itself. The instruction given to the professional to communicate information to a third party is very different from the permission given to this professional to meet the requests emanating from third parties. This second case is not acceptable as it would mean renouncing the principle itself of secrecy.

2) Circulation of information within the group

Further to the legal exceptions, certain institutions of the financial centre wish to obtain from the client the right to exchange information more freely within their banking group for reasons relating to accounting consolidation, IT processing or anti-money laundering. In theory, this issue should be treated in the same manner whether the information crosses the Luxembourg border or not.

This question arises each time international banking or insurance groups consider choosing Luxembourg as a European platform, by way of free provision of services or freedom of establishment through branches and by pooling certain means in order to benefit from economies of scale. Banks and insurance undertakings are not in the same situation. Indeed, bankers can benefit from the expansion of the use of outsourcing under the law of 2 August 2003[12], while, for lack of any mention in the law of 6 December 1991, insurance undertakings are deprived thereof for the moment.

Finally, a financial group often holds – either on a temporary or on a permanent basis – several companies in Luxembourg. An elementary logic consisting in reducing costs entails that companies are located at the same address, allowing them to fully benefit from the services provided to the group. However, where these services allow to access nominative data of clients, the pooling thereof will come up against the constraints of the professional secrecy. The protected person, client of several entities of the same group, suffers from the lack of communication between them. It is thus in the person's strictest interest to give the instruction to the entities of the group to be treated on a global basis and according to its needs.

[11] *Voy. Tr. Arr. Luxembourg, 24 April 1991, Pas.28, 173*

[12] *The law of 2 August 2003 inserted in article 41 of the law of 5 April 1993 a paragraph 5: the duty of secrecy is not applicable to client communication agents, administrative agents of the financial sector, nor to IT system and communication network operators of the financial sector, insofar as the extent to which the information transmitted to such professionals is transmitted under a service agreement pertaining to a regulated activity.*

The aforementioned legal exceptions allow for certain arrangements even for clients of a defined entity of the group and who wish to remain linked thereto.

On the other hand, the automatic "transparency" of the group's entities is not acceptable, nor should the group be allowed to impose the disclosure in its own interest. The legal exceptions of article 41 provide *a contrario* for a restrictive interpretation.

The professional's difficulty to define his obligation stems from the fact that he must assess the circumstances and reasons due to which the client is outside the scope of the secrecy obligation and decide whether that particular case is of such nature as to protect him from any violation.

3) Disclosure to tax administrations

Certain observers, notably politicians, raised the question concerning the compatibility of the Qualified Intermediary Agreement (QIA) with the banking secrecy. In this context, the American fiscal residents request their Luxembourg banker to inform the Internal Revenue Service (IRS) of the interest received on American securities. But, in accordance with point 1, nothing prevents information mechanisms to third parties such as that of the QIA. Indeed, clients give a specific mandate to their banker to communicate specific information to a specific end to their tax authority in the United States.

In the same way, it would be possible, within the scope of the transposition of the savings tax directive, for clients of the Luxembourg financial centre to opt for an exchange of information if they consider it to be in their interest. Again, the information would be determined (interests received), the recipient known and the purpose defined. The interest of the client is determining in both mechanisms, as, for lack of participating therein, he greatly limits his investment possibilities.

These agreements do not imply that bankers commit any offence and do not call into question the inviolability of the secret of those clients who remain attached to it.

Conclusion

We described a certain number of cases where the financial professional or his client have an interest in transmitting information to third parties. These cases can be of very various kinds, but certain situations are likely to be of recurrent nature.

The flexibility given by banking secrecy within the scope of the current Luxembourg positive law is relatively important. The undeniable public order nature only scarcely impairs the client's freedom to direct the information as he sees fit, or to consent to specific disclosures if they are in his own interest. There is no contradiction between the public order and the client's control of the secret. However, he remains a protected person in any circumstances and this nature limits the room for manoeuvre of the financial professionals. The solution to their problem cannot be solved through the general terms and conditions that do not correspond to the required specificity.

