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Chairman's message

Ernst Wilhelm Contzen
Chairman of the ABBL

This year, many of the international financial groups present on the financial centre will ask themselves the following important question: Why are we in Luxembourg? The answer is no longer as straightforward as it may have been in the past.

As a financial centre, Luxembourg still has a lot of cards to play. But competing internationally will certainly not be as easy as it may have been 10 years ago. We have to get used to less spectacular growth and reduced profit margins. We have to take stock and face the simple truth that the golden years of the financial centre are behind us, if only because Europe will dramatically decline in significance and because the global financial industry is shrinking. As a financial centre, we must actively and continuously convince clients, investors and companies why they should come here and why we can offer a service that they do not get elsewhere. Competition will continue to increase as rules become the same everywhere. Luxembourg financial actors need to adapt and continue to provide added value for customers, but also within their groups. It is important to persuade mother companies why a presence in Luxembourg is important even if rules are the same everywhere.

The ABBL and other trade associations have been working continuously with the government in preparing the future of the financial centre, whether it be the move from offshore to onshore of our private banking industry or developing a regulated alternative fund industry.

More than ever before, it is crucial that we tell the world that this financial centre is not a tax driven offshore centre for other countries, but that it is a centre of expertise in a very broad range of financial services such as insurance, funds, international loans, venture capital, clearing and many others. It is also a retail and commercial banking service provider for the entire Greater Region. Luxembourg players come from all over the world and their market is the European single market. You cannot challenge the Luxembourg strategy without challenging the single market as a whole.

I am convinced that this is a crucial moment in the development of our centre and that the risks have never been higher for our industry. The backlash since the beginning of the crisis has been quite formidable. Not only in terms of reputation, but also, and especially, in terms of regulation. The finance industry, particularly in Europe, is faced with an unprecedented wave of regulations.

Unfortunately, not enough thought is spent on exploring how the various pieces of regulation interact with each other and how they affect our business models and our economies. As financial institutions, we want BETTER regulation not simply MORE regulation. In addition, we need a regulatory level playing field. It was precisely uneven application of rules that led to the financial crisis.

Luxembourg plays by the rules, but in order to compete, it must understand the rules better and in more depth, and be more adept at playing the game than its competitors. This means that we need to build on our ability to look beyond our borders when designing and implementing regulatory frameworks. We do not have the luxury of thinking domestically like our bigger neighbours. In essence, we must defend the fundamental freedoms of the single European market, which IS our domestic market. I believe that the current trend of balkanisation into national markets represents the single biggest threat to this country's economy and it is something we must fight at all costs. It is thus not regulatory harmonisation that we should fear, but rather any regulation that fails to take into account, or worse, hinders the provision of cross-border financial services.

"The financial centre, and by extension the country, needs a strong ABBL to defend its interests both at home and abroad. In light of the regulatory flood that we are facing, this has never been more important."

The establishment of a banking union probably represents the most consequential change for the cross-border banking industry in Europe. As far the single supervisory mechanism is concerned, the worst-case scenario, which would have been a single supervisor dominated by the 5 biggest countries and a return of

supervisory powers to Home countries seems to have been avoided so far. But there still remain a lot of open questions, and the impact on Luxembourg cannot be fully gauged at this moment. It is clear, however, that the single supervisory mechanism will be costly for the banking sector. In a first step, the ECB will hire 800 new supervisors. And this is only the beginning. Banks will bear most of the costs. Given the size of our banks' balance sheets in relation to the State budget and the presence of big European cross-border groups, around half of all banks in Luxembourg will fall under the supervision of the ECB. The creation of a single supervisory mechanism thus represents are real turning point for our financial centre.

Wealth management is probably the pillar of our financial centre that has seen the most fundamental shift in recent years. Although the move towards tax compliance has been taking place for quite some time in Luxembourg, there have been a number of accelerating factors in recent years, such as the adoption of the OECD standards, the Swiss bilateral tax agreements and, significantly, FATCA. It is clear that Luxembourg private banks have to adapt their business models In an era of increased transparency. Luxembourg cannot afford any reputational risks. The ABBL has thus been strongly advocating a tax compliant business model, since it believes that it is the only sustainable model for the financial centre. Indeed, no one should make the mistake of thinking that things can stay the same as they were: this is also true for outdated business models. In light of international developments, it should be obvious to anyone that time is running out. There is, of course, a risk that changing business models may result in job losses down the line. It is thus to be hoped that these losses can be counterbalanced by growth in other segments of our wealth management industry.

> "As a financial centre, we must actively and continuously convince clients, investors and companies why they should come here and why we can offer a service that they do not get elsewhere."

The end of banking secrecy for non-resident clients has, in fact, translated into a radical shift of our client base. Although assets under management have remained stable over the past years, smaller clients have left in large numbers while the proportion of high net worth individuals has increased significantly. These clients come to Luxemburg because they need a wealth management that can meet their multijurisdictional needs. As a one-stop shop for their activities, these clients only have the choice in Europe between Luxembourg, London and Switzerland, and Luxembourg is the only one of these countries that is in the euro zone. This is definitely an opportunity for our banks and for the financial centre as a whole.

It is clear that if we are competing with other financial centres on the basis of the same rules, Luxembourg will continue to face increasing pressure on costs. In 2012, our banks once again saw their margins shrink as a result of increasing costs and lower steady revenues sources, such as interest margins and commissions. If we play by the same rules, we cannot afford to be more expensive than our competitors. We need to keep costs down if we do not want to lose activities to more cost-friendly jurisdictions.

Luxembourg's social and economic well-being is tied to the fate of its financial centre. The considerable weight of the financial centre is easily illustrated with a few numbers: it represents nearly 40 % of GDP, 17 % of national employment and 30 % of State tax revenues. I don't think that the relative weight of the financial centre within the Luxembourg economy will change anytime soon. Diversification in other sectors is clearly welcome and should help to take some burden off the shoulders of the financial sector as main driver of growth, but I doubt that any one sector can take up the torch the way the financial sector did from the waning steel

"You cannot challenge the Luxembourg business strategy without challenging the single market as a whole."

industry in the 70s. This is why the government needs to continue to invest in this sector, as it will remain the primary growth and job engine for many years to come. It is important that we also continue to diversify within the financial sector itself, which is already far less monolithic than it was in the past.

