

COMMISSION de SURVEILLANCE
du SECTEUR FINANCIER

In case of discrepancies between the French and the English text, the French text shall prevail

Luxembourg, 19 November 2007

To all credit institutions and
investment firms

CIRCULAR CSSF 07/325

as amended by Circular CSSF 21/765

Re: Provisions relating to credit institutions and investment firms of EU origin established in Luxembourg by way of branches or exercising activities in Luxembourg by way of free provision of services

Dear Sir, Madam,

This circular is issued pursuant to the transposition into Luxembourg law of Directive 2004/39/EC of the European Parliament and of the Council on markets in financial instruments (“MiFID Directive”) through the law of 13 July 2007 on markets in financial instruments (“MiFID Law”) amending the law of 5 April 1993 on the financial sector (“LFS”) and updates the circulars that existed in this field (IML 93/100, IML 98/147). The purpose of this circular is to provide further details on the principle of freedom of establishment by way of branches and free provision of services for credit institutions and investment firms whose head office is in another Member State.

The MiFID Directive incorporates the principles that had already been set down in Directive 93/22/EEC on investment services in the securities field, such as the single authorisation recognised in all the Member States of the European Union. Nevertheless, it raises the level of harmonisation in order to ensure increased investor protection and to allow credit institutions and investment firms to provide their banking and investment activities/services in all Member States based on the principle of supervision by the home supervisory authority. For branches of credit institutions and investment firms of EU origin, certain fields of supervision, however, fall within the remit of the supervisory authority of the host Member State, considered as the authority that is the closest to the

branch and better placed to detect problems and intervene in order to ensure compliance with the rules imposed on branches.

The purpose of this circular is to provide additional information on the role of the CSSF as host authority and to point out to credit institutions and investment firms whose head office is in another Member State the provisions that their Luxembourg branches must comply with under the new regime. Most of the requirements concern both credit institutions and investment firms. Nevertheless, in certain cases, the legislator purposely differentiated between both statuses.

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I. Scope

1. The circular concerns credit institutions whose head office is in another Member State¹ and which provide in Luxembourg, by way of a branch or by free provision of services, activities covered by their authorisation as defined in Annexe I to Directive 2006/48/EC relating to the taking up and pursuit of the business of credit institutions (“CRD Directive”). Pursuant to the aforementioned Annexe, the services and activities provided for in sections A and B of Annexe I to the MiFID Directive, when referring to the financial instruments provided for in section C of Annexe I of that Directive, are subject to mutual recognition in accordance with the CRD Directive.
2. The circular also concerns investment firms whose head office is in another Member State and which provide in Luxembourg, by way of a branch or by free provision of services, investment services/activities covered by their authorisation as defined by section A of Annexe I to the MiFID Directive.
3. Where a credit institution or investment firm whose head office is in another Member State appoints a tied agent (as defined in article 4(1)(25) of the MiFID Directive) established in Luxembourg, this tied agent shall be subject to the provisions of the LFS applicable to Luxembourg branches of credit institutions and investment firms of another Member State. For a credit institution or investment firm whose head office is in another Member State appointing a tied agent in Luxembourg while already having a branch there, the tied agent shall be considered as an additional business place of this branch, as described in point II.1.3. below.

II. Luxembourg branches of credit institutions or investment firms whose head office is in another Member State established in Luxembourg (“the branch” or “the branches”)

II.1. Notifications in connection with the establishment of a branch

II.1.1 Notification procedure for credit institutions or investment firms whose head office is in another Member State wishing to establish a branch in Luxembourg

4. Article 30 of the LFS provides that credit institutions or investment firms whose head office is in another Member State are permitted to establish themselves in Luxembourg by way of a branch after having performed in their home country the notification procedure as referred to in article 25 of the CRD Directive and article 32 of the MiFID Directive and provided that their services/activities are covered by their authorisation and fall within Annexe I to the CRD Directive or section A or B

¹ In accordance with article 1(14) of the LFS, “Member State” shall mean a Member State of the European Union. The States that are contracting parties to the European Economic Area Agreement other than the Member States of the European Union, within the limits set forth by this agreement and related acts are considered as equivalent to Member States of the European Union. “Another Member State” shall mean a Member State other than Luxembourg.

of Annexe I to the MiFID Directive. An authorisation from Luxembourg authorities is not required.

5. Unless there is reason to doubt the adequacy of the administrative structure or the financial situation of the requesting professional, taking into account the activities envisaged, the authority of the home country shall communicate to the CSSF the notification file submitted to that authority by the notifying institution within three months of receipt of that file at the most. The CSSF shall inform the institution on how the supervision will be performed in the fields falling under its competence and shall draw its attention on the conduct of business rules, as well as on the rules of general interest governing the exercise of those services/activities. The branch may commence business on receipt of that information or, failing such information, within two months from the date of transmission of the communication by the authority of the home Member State. The branch informs the CSSF of the date at which business commences, which will be the date on which it will be registered on the official list of credit institutions and investment firms respectively.