This view is not new, but presented in a more detailed and systematic manner as in other Luxembourg legal commentary.

Luxembourg, 1st March 2004

2. The CSSF in figures

	Prudential supervision					*IT matters*		*Matters of general interest*		
	Supervision of banks	*Supervision of UCIs*	*Supervision of PFS*	*Supervision of securities markets*	*Administration and Finance*	*IT systems*	*IT audit*	*Management*	*General Secretariat*	**Total**
Letters	2,628	13,421	1,132	843	584	241	47	122	2,987	**22,005**
Meetings	255	142	95	32	41	58	114	-	14	**751**
On-site inspections	62	6	4	-	-	-	3	-	-	**75**
Internal committee meetings										
> "Banks" committee	2									
> "Pension funds" committee									12	
> "Legal experts" committee									24	
> "UCI" committee		8								
> "Other professionals of the financial sector" committee			2							
> "Domiciliation" committee			1							
> "Securities markets" committee				5						
> "Anti-money laundering" Steering committee									7	
> Prudential supervision consultative committee									5	
International meetings	105	11	4	102	-	1	-	1	4	**227**
Meetings with homologous authorities	3	1	-	-	-	-	-	-	-	**4**
Speeches at conferences	13	4	-	-	-	-	8	2	4	**31**

3. The financial centre in figures

Situation as at 31 December 2003

BANKS

Number	169
Balance sheet total	EUR 655.768 billion
Net profit	EUR 2.882 billion
Employment	22,529 persons

UNDERTAKINGS FOR COLLECTIVE INVESTMENT

Number	1,870
Number of compartments	7,509
Total assets	EUR 953.302 billion

PENSION FUNDS

Number	10

MANAGEMENT COMPANIES

Number	3
Employment	98 persons

PROFESSIONALS OF THE FINANCIAL SECTOR

Number	142
Balance sheet total	EUR 2.547 billion
Net profit	EUR 365.917 million
Employment	4,455 persons

Total employment in supervised entities	27,082 persons

4. Contact telephone numbers

Commission de Surveillance du Secteur Financier

	110, route d'Arlon
	L-1150 Luxembourg
Postal address	L- 2991 LUXEMBOURG
Switchboard	26 25 1 - 1
Fax	26 25 1 - 601 (management)
	- 603 (banks)
	- 604/605 (UCI)
	- 606 (investment activities)
	- 607 (PFS)
	- 608 (administration)
e-mail	direction@cssf.lu
	banques@cssf.lu
	opc@cssf.lu
	psf@cssf.lu
	informatique@cssf.lu
Website	http://www.cssf.lu

Management

26 25 1	201	SCHAUS Jean-Nicolas - *directeur général*
	202	PHILIPPE Arthur - *directeur*
	200	KIEFFER Charles - *directeur*
	203	MICHELS Marcelle - *secrétaire de direction*
	204	REISDORFFER Monique - *secrétaire de direction*
	205	DELOOS Joëlle - *secrétaire de direction*
	206	EICHER Carole - *secrétaire de direction*

Information Technology Audit

26 25 1	395	HAGEN David - *attaché de direction*
	421	BERNARD Claude - *attaché de direction*
	280	DUCARN Pascal - *attaché de direction*

Internal Audit

26 25 1	366	VOLTAIRE Marie-Anne - *attaché de direction*

Director General's Advisors

26 25 1	209	WEITZEL Marc - *conseiller de direction 1re classe*
	334	PESCATORE Geneviève - *attaché de direction*

IT Co-ordination

26 25 1	353	DAMSCHEN Pascale - *attaché de direction 1er en rang*

Systems Security

26 25 1	420	BACKES Constant - *attaché de direction*

General Secretariat

26 25 1	230	BERNA-OST Danièle - *conseiller de direction 1re classe*
	297	MANDER Danielle - *conseiller de direction 1re classe*
	238	JUNCKER Benoît - *conseiller de direction*
	327	CONTÉ Carine - *attaché de direction*
	329	DELOGE Natasha - *attaché de direction*
	313	HEIN Jean-François - *attaché de direction*