In this context, it is important that we continue to work together. Not only the different actors of the financial centre itself, but all stakeholders, both public and private. Any long-term vision for the future of this country needs to pay close attention to the sustainable development of the financial centre. The Luxembourg financial centre has considerable experience in adapting to a changing environment and of leveraging opportunities within a harmonised regulatory framework to the benefit of clients, investors and financial service providers. Despite the many headwinds the global financial industry is currently facing, Luxembourg will thus continue to play a pivotal role in international cross-border finance.

During the last three years as Chairman of the ABBL, I have come to fully appreciate the fact that the ABBL provides real added value to the financial centre and this country. In an ever more complex regulatory and legal environment, the ABBL represents a rare example of an industry successfully mutualising its costs and resources in order to concretely work, on a day-to-day basis, to achieve a common goal: maintaining a competitive international financial centre. The financial centre, and by extension the country, needs a strong ABBL to defend its interests both at home and abroad. In light of the regulatory flood that we are facing, this has never been more important. The ABBL is celebrating its 75th anniversary next year. As the financial centre's oldest and most powerful association, the ABBL has played a central role in shaping today's financial centre. It will continue doing so by shaping the financial centre of tomorrow.

Luxembourg, 5 March 2013

ABBL Management Board

Jean-Jacques Rommes
Chief Executive Officer
Head of the Management Board

Rüdiger Jung
Member of the Management Board
Legal and Tax

Serge de Cillia
Member of the Management Board
Banking and Finance

Daniel Lehmeier
Member of the Management Board
Support Services

1. European institutions 2012 / 2013: looking back and forward

From 2012…

The year 2012 comes to a close and it has been a year of change and of laying groundwork for the future legislative landscape in the EU.

The starting gunshot of the banking union by the Heads of State and of Government at the June European Council meeting has indeed been hailed as the most important step in the EU's integration process since the creation of the euro. And the Commission has been fast to deliver. On 11 September 2012, it presented its legislative proposals for a **single supervisory mechanism** with the European Parliament and the Council drafting positions of their own in late November, respectively in mid December. In all these internal discussions, the issues of the scope and of governance have been very prominent. A quick conclusion of the negotiations between the institutions is not excluded at the time of writing of this article. The EU would indeed have delivered the first step of the banking union with remarkable speed.

On the new **capital requirements** translating the Basel III agreement into EU law, the co-legislators have been working intensely the whole year through. Both the European Parliament and the Council have hammered out internal positions and are currently still negotiating in the trialogue to agree on a common text.

The Commission also presented its long expected proposal for a directive on the **recovery and resolution** of credit institutions ("crisis management") which has since been in negotiations on the European Parliament as well as on the Council side.

The **MiFID and MiFIR** texts presented by the Commission in October 2011, were hotly debated in the European Parliament, in particular with regards to the issues of fees/inducements and OTFs (Organised Trading Facilities). The European Parliament adopted its position on 26 October 2012, whilst the Council is still struggling to reach an agreement having difficulties on the same issues.

The Commission also presented its **Packaged Retail Investment Products** proposal on 3 July 2012, which is still being discussed at European Parliament and Council level.

The Commission furthermore prepared and adopted the **AIFMD delegated acts** via a regulation in December 2012. This regulation is important for depositary banks as it defines their tasks, obligations and liability and thereby also creates a precedent for the UCITS world.

In terms of UCITS, the European Commission presented **UCITS V** on 3 July 2012, focusing on the depository regime, remuneration and sanctions. This text is still being discussed at European Parliament and Council Level. The Commission has also published, on 26 July, a **consultation on UCITS**, opening the debate on many issues, including the depositary passport and eligible assets.

On issues like the Commission's proposals on the **European Account Preservation Order** or the **Data Protection** regulation, work has been going on slowly but surely in both the European Parliament and the Council.

The debate around **Central Securities Depositories** is still continuing in both the European Parliament and the Council, focusing mainly on the issue of whether or not to separate activities and on licensing.

… to 2013.

The year promises to be busy in terms of new regulatory proposals coming from Brussels for financial services, and the banking sector at large will be most impacted by these new initiatives and pending legislation. The European Commission will focus its attention on the vaster project of the banking union and on what it considers to be loopholes that it may have left in its recent regulatory network, as well as on dossiers that have been postponed several times.

An agreement on the **recovery and resolution** directive is expected by the middle of 2013, together with the revision of the **deposit guarantee schemes** directive. Indeed, the Commission will build on this element when presenting its next step in the banking union: a **Single Resolution Mechanism** with at its heart a Single Resolution Authority.

At the time of writing, the **CRD IV / CRR** package is in the last stages of the trialogue negotiations between the legislators, with an agreement expected in early 2013. Next to the prudential requirements and the distribution of responsibilities and competences, the issue of the date of implementation will be interesting to follow.

Furthermore, after the Autumn 2012 report of the high level expert group on **bank structure** chaired by Erkki Liikanen, the Commission has been mandated by the European Council to come forward with its own proposals. A legislative initiative is expected in 2013.

Following its July 2012 public consultation on **UCITS** - dealing in particular with a potential depository passport and eligible assets - the European Commission intends to adopt legislative proposals in the second half of 2013.

Following a public consultation on **shadow banking** carried out in 2012, and the work underway at FSB level, the European Commission intends to present legislative proposals in the second half of 2013. In particular, the Commission is focusing its efforts on a proposal on **Money Market Funds** and a review of the **Securities Law Directive** in order to tackle the issues of repo and securities lending.

The Commission is also planning to come forward in Q1 2013 with a proposal for a directive to review the **anti-money laundering directive** of 2005.