II.1.2 Changes to the notification

6. Any change to the information to be provided in a notification as mentioned below (article 32(2) of the MiFID Directive and article 26 of the CRD Directive) shall be notified in writing at least one month before the change comes into force. The following information is concerned:
 - (a) the programme of operations stating the investment or banking services/activities as well as the ancillary services which the branch intends to perform, and the organisational structure of the branch and the use, where applicable, of a tied agent;
 - (b) the address in the host Member State from which documents may be obtained;
 - (c) the name of the person(s) responsible for the management of the branch.
7. In accordance with article 26(3) of the CRD Directive, credit institutions shall notify any change referred to in point 6 to the competent authority of their home country as well as to the CSSF. On the other hand, in accordance with article 32(9) of the MiFID Directive, investment firms shall notify any change as referred to in point 6 solely to the competent authority of the home Member State which shall communicate the change to the CSSF.

II.1.3 Opening of additional places of business

8. A credit institution or investment firm of EU origin having a branch in Luxembourg may freely open additional places of business without having to use the notification procedure referred to in point II.1.1 of this circular. In accordance with article 1(32) of the LFS, several places of business established in Luxembourg by a credit institution or investment firm whose head office is in another Member State are regarded as a single branch.

9. The credit institution or investment firm EU origin shall designate one of the places of business as the head office of the establishment in Luxembourg. The managers of this head office shall have authority over all the places of business established in Luxembourg and shall be the contacts of the CSSF. Where opening additional places of business constitutes a change of the programme of operations and/or implies a change in the address of the head place of business, the credit institution or investment firm of another Member State shall inform the competent authorities beforehand, in accordance with point 7 above, of the opening of additional places of business.
10. The head place of business shall transmit annually to the CSSF, by 31 January, a list stating the addresses of the places of business that the branch has in Luxembourg.

II.2 Branch infrastructure

11. As opposed to the freedom to provide services, the establishment of a branch implies the existence in Luxembourg of an operational unit ensuring a permanent physical presence of the credit institution or investment firm.
12. On account of its geographical distance and its activity in specific markets, a Luxembourg branch enjoys a certain functional independence from its head office in the home country. Moreover, in the exercise of its activities it shall comply with certain specific rules that apply under the Luxembourg legislation. These factors, together with the CSSF's right to monitor as host authority in accordance with its residual competences, imply that the branch, as an entity, must meet certain organisational and infrastructure requirements, as described below.
 - The effective management of the branch must be exercised in Luxembourg in accordance with the rules and instructions set out by the head office of the branch. The branch in Luxembourg represents an operational entity whose staff numbers depend on the activities carried on. Another entity of the group may by no means enter into transactions on behalf of the Luxembourg branch.
 - The credit institution or investment firm entrusts the management of the branch to one or more managers, of whom at least one must reside in Luxembourg. Those persons must have adequate professional experience and competence.
 - Any branch established in Luxembourg must have an administrative structure. All accounting and all transaction-related documents must be available at the branch. In accordance with article 45(5) of the LFS, the branch shall arrange for records to be kept of all services and transactions undertaken by it, in accordance with the period laid down in the Commercial Code, which shall be sufficient to allow the CSSF to monitor compliance with the requirements under the LFS and, in particular, its obligations towards clients or potential clients, without prejudice to the possibility for the competent authority of the home Member State to have direct access to these records.

II.3 General legal framework

13. Branches shall respect the general legal framework (general laws, in particular as regards civil law, commercial law, labour law and criminal law) applicable to all activities performed in Luxembourg. Moreover, by virtue of article 35(4) of the LFS, the branches are required to apply the Luxembourg standards adopted in relation to anti-money laundering and terrorist financing (cf. law of 12 November 2004 on the fight against money laundering and terrorist financing, as amended, and Circular CSSF 05/211) and in relation to professional secrecy.
14. Where a branch does not comply with these legal requirements, article 46(2) of the LFS authorises the CSSF to take the necessary steps as described in point 34 below in order to remedy such situation.

II.4. Supervision of the branch

II.4.1 General provisions

15. The competent authorities of the home Member State shall be responsible for the supervision of services/activities provided by the branch without prejudice to the provisions on the competences conferred upon the CSSF by the LFS.
16. The competent authorities of the home country and the CSSF shall actively cooperate in the context of their respective supervisory missions; the arrangements for this cooperation may be fixed in bilateral Memoranda of Understanding between the authorities concerned.