26 25 1 | 301 HEINTZ Michel - *attaché de direction*
| 393 HOLTZMER Nadine - *attaché de direction*
| 237 MASTALSKA Iwona - *attaché de direction*
| 348 TRAUSCH Christiane - *attaché de direction*

Department for Supervision of Banks

26 25 1 | 222 SIMON Claude - *premier conseiller de direction*
| 235 BISDORFF Frank - *conseiller de direction 1re classe*

| 229 ENGLARO Ed - *conseiller de direction 1re classe*
| 219 GASPARD Nico - *conseiller de direction 1re classe*
| 217 KAMPHAUS-GOEDERT Danièle - *conseiller de direction 1re classe*
| 258 STEFFEN Jean-Paul - *conseiller de direction 1re classe*
| 315 STROCK Romain - *conseiller de direction 1re classe*
| 310 WAGNER Patrick - *conseiller de direction 1re classe*
| 213 WILHELMUS Marc - *conseiller de direction 1re classe*
| 218 BAUSCH Marco - *conseiller de direction*
| 224 DE RON Joan - *conseiller de direction*
| 294 LEY Jean - *conseiller de direction*
| 214 MEHLING Marguy - *conseiller de direction*
| 233 MERSCH Jean - *conseiller de direction*
| 312 REISER Claude - *conseiller de direction*
| 262 BECKERS Jean-Louis - *attaché de direction 1er en rang*
| 365 BORDET Marc - *attaché de direction 1er en rang*
| 354 DALEIDEN Françoise - *attaché de direction 1er en rang*
| 215 DE BORTOLI Romain - *attaché de direction 1er en rang*
| 307 HAAS Guy - *attaché de direction 1er en rang*
| 324 LAHR Isabelle - *attaché de direction 1er en rang*
| 352 MARTINY Joëlle - *attaché de direction 1er en rang*
| 328 MOES Claude - *attaché de direction 1er en rang*
| 279 PINTO Christina - *attaché de direction 1er en rang*
| 302 REINARD Davy - *attaché de direction 1er en rang*
| 290 TOCK Claudine - *attaché de direction 1er en rang*
| 367 TRIERWEILER Michèle - *attaché de direction 1er en rang*

26 25 1 | 351 WAGNER Martine - *attaché de direction 1er en rang*
| 309 WEIS Alain - *attaché de direction 1er en rang*
| 225 AZEVEDO PEREIRA Carlos - *attaché de direction*
| 299 CECCARELLI Monica - *attaché de direction*
| 275 DONDELINGER Anouk - *attaché de direction*
| 288 DUARTE Jean-Louis - *attaché de direction*
| 304 HOSCHEID Alain - *attaché de direction*
| 298 JANK Gilles - *attaché de direction*
| 372 KIEFFER Gérard - *attaché de direction*
| 308 KIRSCH Ronald - *attaché de direction*
| 316 MAAR Patrick - *attaché de direction*
| 394 MANZARI Nadia - *attaché de direction*
| 399 NEU Manuel - *attaché de direction*
| 371 POLFER Steve - *attaché de direction*
| 397 REIMEN Edouard - *attaché de direction*
| 317 SARMENTO Marina - *attaché de direction*
| 318 SIMON Yves - *attaché de direction*
| 319 STREWELER Jacques - *attaché de direction*
| 398 WAMPACH Claude - *attaché de direction*
| 292 DELAGARDELLE Michèle - *secrétaire*
| 221 WANDERSCHEID Claudine - *secrétaire*