On the **data protection** regulation, agreements inside the European Parliament and the Council are expected in Spring with trialogues starting in the summer.

Regarding the **European Account Preservation Order**, the European Parliament is currently scheduled to go to plenary before the summer. On the Council side progress is to be expected as well and in parallel.

The European Commission is also planning to present a “**retail banking services**” package early 2013. This package will focus on **transparency of bank fees, bank account switching** and the **access to a basic bank account**.

Furthermore, the European Commission is working on several issues regarding **payments** and will come up with a proposal early 2013. In particular, the European Commission is working on the **review of Payment Services Directive**, focusing on surcharging and interchange fees, and is also looking closely at SEPA governance.

Indeed the European Commission announced that it will table a draft regulation which will ban, in the long run, the multilateral interchange fees in card payments, thus questioning the prevailing and well proven 4 corner model, which is today the basis of interoperability principles allowing acquiring and issuing banks to provide secure and high quality payment services to millions of card holders and merchants throughout Europe and beyond.

Another regulatory initiative currently under study by the European Commission is the right it wants to give to third party providers active in internet payments to accessbank account information. This initiative is posing many issues relating to customer demand, liability, risk, data privacy, banking secrecy, commercial agreements between the various parties, security of access and technical developments, etc., all to be carefully examined.

The **Savings Tax Directive** has been in negotiations since 2008 and promises to be on the table for a while. Developments around FATCA and any potential Rubik style agreements will have an impact on the issue and need to be watched.

Finally, the proposal for a directive on a **Financial Transaction Tax** for the Member States participating in the enhanced cooperation is expected in early 2013. The Commission has already announced that the text will be very similar to the 2011 legislative proposal for all 27 Member States.

2013 will again be a busy year on the legislative side, as will be the years to come when the post-2008 legislation will be up for revision. Indeed, in the new acts, new revisions have been built in which will be triggered over the next few years. The Commission is also entitled to decide on its own to review and report on the working of the existing legislation and thereby sustaining a high flow of EU legislative initiatives. Yet, thinking back to the 1999-2005 Financial Services Action Plan, has that not been the case ever since?

Brussels, 20 December 2012

Regulatory wave

▪ Exchange of information ▪ AIFMD ▪
ICSD & DGSD ▪ MiFID & MiFIR ▪ Retail
Banking Package ▪ PRIPs ▪ Crisis
management ▪ VAT ▪ Data Protection ▪
CSDs ▪ EMIR ▪ Shadow banking ▪ Account
preservation order ▪ Legal entity identifier ▪
AML 4 ▪ MAD / MAR ▪ Securities Law ▪ T2S
▪ Mobile payments ▪ Basel 3/ CRR/CRD IV ▪
FTT ▪ Banking Union & SSM ▪ UCITS 5 & 6
▪ Recovery & Resolution ▪ SEPA ▪
Bank structure ▪ Savings Tax Directive

2. Financial Market Regulation

Conventional wisdom has it that a good picture is worth a long discourse. This year in the financial market regulation section of the ABBL annual report we will try to innovate and give you a timeline of regulatory events that arose during the past year.

Regulatory Timeline 2012

JAN FEB MAR APR MAY JUN JUL

2011

19 February: agreement on the **EMIR regulation** Level 1.

20 February: publication by ESMA, EBA and EIOPA of level 2 consultation on the application of EMIR, notably to develop margin requirements, cost of out of clearing, reporting template to Trade repositories. The ABBL responds to the 3 consultations.

MIFID II: The Rapporteur on MIFID II in the European Parliament receives over 500 responses to his consultation on the MIFID draft regulation issued at the end of 2011 by the EU Commission. The ABBL's response is one of them.

CSD-R: The EU Commission issues its draft regulation for Central Securities depositaries. There are several highlights, among them: convergence on T+2 settlement, opening of CSD services to competition and, at the last minute, introduction of a derogation for CSDs with a banking license.

PRIPS: The EU Commission releases its draft regulation on Packaged Retail investment Products, with the aim to present on a 2 (to 3) page document all information needed by a retail investor so that he/she is able to discriminate among a range of similar products, be they insurance, structured notes, etc… and all this in plain English wording. The ABBL is supportive of the idea although the responsibility regime needs to be revised and wording of the different items should not be too simplistic.

16 August: **EMIR** is in force. All OTC derivatives trades that are in force from this date shall be reported to trade repositories, when available.

OTC Derivatives: IOSCO and BCBS publishes a consultation document on margin requirements for non-cleared OTC derivatives and the capital cushion required.

Shadow Banking: the European Commission launches a consultation on SB. It identifies REPO, securities lending, Money Market Funds, some form of re-insurance among a list of activities that would require banking-like prudential regulation.

AUG SEP OCT NOV DEC

2013

UCITS VI: A few days after its proposal on UCITS V, the EU Commission launches a general consultation on the UCITS framework under the UCITS VI label. The document can be understood as a return to basic UCITS principles.

26 September: The ABBL together with Deloitte publishes an update of the White Paper on **T2S**.

27 September: ESMA publishes its advice for Level 2 rules on **EMIR**, one of its main add-ons is the concept of indirect clearing (clearing offered by clients of clearing members to their own clients).

UCITS V: The EU Commission publishes its draft proposal on UCITS V. The purpose is to align the depositary and remuneration standards with those of the AIFM, adding some more responsibilities for the depositary, as UCITS are aimed at retail investors. The ABBL/ALFI Depositary Bank Forum comments on the proposal: convergence is the goal, AIFM standards are comprehensive enough.

Shadow Banking: the European Parliament prepares an own initiative report on its views on SB asking for generalisation of Trade Repositories for all transactions including REPO, Securities lending. The ABBL contributes to the report.

EMIR L2: Contrary to AIFM, the EU Commission fully translates ESMA advice into draft technical standards for level regulation on EMIR, defining notably indirect clearing and templates of reporting to Trade Repositories. But the regulatory story is not over yet, some more rules are required, notably capital requirement for non cleared OTC derivatives.

