

**COMMISSION de SURVEILLANCE  
du SECTEUR FINANCIER**

Luxembourg, 22 April 2008

To all supervised entities

<p><b>CIRCULAR CSSF 08/350</b></p> <p><b>as amended by Circular CSSF 13/568</b></p>
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**Re: Details relating to the amendments introduced by the law of 13 July 2007 on markets in financial instruments to the PFS statuses referred to in articles 29-1, 29-2, 29-3 or 29-4 and designated “support PFS”; Amendment to the prudential supervisory procedures for support PFS**

Ladies and Gentlemen,

The purpose of this circular is to provide details on the amendments introduced by the law of 13 July 2007 on markets in financial instruments to the PFS statuses authorised only to perform an activity within the meaning of articles 29-1, 29-2, 29-3 or 29-4 of the law of 5 April 1993 on the financial sector, as amended, (hereinafter “the Law” or the LFS). These PFS, referred to in “Subsection 3: PFS carrying out an activity connected or complementary to a financial sector activity” of the Law, are designated hereafter as “support PFS”. The PFS also referred to in that subsection that carry out a complementary activity of the financial sector (domiciliation agents, professionals performing services of setting up and of management of companies) are not covered by this circular.

In this circular, the term “financial professional” covers support PFS’s clients and comprises notably the financial professionals falling under the LFS as well as insurance and reinsurance undertakings.

This circular also provides first indications on the changes to the supervisory mode for support PFS. These details are provided in order to promote efficiency, taking into account the specificities of the support PFS activities.

In detail, this circular covers the following items:

- The description of the activities differentiating primary IT systems operators of the financial sector (OSIP), authorised in accordance with article 29-3 of the Law, from secondary IT systems and communication networks operators of the financial sector (OSIS), authorised in accordance with article 29-4 of the Law, and from IT service providers not having a PFS status.
- The supervisory mode for support PFS, which focus more on a targeted risk management in relation to the activities provided to the financial sector, particularly due to the fact that OSIP and OSIS are no longer restricted to provide services exclusively to the financial sector.

The circular does not cover the outsourcing from the point of view of support PFS's clients relying on these services. As professionals falling under the Law, the provisions of circulars "IML 96/126, CSSF 05/178 and CSSF 12/552"<sup>1</sup> on administrative and accounting organisation, and notably in relation to foreign intra-group outsourcing procedures, remain applicable.

## 1. Description of the activities of OSIP and OSIS

The law of 13 July 2007 on markets in financial instruments provides a split of the status IT systems and communication networks operator of the financial sector (OSIRC) into two new statuses: primary IT systems operators of the financial sector (OSIP) (article 29-3 of the Law) and secondary IT systems and communication networks operators of the financial sector (OSIS) (article 29-4 of the Law).

The legislator has introduced this distinction in order to take into account the difference in nature of the risks related to the operating of systems which, on the one hand, have a direct impact on the accounts and financial statements of the financial professionals, and, on the other hand, on the other IT systems and communication networks.

- 1.1. The OSIP status renews the principal aspects of the old OSIRC status, the difference being that the service provider is in charge of IT systems which are part of the specific IT system belonging to the listed professionals and which allow the drawing up of the accounts and financial statements.
- 1.1.1. "The specific IT system belonging to" the financial professional, that is an OSIP client, shall be defined as any IT system, being hardware or software, tightly linked to the accounting function of this institution and constituting its main support. This system must not necessarily belong to the financial professional. The OSIP may also make it available to its clients on condition that the IT system constitutes an environment exclusively dedicated to the processing of the client's data.

The IT systems used by an OSIP may be mutualised, on condition that each environment dedicated to an OSIP client complies with the above definition of

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<sup>1</sup> Circular CSSF 13/568

“specific IT system belonging to the financial professional” and that there is a perfect segregation between these environments.

1.1.2. The IT systems allowing the establishment of accounts and financial statements are those which

- record the accounting entries;
- establish the accounts balances or the accounts statements on the basis of management decisions (insofar as they are included in the accounting function);
- establish the accounts statements on the basis of publications of financial data, including the annual accounts, the intermediary financial statements and the legal and prudential reporting required.