Department for Supervision of Undertakings for Collective Investment

26 25 1 | 210 DELCOURT Simone - *premier conseiller de direction*
| 242 GREISCHER Irmine - *conseiller de direction 1re classe*

| 240 BODRY Pierre - *conseiller de direction 1re classe*
| 223 CAMPILL Christiane - *conseiller de direction 1re classe*
| 234 CONRATH Anne - *conseiller de direction*
| 226 HENTGEN François - *conseiller de direction*
| 343 BERCHEM Pascal - *attaché de direction 1er en rang*
| 381 DE CILLIA Angela - *attaché de direction 1er en rang*
| 355 FELTEN-ENDERS Pascale - *attaché de direction 1er en rang*
| 342 GOY Jean-Marc - *attaché de direction 1er en rang*
| 380 OLIVERA Géraldine - *attaché de direction 1er en rang*

26 25 1 | 379 ONTANO Fabio - *attaché de direction 1er en rang*
| 344 PAULY Marc - *attaché de direction 1er en rang*
| 320 STEINBACH Claude - *attaché de direction 1er en rang*
| 321 STROCK Alain - *attaché de direction 1er en rang*
| 345 TANSON Eric - *attaché de direction 1er en rang*
| 306 BERGAMO Didier - *attaché de direction*
| 323 CUBRIC Nathalie - *attaché de direction*
| 347 HERTGES Joëlle - *attaché de direction*
| 340 MONTEBRUSCO Roberto - *attaché de direction*
| 341 REDING Pierre - *attaché de direction*
| 291 SCHMIT Isabelle Maryline - *attaché de direction*
| 249 BARTHELS Nico - *inspecteur principal 1er en rang*
| 245 KOEPP Francis - *inspecteur principal 1er en rang*
| 227 BOS Jolanda - *inspecteur principal*
| 247 GILLEN Ralph - *inspecteur principal*
| 283 MARBACH Vic - *inspecteur principal*
| 269 THILGES Charles - *inspecteur principal*
| 220 ANDRE-ZIMMER Adrienne - *inspecteur*
| 289 GIEL-MARKOVINOVIC Anica - *inspecteur*
| 254 GOFFINET Joël - *inspecteur*
| 246 KERGER Martine - *inspecteur*
| 284 SIEBENALER Marc - *inspecteur*
| 243 NEUMANN Danielle - *chef de bureau*
| 278 SCHMIT Pascale - *chef de bureau*
| 322 CICCARELLI Daniel - *chef de bureau adjoint*
| 241 GASCHE Francis - *chef de bureau adjoint*
| 253 GROSBUSCH Nicole - *chef de bureau adjoint*
| 305 PLEGER Nadine - *chef de bureau adjoint*
| 337 APPENZELLER Géraldine - *rédacteur principal*
| 383 BARITUSSIO Marie-Louise - *rédacteur principal*
| 387 DECKER Marc - *rédacteur principal*
| 244 HERR Dominique - *rédacteur principal*
| 338 HOFFMANN Karin - *rédacteur principal*
| 384 KRIER Claude - *rédacteur principal*
| 382 LAUX Josiane - *rédacteur principal*
| 256 LIPPERT Francis - *rédacteur principal*

26 25 1 | 331 MORLAK Guy - *rédacteur principal*
| 330 RACKE Marc - *rédacteur principal*
| 335 REISDORFF Nathalie - *rédacteur principal*
| 339 SCHOTT René - *rédacteur principal*
| 385 THIELEN Claudine - *rédacteur principal*
| 282 WAGNER Claude - *rédacteur principal*
| 333 WAGNER Suzanne - *rédacteur principal*
| 336 WILHELM Michèle - *rédacteur principal*
| 390 ALONSO Yolanda - *rédacteur*
| 360 BACKES Son - *rédacteur*
| 361 BONIFAS Stéphanie - *rédacteur*
| 373 CHARNAUT Laurent - *rédacteur*
| 388 CHRISTOPHORY Danièle - *rédacteur*
| 272 COLOMBO Marie-Rose - *rédacteur*
| 374 EWEN Tom - *rédacteur*
| 362 HOFFELD Anne-Marie - *rédacteur*
| 389 MANNES Martin - *rédacteur*
| 363 REUTER Dave - *rédacteur*
| 273 SCHIAVO Sabine - *rédacteur*
| 268 SCHMITZ Daniel - *rédacteur*
| 375 STOFFEL Thierry - *rédacteur*
| 293 HOUEL Damien - *employé*
| 281 PIERRARD Evelyne - *employé*
| 271 REUTER-WEYLER Diane - *employé*
| 251 BETTINELLI Sandy - *secrétaire*
| 236 DOS SANTOS Carla - *secrétaire*
| 332 FRANTZ Karin - *secrétaire*
| 386 KUEHLER Simone - *secrétaire*