MIFID II: The text is adopted in the EU Parliament. This is the second of 3 versions, before the grand bargain where all texts will be reconciled into final and official version. The EP text is much more prescriptive in terms of governance structure (notably gender equality and composition and qualification of the boards). It builds around a complex approach regarding inducements where disclosures are privileged, even if Member States may impose more restrictive measures. For the EP, UCITS are not complex products, which is definitely good news for the industry. **MAD II**, Market Abuse Directive (and Regulation) are adopted the same day.

AIFM L2: After nearly one year of internal debate, the EU Commission finally issues its draft level regulation on AIFM – a core element is the new and much enlarged responsibilities of the depositary institution. The ABBL/ALFI Depositary Bank Forum lobbies intensively on this issue during the whole year.

Shadow Banking: The FSB (Financial Stability Board) publishes its consultation document on how to address SB, to determine which activities or institutions fall within its remit. The proposed approach is extremely extensive and considers that whenever there is a non-alignment between asset and liabilities there is a potential risk, thus even private equity funds may become shadow banking activities. Regarding REPO and securities lending the preferred approach is to introduce both a register and numerical haircuts or floor. The ABBL responds to this consultation (01/2013).

Financial Markets

As one may infer from the timeline on the previous page, the year 2012 was a very busy year. ABBL intervention was required in various places and at many different levels; from a local perspective with the development of fund regulation in Luxembourg up to the global level where the association shared its views on shadow banking. As may have been expected, 2012 was particularly intense on the MIFID regulation front, where the European Parliament made some surprising and unexpected moves, notably on the categorisation of the OTFs (Organised Trading Facilities) and on the disclosure of inducements paid or received, as well as on the governance structure and limitation of mandates at the top of financial firms. Interestingly, as 2012 came to a close, the EU Council, representing Member States, had taken no view itself and handed the dossier over to the Irish Presidency, and likely to the one after that, namely Lithuania. Fortunately, one dossier that is really advanced and can be nearly considered closed is the Market Abuse Regulation (number II), where both at the European Parliament and Council compromises have been reached. The text may, however, not work fully until MIFID II is implemented

Funds and depositary institutions

Two of the dossiers of the year impacting Luxembourg the most were the AIFM and UCITS V. Regarding the AIFM, from January until December, the industry lobbied the EU Commission to release a text, sticking to its initial position, namely asking the Commission not to deviate from ESMA's carefully balanced proposal, drafted after extensive consultation, and not to impose extra liabilities or burdens without clear benefits. On both counts the industry failed to make its voice heard and have its concerns taken into consideration, which now leaves the need for an adjustment in the various organisations to be ready by July 2013. The Luxembourg government has already worked on a draft transposition of the level 1 text and brought changes to the different connected regulations. The proposal should be voted in 2013. Regarding UCITS V, the EU Commission proposal published in July is considered to be a purely technical text of alignment with the AIFM to introduce similar responsibilities and duties for depositaries. Because UCITS are aimed mostly at retail clients, there was a political need to do more. The problem is that this may not be appropriate, given that the AIFM framework is very comprehensive and the rights attached to financial instruments is independent of who is the owner of an AIF or UCITS funds. US law or Uzbek law apply in the same manner to their respective instruments (a share of equity is a share of equity, whether it is bought by an AIF or a UCITS).

Post-trade markets

T2S made some progress, notably because there are now official signatures to the contracts between the CSDs and the ECB (European Central Bank). The timeline for implementation ranges from late 2015 for the first wave up to early 2017. The two CSDs qualified in Luxembourg have signed and will be in the second wave.

EMIR is the second important topic of 2012. In the cold winter of February, it saw its approval by the EU institutions, and 5 months later its translation into all EU languages and application across the EU (it is a regulation, not a directive). This does not mean that EMIR is workable as such. It took the three EU supervisory agencies, ESMA, EBA and EIOPA, the best part of 2012 to define level 2 measures, with the bulk of the work published just before Christmas by the EU Commission and pending tacit approval by the EU Parliament. Even when finished, it is likely that EMIR will not function before the end of this year as this level measure is only one part of the required regulation and that from 1 January 2013 a delay of at least 6 months is required for agreement of Central Counterparties, Trade Repositories or products subject to clearing.

Banking and Finance

3. Banking Supervision

Banking Union

The so-called “Banking Union” concept was mentioned for the first time at the EU Summit of 29 June 2012. This ambitious initiative aims at integrating, within the euro zone, the institutional framework of banking supervision. It consists of a Single Supervisory Mechanism (the SSM) placed under the responsibility of the European Central Bank, a single EU Deposit Guarantee Scheme and Resolution Scheme set up under the control of a EU Resolution Authority, and a single set of rules (the single rulebook). The motivation of the EU politicians is to restore confidence in the euro zone’s capacity to overcome the current crisis, paving the way towards a more complete fiscal, economic and political integration. Keeping pace with that momentum, the European Commission published in September a proposal of an EU Regulation transferring to the ECB the prudential supervision of banks established in the euro zone. The Commission also drafted a proposal amending the voting mechanism of the European Banking Authority, in order to reflect the new balance of powers between the countries participating to the SSM and those remaining outside of the SSM.

Three months later, concluding intensive discussions, the EU Parliament and the EU Council agreed on their respective positions. Since January, the EU tripartite negotiations Council/Parliament/Commission (i.e. the Trialogue) have been initiated by the Irish Presidency with the objective to reach a final agreement by the end of March 2013.

The ABBL has seized the opportunity to convey its position on this far-reaching topic, by emphasising first that quality of regulation should prevail over speed of implementation. The ABBL has also stressed that the SSM must fulfil the following conditions:

1. Independence is key. The ABBL has always insisted that any transfer of competences to EU-wide authorities is beneficial to the financial stability and to the public interest only if these authorities are fully independent from national political interests, and have the capacity, through a EU mandate and adequate governance, to make the general interest prevail over the national one.