II.4.2 Scope of the CSSF's supervision

17. In accordance with article 45(4) of the LFS, the supervision of investment services/activities which the branch provides in Luxembourg falls under the responsibility of the CSSF, which shall ensure that the branch complies with the obligations set out in articles 37-3 (conduct of business rules when providing investment services to clients), 37-5 (obligation to execute orders on terms most favourable to the client) and 37-6 (client order handling rules) of the LFS. Circular CSSF 07/307 provides further clarifications on this subject.
18. The CSSF is also competent to ensure that the investment services provided by the branch comply with the obligations set out in articles 26 (obligation for systematic internalisers to publish firm quotes), 27 (post-trade disclosure by credit institutions and investment firms) and 28 (obligation to uphold integrity of markets, report transactions and maintain records) of the MiFID law.
19. In accordance with article 45(6) of the LFS, the branches shall provide the CSSF, upon request, with the information necessary to the monitoring of their compliance with the standards applicable in Luxembourg for the cases provided for in points 17 and 18 above. The information to be provided by these branches is the same information as the CSSF requires for these purposes from credit institutions and investment firms authorised in Luxembourg.

20. The supervision of the CSSF as described above is a limited exception to the principle of supervision by the competent home authority, which remains responsible for the supervision of services/activities of branches established in Luxembourg as regards the services/activities performed within the territory of the home Member State of the credit institution or investment firm and all services/activities provided in another Member State. Indeed, all services/activities provided by a branch outside the Luxembourg territory are considered as services/activities performed by the credit institution or investment firm, and not by the branch established in Luxembourg.
21. Branches dealing only with eligible counterparties, as defined in article 37-7 of the LFS, are exempted from the application of articles 37-3 (conduct of business rules), 37-5 (best execution) and 37-6(1) (client order handling rules) of the LFS (cf. Circular CSSF 07/307, point 41).
22. As regards exclusively branches of credit institutions, article 45(3) of the LFS entrusts the CSSF, in cooperation with the competent authority of the home Member State, with the supervision of the liquidity of these branches. For the performance of its responsibilities in this field, the CSSF requires these branches to provide it with the same information as provided by Luxembourg-incorporated credit institutions (article 45(6) of the LFS).

II.4.3 Instruments of supervision

1. Periodic reports to provide to the CSSF

(a) Requirement for branches to report transactions on financial instruments

23. In accordance with article 35(1) of the MiFID Law, the CSSF is the authority competent for the investment services provided and the investment activities performed in Luxembourg by the Luxembourg branches of credit institutions and investment firms authorised in another Member State. These branches must report their transactions to the CSSF.
24. As per the provisions of article 32(7) of the MiFID Directive, these branches shall report the transactions undertaken by them and considered as investment services provided outside Luxembourg to the competent authority of the home Member State. In accordance with CESR guidelines on reporting for branches (cf. Annexe 3: *CESR Level 3 Guidelines on MiFID Transaction reporting* published on 29 May 2007, ref. CESR/07-301), the branches concerned may however choose to report to the CSSF in its capacity as competent authority of the host Member State, all transactions, whether executed within the context of investment services provided in Luxembourg or outside the territory of Luxembourg. The CSSF will forward the appropriate information to the home Member State authority.
25. Circular CSSF 07/302 provides further clarifications on the obligation to report transactions on financial instruments.

(b) Specific provisions relating to branches of credit institutions whose head office is in another Member State

26. In accordance with article 45(6) of the LFS, the details and procedures of the reporting by branches are indicated in the summary of periodic information to be provided by credit institutions to the CSSF, under point I.3 of Annexe 3 of circular CSSF 07/316.

(c) Specific provisions relating to branches of investment firms whose head office is in another Member State

27. In accordance with article 45(6) of the LFS, branches must submit a statistical balance sheet (and off-balance sheet) and a statistical profit and loss account.

2. External audit

28. The procedure for the external audit of branches' accounts falls under the competence of the home authorities.
29. Branches are required, however, to have a review executed by an external auditor for specific subjects on which the CSSF maintains a control responsibility as host authority, in particular as regards compliance with the rules on the prevention of money laundering and compliance with conduct of business rules when providing investment services to clients.

For the purpose of drawing up its report, the *réviseur d'entreprises* (statutory auditor) shall apply *mutatis mutandis* the provisions applicable to the establishment of the annual long form audit report to comply with the professional obligations as regards the fight against money laundering and terrorist financing and the conduct of business rules when providing investment services. The report of the *réviseur d'entreprises* includes a description of the procedures and controls in place within the branch as well as an appraisal by the *réviseur d'entreprises*. The descriptive parts of the reports shall be made available to the *réviseur d'entreprises* by the branches.