1.2. An OSIS status may only be granted to professionals in charge of the operation of IT systems and communication networks other than those required for establishing the accounts and financial statements.

1.2.1. This category notably includes

- the systems which are used for
  - the drawing up of management data;
  - the risk management or the management of its financial positions (assets and liabilities management);as far as these are not included in the accounting function,
- the systems on which the implementation of the rules of conduct, the provision of investment services to clients, the execution of orders or any other activity of the financial sector are based (for example credit activity, activity of services or domiciliation).

For example, a portfolio management software application drawing up financial statements intended for its clients shall not be considered as allowing the drawing up of financial statements of the financial professional itself, unless this application performs accounting entries or unless the result of this application is made of accounting entries injected without any prior control within another accounting application.

Being in charge of IT systems and of software which establish financial situations intended for clients and of which the information produced does not have any direct impact on the professional’s financial statements is not considered as an activity requiring an OSIP status.

Similarly, “data warehouse” systems, office applications based on spreadsheets and software for data layout, may provide information which helps the management of the financial professional’s activity or which contributes in the drawing up of the reporting for the authorities, but as long as the produced information is not constituted of accounting entries or is not injected without any

other verification into an accounting system, their management does not fall under the OSIP status.

Consequently, the management of any accounting system or application producing information constituted of accounting entries or account information which are injected without any further verification into the accounting software must exclusively fall under an OSIP status whatever the classification stated in the previous paragraph may be (ex.: office applications, datawarehouse, reporting,...)

- 1.2.2. The operating of secondary IT systems and communication networks of professionals as referred to in article 29-4(1) of the LFS include notably office applications, electronic mail management, electronic storage and archiving of the client's documents and identification documents on condition that these functions be only of technical nature and that the management of the retention period and the deletion exclude service provisions requiring an authorisation as client communication agent (ACC) according to article 29-1 of the Law.

Payment or settlement systems, as well as trading platforms are not, by default, part of the specific IT system belonging to the financial professional.

*A priori* the following are not considered as systems allowing the establishment of accounts and financial statements:

- the systems and applications collecting or processing prices or rates of securities or exchange rates, as well as information on corporate actions feeding or constituting a securities database;
- EAI software (Enterprise Application Integration), also called "middleware" and used for the communication of and between heterogeneous applications;
- transaction reconciliation software;
- the autonomous storage systems (equipment for network attached storage, NAS), including systems for the storage of historical data or of archives;
- the systems for the transmission of financial information, including the transmission of legal reporting.

Finally, paragraph (2) of article 29-4 of the Law foresees that an OSIS is also authorised to perform the installation and the maintenance of the IT systems and networks as referred to in paragraph (1) of the same article. It must be specified that these complementary services may include the sale of IT equipment constituting these systems and networks.

- 1.2.3. Similarly to OSIP, OSIS may provide their services by using IT systems belonging to clients or make such a system available to their clients while ensuring that a dedicated environment is reserved for each one of them.

- 1.3. The common characteristic for OSIP and OSIS statuses is that they are in charge of the functioning of IT systems. Besides the operating of the technical platform,

the functioning includes the reception of incoming data, their processing, their storage and the production of the outgoing data related to the client's activity or service relying on this IT system.

In this respect, OSIP and OSIS differ from other service providers, which intervention is limited to development services, to the installation and the maintenance of IT systems or applications. Points 3.2, 4.5 and 6 of Circular CSSF 06/240 of 22 March 2006 provide some examples of interventions accessible to service providers which do not have a status as OSIP or OSIS. These service providers shall consequently not be authorised on the basis of the Law and shall not fall under the provisions of professional secrecy of article 41(5). The circular also reiterates that service providers which do not provide services related to operating and thus to the proper functioning of a system, may not be entitled to have an OSIP or OSIS status.

The difference between the status "IT systems operator" and the status "administrative agent" as described in point 2 of Circular CSSF 06/240 also remains applicable.