2. The voting system of the new Supervisory Board to be set up inside the ECB must offer sufficient safeguards against the constitution of political alliances. Therefore, the ABBL thinks that it should be similar to the voting system of the Governing Council in monetary policy matters, which is based on the "one member, one vote" principle.

3. For the sake of efficiency, the ABBL thinks that the SSM should strike a right balance and preserve the effective role of the national supervisors in the conduct of the day-to-day supervision.

4. The SSM should solve the issue of allocation of powers between home and host supervisors in euro area Member States because it transfers the powers of both home and host supervisors to the ECB. However, it is important to introduce a safeguard ensuring that, where the ECB delegates back supervisory powers to the national supervisors, this does not create imbalances between the home and the host supervisors' powers.

5. It is foreseen that the ECB will authorise the establishment of credit institutions based on the preliminary assessment of the national supervisor. Whilst we agree with this procedure, the ABBL would nevertheless welcome a short time limit for the final decision of the ECB.

In order to ensure the consistency of the whole framework, the ABBL encourages the Commission to quickly table the proposals on the further blocks of the Banking Union. In this respect, we advocate the quick creation of an independent EU Resolution Authority, taking the form of an EU institution, backed by the national resolution funds. In parallel, it will be necessary to centralise at EU level the Resolution Fund and the Deposit Guarantee Scheme, which could be merged into a single Fund, and to clarify their possible linkages with the European Stability Mechanism.

EU Crisis Management Framework

On 6 June 2012, the Commission adopted a legislative proposal for bank recovery and resolution. The proposed framework sets out the necessary steps and powers to ensure that bank failures across the EU are managed in a way that avoids financial instability and minimises costs for taxpayers.

The ABBL supports the creation of a EU framework minimising the cost of bank failures for the society, and has communicated its key messages to the EU authorities:

1. It should be made clear in the Directive that decisions taken by the authorities or by the

EBA with regards to cross-border banking groups' recovery, early intervention and resolution guarantee that the financial stability will be preserved in the countries where a group operates.

2. Recovery and Resolution Plans of cross-border banking groups should be primarily elaborated at group level, which must be comprehensive and include all the legal entities belonging to the group. Regarding the legal entity level, we believe that Recovery Plans elaborated on a standalone basis only make sense for the groups' subsidiaries that are material: indeed, non-material subsidiaries do not have the capacity to overcome financial difficulties without the support of the group.

3. Decisions related to group resolution (i.e. resolution plans, implementing resolution tools, etc.) must be taken based on a joint agreement. In case of disagreement with the decision of the home resolution authority, the host resolution authority should be able to take its own decision on resolution measures affecting a subsidiary located in its jurisdiction.

4. The contribution of the Deposit Guarantee Schemes (the DGS) to the bail-in mechanism is a matter of concern. Indeed, forcing the DGS to absorb losses arising from resolution in the place of the covered depositors represents potentially a double burden for the DGS, because, in addition to the resolution losses, they will have to reimburse the covered depositors if the bank is liquidated. After the resolution of the institution new difficulties may arise, making a new resolution or a liquidation necessary, and triggering a second intervention by the deposit guarantee scheme. This will threaten the viability of any deposit guarantee scheme and it will also have a negative impact on financial stability, especially in times of financial stress. In the same vein, the ABBL strongly believes that the Directive should not impose on the Member States to remove the DGS' preference from their national insolvency law. This critical decision to rank the DGS *pari passu* with the other unsecured creditors should also be left to the discretion of the Member States.

Basel III / CRD IV

The European Commission published on 20 July 2011, the official proposal of the "CRD IV package" transposing the Basel III framework into EU legislation. The CRD IV proposal consists of a Regulation and of a Directive, both of which will replace the existing CRD. The Regulation constitutes the major part of the proposal as it contains the technical rules directly addressed to institutions. As a regulation, it will be directly applicable in all EU Member States without any transposition from the national supervisors. The Directive mainly contains rules addressed to Member States, needing transposition into national law (taking up of business, cooperation among authorities in the EU, etc.) as well as the pillar II requirements and the new capital buffers.

Since January 2013, the Irish presidency of the Council has taken over the Trialogue negotiations, with the objective to close the dossier by the end of March 2013. A few contentious issues remain to be agreed upon, namely the flexibility package (i.e. the degree of flexibility that national authorities and the Commission will be granted to set stricter prudential requirements), various points of the new liquidity rules, and the remuneration of the management bodies. As regards the timeline, the new requirements are likely to come into force by 1 January 2014.

In parallel, the Basel Committee released in January 2013 the amended version of the framework for the new Liquidity Coverage Ratio (the LCR). This new framework entails significant positive changes for the banking industry, whose major concerns have been taken into consideration by the Basel Committee. Among others, the ABBL welcomes the extended implementation period of the LCR that will become fully binding in January 2019, the eligibility of additional asset classes to the pool of High Quality and Liquid Assets, and the lowering of some outflow factors (e.g. on deposits taken from non-financial corporate). The ABBL calls on the EU authorities for a prompt integration of the revised LCR in the CRD IV framework.

Structural Reform of the EU Banking Sector: the Liikanen Report

The High-Level Expert Group (HLEG) chaired by Erkki Liikanen, Governor of the Finnish Central Bank, was established by the European Commission in February 2012 with the mandate to consider whether there is a need for structural reforms of the EU banking sector to establish a safe, stable and efficient banking system serving the needs of citizens, the EU economy and the internal market. The HLEG released its final report on 2 October 2012, which was subject to an open consultation from 2 October - 13 November 2012. After this, the Commission will consider the next steps, including a possible legal proposal.

The main and most controversial recommendation of the Liikanen report touches the mandatory separation of proprietary trading activities and other significant trading activities, including the market-making activity, exceeding a certain threshold. Moreover, a broader separation of activities may be imposed by the supervisors based on their assessment of the Recovery and Resolution Plans to be drafted in the context on the Crisis Management Directive.