Department for Supervision of the other Professionals of the Financial Sector

26 25 1	231	BISDORFF-LETSCH Sonny - *conseiller de direction 1re classe*
	212	LOSCH Denise - *conseiller de direction 1re classe*
	325	FELICETTI Carlo - *attaché de direction*
	356	JACOBY Brigitte - *attaché de direction*
	396	NEY Carole - *attaché de direction*
	377	PLETSCHETTE Luc - *attaché de direction*
	208	MIOTTO Claudia - *inspecteur principal*
	285	MAMER Sylvie - *inspecteur*
	349	MERKES Carine - *inspecteur*
	267	MARSON Anne - *chef de bureau adjoint*
	286	SIMON Martine - *rédacteur principal*
	461	BRIMEYER Gérard - *rédacteur*
	274	LAUTERBOUR Emilie - *secrétaire*

Department for Supervision of Securities Markets

26 25 1	232	KAUTHEN Françoise - *attaché de direction*
	376	ZIMMER Annick - *attaché de direction*
	311	HENGEN Mylène - *conseiller de direction adjoint*
	326	GLOESENER Simone - *attaché de direction*
	350	LUU Ngoc Dinh - *attaché de direction*
	392	VAN DE BERG Pierre - *attaché de direction*
	391	WEIRICH Karin - *attaché de direction*
	358	HOFFMANN Malou - *rédacteur*
	460	WAMPACH Maggy - *rédacteur*
	357	NICOLAY Sylvie - *employé*
	276	PULCINI Marie-Josée - *secrétaire*

Administration and Finance

26 25 1	255	JUNGERS Edmond - *conseiller de direction 1re classe*
	259	BECHTOLD Georges - *inspecteur principal 1er en rang*
	252	WEBER Jean-Paul - *attaché de direction*
	364	KIRSCH Alain - *rédacteur principal*
	378	PLETSCHETTE Carlo - *rédacteur principal*
	264	ROLLER Fernand - *huissier dirigeant*
	265	DOMINGUES Raul - *huissier de salle*
	263	VALENTE Marco - *huissier de salle*
	266	CLEMENT Paul - *employé*
	248	DEMUTH Elisabeth - *employé*
	257	CALZETTONI Milena - *secrétaire*

IT Department

26 25 1	401	FRANCK Jean-Luc - *attaché de direction*
	402	WAGNER Sandra - *attaché de direction*
	415	ALMEIDA Joao Pedro - *rédacteur*
	405	DUHR Jean-Jacques - *rédacteur*
	403	HERLING Paul - *rédacteur*
	406	LAUER Edouard - *rédacteur*
	417	PROTH Karin - *rédacteur*
	416	SCHILTZ Carine - *rédacteur*
	411	WAGENER Guy - *rédacteur*
	407	BURNOTTE Jean-François - *employé*
	408	ESCHETTE Nadine - *employé*
	409	FRANTZEN Guy - *employé*
	410	KOHL Marc - *employé*

COMMISSION de SURVEILLANCE
du SECTEUR FINANCIER

110, route d'Arlon • L-2991 LUXEMBOURG

luxembourg.