- 1.3.1. Without prejudice to the responsibilities incumbent on the beneficiaries of the services for whom circulars "IML 96/126, CSSF 05/178 and CSSF 12/552"<sup>2</sup> are applicable, OSIP and OSIS must take the necessary measures to allow the system or network, of which they are in charge, to function by preserving the availability, the integrity and the confidentiality of the information and the processing operating within, as well as the mechanisms of IT traceability and evidence inherent in the system and linked to these processing.
- 1.3.2. The law of 13 July 2007 also abrogated the exclusive service provision condition to clients of the financial sector for the IT provisions of OSIP and OSIS. These may now conclude contracts and provide services outside the financial world.

## **2. Supervisory mode for support PFS**

The main specificity of support PFS within the financial sector is the fact that they do not accept and manage clients' or investors' financial assets and that their main activity is to offer support services to other financial professionals, services which are more of an organisational and technical nature than financial. Furthermore, these services are not only offered to the financial sector.

In order to promote efficiency, it becomes crucial for the CSSF, as well as for support PFS, to refocus the prudential supervision as regards the issues and risk exposures brought upon the financial sector exclusively. The CSSF is currently reflecting on this matter.

The contemplated model of supervision will be a Risk Based Approach. The support PFS must consequently prepare for the implementation of risk

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<sup>2</sup> Circular CSSF 13/568

assessment and management process for the provision of service to the financial sector.

This risk analysis and management process towards the financial sector will be part of the internal control put or to be put in place by the support PFS in accordance with Circular IML 98/143.

### **3. Prudential rules and rules of conduct**

- 3.1. The prudential rules and the rules of conduct described in articles 36 and 36-1 of the Law are entirely applicable to support PFS, except for paragraph (2) of article 36-1 which is only applicable to administrative agents. The clients' interests, the market integrity, the experience in the area of investment must be put into the context of the specific service provision of support PFS activities.

The clients' interests must be at least interpreted so as to avoid that the service provision being prejudicial to the client of the financial sector, even if the contractual conditions are observed.

The market mentioned as having to remain upright is at the same time the field of the outsourced activity and the one of financial activities and services.

The experience in the area of investment must be understood as the experience linked to the outsourced activities. As an example, a financial professional outsourcing its IT may not have the specific competence to assess the proper investments for the implementation of an IT infrastructure adapted to his needs. The contract between a support PFS and its financial professional client, must provide for the extent of information the client requires in order for the latter to be able to judge the rightfulness of the investments which would be made specifically for the needs of this service provision.

- 3.2. Due to the extension of the scope of intervention, the variety of services offered by support PFS is likely to be significantly larger and diverse than the variety offered to the financial sector, with very different risks as well.

The service provisions other than those performed for the financial sector must be in line with the PFS activities and under no circumstances shall they be likely to negatively influence the service provisions to the financial sector.

The service provisions to entities of the financial sector must be realised under the best quality and availability conditions and the service provisions outside the financial sector may under no circumstances hinder service provisions to the financial sector, or even impact the latter due to a reputational spill-over risk from outside the financial sector.

- 3.3. As soon as an OSIP or OSIS provider decides to share amongst customers a single physical environment, being its own IT system or not, it will have to clearly communicate the contemplated solution to the concerned clients, so as to make them understand the effects and limits. If this mutualisation has not been foreseen in the initial contract, if its conditions have fundamentally changed, or

if there have been important changes in the service provision which cannot be accepted by the financial professional which is subject to specific obligations in its prudential context, a transitional solution must be provided for in the contract in order to enable a transfer of the service provision to another subcontractor or a takeover of the service provision by the financial professional itself.

#### **4. Transitional provision**

- 4.1. Article 29-3(6) of the Law states that OSIRCs, authorised under article 29-3 as such at the time of the entry into force of the law of 13 July 2007, shall benefit *ex officio* from the status as OSIP. The professionals wishing to adopt the OSIS status must make a request for the amendment of their authorisation.
  
- 4.2. The change from an OSIRC status to an OSIP or OSIS status must be considered as a new authorisation. Article 23(1) of the Law, amended by article 95 of the law of 13 July 2007 on markets in financial instruments states that “the authorisation shall be withdrawn if the PFS does not make use of the authorisation within 12 months after granting, expressly renounces the authorisation or has performed no financial activity, nor a connected or complementary activity listed in sub-section 3 of section 2 of this chapter for the preceding six months.” The period of 12 months shall thus apply as from 1 November 2007.

Yours faithfully,

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