In its response to the consultation, the ABBL shared the general concerns expressed by the European banking industry on the impacts of the proposed measures:

1. Negative impacts on the universal banking model through the reduction of the diversification benefits within a banking group: the centralisation of liquidity management or the allocation of capital across business lines will become less effective in the future;

2. Creation of a two-tier system where banks below the separation threshold will benefit from an undue competitive advantage;

3. Increase of the funding costs for the trading entity and, hence, for the banking group with negative consequences on the financing of the "real economy";

4. The possibility of a broader separation resulting from the Recovery and Resolution Plans' supervisory assessment is too intrusive and creates legal uncertainty. We do not agree that supervisory authorities interfere in the business model of banks, or require changing their legal or operational structure. It is not the role and not the responsibility of the authorities to shape ex ante the organisation of (highly) regulated banking institutions when they are in a situation of going concern.

The ABBL believes that the finalisation of the ongoing international regulatory reform agenda – including important measures still in the pipeline – will help reach the regulatory objectives mentioned in the mandate of the HLEG, e.g. i) to increase the stability of the European financial sector by reducing risk both at micro and macro level; ii) to ensure orderly resolution of financial institutions – also for systemically important banks – without having to call on taxpayers; iii) to maintain the integrity of the Internal Market and iv) to ensure the ability of banks to serve the real economy.

Legal and Tax

4. Legal and Tax

FATCA

2012 has been another busy year when it comes to FATCA. Unlike 2011, where the main effort was directed towards an essentially high level assessment of the legal and policy challenges resulting from FATCA, during 2012 greater focus was placed on the implementation side. This move is due essentially to the release by the U.S. Department of Treasury of many of the relevant operational provisions throughout the year and the existence of looming compliance deadlines. The discussions on the appropriate intergovernmental agreement (IGA) for Luxembourg constituted the other main point of attention.

Regulatory framework unveiled

On 8 February 2012, the U.S. Internal Revenue Service (IRS) released nearly 400 pages of proposed regulations under FATCA (the Proposed Regulations), which follow up on guidance previously issued in the form of notices in 2010 and 2011. On the same day, the IRS also released a joint statement indicating that it is pursuing FATCA partnerships with France, Germany, Italy, Spain and the United Kingdom, the aim of which is to reduce the legal impediment to compliance, simplify practical implementation and reduce the costs incurred by financial institutions.

The release of this regulatory package was followed, on 15 May 2012, by a hearing held in Washington. Twenty speakers, including a representative of the European Banking Federation from the ranks of the ABBL, gave testimony to a panel of IRS and US Treasury personnel. The implementation timeline and proposed FATCA partnership agreements mentioned above were among the most recurrent themes of testimony.

In the meantime, at the ABBL level, these events prompted the creation, in May 2012, of a specific working group with a representative panel of project managers from our members, which met, and still meets, on a regular basis in order to discuss FATCA from an operational perspective and, where appropriate, define best practices with respect to the most salient matters.

Implementation timeline

The IRS released on 24 October 2012 Announcement 2012-42, which provided that the final regulations on FATCA (the Final Regulations), when issued, will:

- defer the earliest effective date of FFI agreements until 1 January 2014;
- postpone, basically by six months, the effective dates prescribed in the Proposed Regulations for client on-boarding and pre-existing ac-

counts review, so as to align these dates to those prescribed in the Model IGAs; and
- defer gross proceeds withholding until 1 January 2017.

This revised timeline, which is effectively upheld by the Final Regulations, provides notably for the convergence of multiple FATCA deadlines on 1 January 2014, with various FATCA due diligence, reporting and withholding obligations (the latter with respect to prima facie financial institutions) now being effective within the same year.

Which Model IGA for Luxembourg?

On 8 November 2012, the US Treasury announced that 50 countries, including Luxembourg, are in discussions regarding intergovernmental agreements on FATCA (IGAs). On 11 December 2012, a press release from Minister Frieden confirmed the Government's willingness to initiate, within short notice, the formal negotiations of the Luxembourg IGA with the US Government.

When it comes to the format of the IGA proper, two alternatives are at stake: on the one hand, the so-called "Model 1", based on the negotiations carried out between the United States and the "G5" countries, and, on the other hand, the so-called "Model 2", based on the approach adopted by the Swiss Government (and, to a certain extent, the Japanese Government). Model 1 essentially requires the financial institutions of the relevant partner country to report information to their national government on the basis of domestic legislation, followed by the automatic exchange of information by said government with the USA. Model 2, by contrast, requires financial institutions of the relevant partner country to report directly to the USA both account-specific information for non-recalcitrant account holders and aggregate information for recalcitrant account holders, according to FATCA regulations, supplemented by exchange of information upon request between the relevant national government and the US Government with respect to US recalcitrant account holders.

The pros and cons of each Model IGA and their respective implications at EU level are carefully assessed by the Government, notably in light of the most favoured nation clause set forth under article 19 of Council Directive 2011/16/EU of 15 February 2011 on administrative cooperation in the field of taxation. In this respect, the ABBL is of the opinion that Model 1, in the sense that it would automatically trigger the application of the most favoured nation clause under Directive 2011/16/EU, would immediately take away any room for manoeuvring vis-à-vis EU partner countries with respect to all matters pertaining to automatic exchange of information so that, in the present political context, the conclusion of an IGA based on Model 2 constitutes the preferred alternative.

On the technical side, the main effort is currently focused on the preparation of the Annex II of the IGA, which lists the institutions and products that would meet the requirements under FATCA to be an exempt beneficial owner or deemed compliant FFI, or the extent to which the products would meet the requirements to be excepted under the definition of financial account under FATCA. This document, together with the covering justifications to be provided to the US Government, is under preparation by a joint working party involving members of the ABBL, ALFI, ACA and the association of the Luxembourg pension funds (ALFP), which reports to the competent officer at the Ministry of Finance on a regular basis.