30. In accordance with article 54(2) of the LFS, the CSSF has the right to appoint the external auditor of the credit institution or investment firm to execute controls at the Luxembourg branch on subjects for which the CSSF is competent.
31. Where the CSSF decides to make use of this facility, it shall communicate to the managers of the branch the terms of the mandate to be given to the auditors. The managers of the branch shall liaise with the auditor of the head office of the credit institution or investment firm or, where applicable, its local representative and organise the practical schedule of the audit. The branch shall communicate the audit report issued by the external auditor to the CSSF.

3. On-the-spot inspections by the authority of the home country and the CSSF

32. The competent home authorities may carry on on-the-spot controls at the branches of credit institutions (article 45(7) of the LFS) and investment firms (article 45(9) of the LFS) established in Luxembourg whose head office is in another EU Member State, after having informed the CSSF. They may also request the CSSF to verify some information. In this case, the CSSF shall either carry out the verification itself or appoint an auditor or any other independent expert at the expenses of the branch.

II.4.4 Measures to be taken by the CSSF in case of non-compliance by the branch with the Luxembourg provisions or in case of emergency

33. Article 46 of the LFS describes the precautionary measures available to the CSSF as host Member State.
34. Paragraph (1) of that article provides that the CSSF shall refer to the competent authority of the home Member State of the credit institution or investment firm whenever it has clear and demonstrable grounds for believing that one of its branches in Luxembourg is in breach of the obligations arising from the provisions of the LFS which do not confer powers on the CSSF. If the irregular situation persists, despite the measures taken by the competent authority of the home Member State of the credit institution or investment firm or because such measures prove inadequate, the CSSF may take, after informing the competent authority of the home Member State, all appropriate measures needed in order to protect investors or the proper functioning of the markets in Luxembourg.
35. If a branch does not comply with the requirements of the LFS which confer powers on the CSSF, the latter may address an injunction to the credit institution or the investment firm as provided for in article 59 of the LFS. If the credit institution or investment firm concerned fails to take the necessary steps, the CSSF shall take all appropriate measures to ensure that the credit institution or investment firm puts an end to the irregular situation. The CSSF shall inform the competent authority of the home Member State of the measures taken. If, despite the measures taken, the irregular situation persists, the CSSF may take, after having informed the competent authority of the home Member State, the appropriate measures to prevent or penalise further irregularities, or even prevent the credit institution or investment firm from initiating any new transaction in Luxembourg. Such measures shall be notified to the European Commission.
36. Article 46(4) of the LFS provides that, in emergencies and before following the procedure described in point 35 above, the CSSF may take any precautionary measures necessary to protect the interests of depositors, investors or others to whom services are provided. Such measures shall be notified to the European Commission and to the competent authorities of the home Member State.

III. Free provision of services in Luxembourg by credit institutions and investment firms whose head office is in another Member State

III.1. Notifications relating to the freedom to provide services

37. According to article 28(1) of the CRD Directive, any credit institution whose head office is in another Member State wishing to exercise the freedom to provide services by carrying on its activities in Luxembourg for the first time shall notify the competent authorities of its home country of the activities it intends to carry on. These activities must be included in Annexe I to Directive 2006/48/EC.
38. According to article 31(1) and (2) of the MiFID Directive, any investment firm authorised by the competent authority of another Member State may exercise the freedom to provide services/activities in Luxembourg by way of free provision of services provided that such services/activities are covered by its authorisation. The exercise of these services/activities is not subject to an additional authorisation by the CSSF. A mere communication to the competent authority of the home Member State is sufficient.
39. The authority of the home country shall transmit the notification of the institution to the CSSF within one month. The credit institution or investment firm may commence the provision of its services/activities in Luxembourg as soon as it is informed of this transmission.
40. Any change in the initial details included in the notification must be notified in writing to the authority of the home country at least one month before the implementation of this change, which will transmit it to the CSSF.

III.2 Non-compliance with the Luxembourg provisions by credit institutions or investment firms performing activities/services under the freedom to provide services in Luxembourg

41. The provisions of point 34 of this circular also apply to credit institutions and investment firms performing activities/services under the freedom to provide services in Luxembourg.

IV. Transitional provisions

42. Pursuant to article 71 of the MiFID Directive, credit institutions and investment firms of another Member State, already authorised to provide investment services and activities in Luxembourg through the establishment of branches or by providing services may continue to perform their activities and provide their services in Luxembourg without having to submit a new notification at the entry into force of the MiFID law, on 1 November 2007.
43. However, where credit institutions or investment firms of another Member State intend to exercise for the first time, as from 1 November 2007, new activities and services not covered by their existing passport in Luxembourg, they shall submit a notification for these new services/activities in accordance with articles 31 and 32 of the MiFID Directive to the competent authority of their home Member State.

V. Repealing provisions and entry into force

44. This circular enters into force on 19 November 2007. Circulars IML 93/100 and IML 98/147 are repealed with effect on 19 November 2007.

Yours faithfully,

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