Some points to consider for 2013

- The IRS eventually released the long-expected final regulations under FATCA on 17 January 2013 (officially published on 28 January 2013). Still to come are numerous additional items, such as the draft FFI agreement, details about the FFI registration portal, which should be accessible by 15 July 2013, and revised forms W-8 to identify account holders.
- The formal negotiations on the Luxembourg IGA should start by mid-March 2013. One can reasonably assume that the decision about the appropriate Model IGA will be met by then. Minister Frieden has recently announced that the aim is to conclude the IGA by Q3 2013 at the latest. One should bear in mind that the domestic implementation package needs to be adopted by the end of the year.
- The OECD is currently discussing the adoption of TRACE as the reporting channel under FATCA. As far as the European banking industry is concerned, the merits of TRACE, notably from an economic perspective, remain to be assessed, considering in particular the fact that European banks are currently using another IT interface under the EU Savings Directive. The European Banking Federation is to provide input in this respect via a dedicated task force created in November 2012 (“TRIES”).

Exchange of information for tax purposes

Luxembourg currently relies on *exchange of information on request*, as enshrined in most of its double tax treaties (DTTs), as the most proven and balanced technique of exchange of information, notably in terms of privacy rights and data protection. The ABBL welcomes and supports this approach. Significant development towards an expansion of the scope of the information that can be requested by foreign tax authorities or, as the case may be, that shall be provided to the same authorities on an automatic basis, have occurred throughout the year.

■ Taking stock of current policy and practices

Following the spring 2009 G20 Meeting in London, Luxembourg has enacted a significant change in its double tax treaty policy towards the adoption of information exchange clauses modeled on Art. 26(5) of the OECD Model Tax Convention (OECD-MTC). Through a law dated 31 March 2010[1] (the 2010 Law), 15 protocols to existing double tax treaties (DTTs) and 5 new DTTs containing an exchange of information clause modelled on Art. 26(5) OECD-MTC were ratified and a specific procedure for the treatment of information exchange requests under these clauses was enacted. Further to the ratification of 7 additional DTTs, as of 1 January 2013, out of 64 DTTs concluded by Luxembourg that are in force, 44 of those DTTs contain an exchange of information clause that fulfils the OECD standards and for 25 of that group, such a clause is already enforceable[2]. This group of 25 countries should be extended to another 12 countries within relatively short notice upon adoption by

1 *Loi du 31 mars 2010 portant approbation des conventions fiscales et prévoyant la procédure y applicable en matière d'échange de renseignements sur demande.*

2 The new clause is already applicable vis-à-vis: *Armenia, Austria, Bahrain, Barbados, Denmark, Finland, France, Germany, Hong Kong, Iceland, India, Japan, Liechtenstein, Mexico, Monaco, the Netherlands, Norway, Panama, Portugal, Qatar, Spain, Sweden, Switzerland, Turkey and the United Kingdom. The new clause has already been concluded, but has not yet entered into force, pending ratification by both contracting States, vis-à-vis the following countries: Belgium, Canada, Croatia, Italy, Kazakhstan, Macedonia, Malta, Mauritius, Oman, Poland, the Republic of Korea, Romania, Russia, San Marino, Saudi Arabia, Seychelles, Sri Lanka, Tajikistan and the United States* (source: *Administration des contributions directes*).

the Parliament of the relevant draft bill tabled by the Government on 20 November 2012[3]. In the meantime, comparable standards have become generally applicable in relation to all 27 EU Member States as of 1 January 2013 upon entry into force of Council Directive 2011/16/EU of 15 February 2011 on administrative cooperation in the field of taxation.

The extent of the information that can be provided by the Luxembourg authorities on the basis of the exchange information clause modeled on Art. 26(5) OECD-MTC is defined by reference to the criterion of the "foreseeable relevance" of the requested information, a concept in turn closely bound to the concept of "fishing expedition". Both concepts have been significantly refined by the applicable case law handed down by Luxembourg courts since the adoption of the 2010 Law[4].

As of 31 December 2012, about 20 judgments have been handed down by the administrative courts with respect to information requests lodged by foreign tax authorities on the basis of treaty provisions modeled on Article 26(5) of the OECD Model Tax Convention. Most of the judgments of the court of first instance (*Tribunal administratif*) have been subsequently appealed before the administrative court of appeal (*Cour administrative*) and the underlying information requests invariably originate so far from 3 jurisdictions, namely France, the Netherlands and Sweden.

From the above-mentioned case law, one can conclude that an information request relates to "foreseeably relevant information" in the sense of Art. 26(1) OECD-MTC, and thus does not constitute a "fishing expedition", if

(i) it relates to one or several specific tax files or given taxpayers; and

3 *Projet de loi n° 6501 portant approbation de conventions fiscales et prévoyant la procédure y applicable en matière d'échange de renseignements sur demande*. This draft bill provides for the ratification, on the Luxembourg side, of protocols to 8 existing DTTs concluded with *Canada, the Republic of Korea, Italy, Malta, Poland, Rumania, Russia and Switzerland*, and the ratification, still on the Luxembourg side, of 5 new DTTs concluded with *Germany, Kazakhstan, Macedonia, Seychelles and Tajikistan*.

4 See in particular: Cour administrative, 21 May 2012, no. 29869C.

(ii) the said request unequivocally identifies the taxpayers effectively under investigation.

This being said, these concepts remain a moving target and will certainly be further discussed and refined in the context of grouped requests, as further discussed below.

Grouped requests

The OECD updated, on 17 July 2012, its commentary to Article 26 OECD-MTC. This update explicitly allows for grouped requests, meaning that tax authorities are able to ask for information *on a group of taxpayers, without naming them individually*, insofar as the requesting State provides, inter alia, a detailed description of the group of taxpayers targeted. A grouped request may for instance target a determined number of taxpayers that can be separately identified on the basis of an individual criterion (e.g. a credit card number). Such a kind of request constitutes, in fact, the sum of individual requests each relating to a taxpayer that can be unequivocally identified. More questionable, to our view, would be a request that would relate to an undetermined number of taxpayers defined on the basis of a generic behavioral pattern (e.g. the subscription to a certain financial product).

According to the OECD, all OECD member countries have endorsed this update on grouped requests and it seems that the Luxembourg tax authorities are willing to apply the same to any requests lodged on or after 17 July 2012, that is based on *existing* treaty provisions modeled on Art. 26(5) OECD-MTC by virtue of the so-called principle of *dynamic interpretation of tax treaties*. This approach, which currently prevails among tax authorities and seems to be upheld by Luxembourg courts[5], is questionable and one could legitimately expect, at the very least, additional exchange of letters between Luxembourg and the relevant contracting States clarifying the conditions of the exchange of information with respect to grouped requests.

All in all, the ABBL is of the view that an overhaul of the current domestic provisions pertaining to information exchange, notably the 2010 Law, which was enacted in the context of individual information requests, needs to be updated and there is an even more pressing need to clarify the permissible scope of such requests.

Automatic exchange of information

Luxembourg essentially implements the automatic exchange of information within the

5 See: *Tribunal administratif*, 15 November 2012, no. 30799.

framework of the Savings Directive 2003/48/EC[6] regarding payees who have elected the information exchange route (and who are not, therefore, subject to the 35% withholding tax otherwise applicable), subject, however, to appropriate safeguards. Luxembourg paying agents can only report the relevant personal information regarding a payee to the Luxembourg tax authorities (for continuation to the tax administration of the payee's country of residence) if the payee has given, beforehand, *an explicit and unconditional mandate* to the paying agent to transfer, via the Luxembourg tax authorities, said information to the foreign tax authority[7]. One can expect that these requirements, in terms of qualified consent from the payee, will be strengthened in the future considering the terms of the draft EU Data Protection Regulation unveiled by the European Commission on 25 January 2012 that will supersede, at some point, the current EU Data Protection Directive 95/46/EC[8].

The interaction between FATCA and the political debate on the automatic exchange of information at EU level has already been mentioned in the present report. Incidentally, it is noted that, as of 31 December 2012, the relevant directive (Council Directive 2011/16/EU) has not yet been transposed into Luxembourg law, pending the adoption of the relevant draft bill by Parliament[9].

Going forward, another form of automatic exchange of information, the *spontaneous exchange of information*, will result from the transposition into Luxembourg law of article 8 of the aforementioned Council Directive 2011/16/EU, which provides that, no later than 1 January 2015, Luxembourg will be required to exchange, among EU Member States, information pertaining to residents of other EU Member States, with respect to taxable periods starting on 1 January 2014, and concerning (at least) three specific categories of income listed under said article 8, to the extent that said information is already available to the Luxembourg tax authorities. So far, Luxembourg intends to communicate automatically on income from employment, Director's fees and pensions.

6 Council Directive 2003/48/EC of 3 June 2003 on taxation of savings income in the form of interest payments.

7 Art. 13 Savings Directive.

8 Council Directive 95/46/EC of 24 October 1995 on the protection of individuals with regard to the processing of personal data and on the free movement of such data.

9 *Projet de loi portant transposition de la directive 2011/16/UE du Conseil du 15 février 2011 relative à la coopération administrative dans le domaine fiscal (…).*

Financial Transaction Tax

During 2012, it became clear that EU Member States had insurmountable divergences of opinion on the question whether to introduce a financial transaction tax. This situation temporarily slowed down the – barely disguised - rush towards money of certain member states, but the most cash hungry amongst them quickly came up with a new approach, the "enhanced cooperation procedure". The decision of the Council to authorise 11 member states to proceed with the implementation of the tax will certainly lead to a quick adoption of the directive amongst these Member States.

Previous experiences with similar taxes in Sweden and, more recently, in France (with a less ambitious scope), clearly indicate that relocations or substitutions of activities *will* take place. The existence of a "two-speed Europe" combined with *a very extensive and extraterritorial scope* of the future directive puts Luxembourg in a very difficult position:

- on the one hand, the actors of the Luxembourg financial sector need to ensure their *competitiveness* compared to countries (EU and non-EU) that do not participate,
- on the other, they *will be more hit than others* by the indirect and extraterritorial aspects of the tax, because of their closely interwoven relations with the surrounding neighbouring countries applying the tax.

The EU Commission now has adopted a proposal of a directive for the 11 countries that wish to take part. Adoption of a proposal does not mean adoption of the directive. The European Parliament needs to give its opinion and there will certainly be a lot of discussions around this directive during the rest of the year. However, the Commission (and the 11 Member States) have set a very ambitious timeline for its adoption and the *Lisbon Treaty* has removed any possibility of a veto of the non-participating countries, … *except if* vital interests are concerned.

The ABBL, like ALFI, were deeply involved and will now be even more so to at least fight the *most burdensome* extraterritorial aspects of the tax, such as the "*issuer principle*". This principle obliges financial intermediaries in non-participating countries to apply the tax to securities issued on the territory of one of the 11 countries, *even if the* financial intermediaries' country has decided to not apply the tax. The 11 participating countries justify this approach with the fact that the "*place of birth*" of the security is within their territory. But this *link* trying to justify a taxation right of the issuer countries is very doubtful, as there is also the *ownership link*, which seems to constitute a much stronger relationship (with the country where the old owner of a security agrees with the new one on the transfer of ownership). In other words: as the company having issued the security only passively supports the change of ownership (obligation to register the change of ownership in its shareholder's register), there might be a link to this country, but the place where the buyer and seller "shake hands" to agree on the transfer of ownership seems to constitute the stronger link and the only one that is *genuine* enough to create taxation rights of a country.

Whatever the outcome of this debate will be, one thing is certain: a Europe of two speeds necessarily implies the creation and the future existence of a (more or less) deep trench between both parts of Europe.

New developments in the area of anti-money laundering

1. New FATF recommendations

In February 2012, the Financial Action Task Force (FATF), whose mandate has been renewed for a further eight years, issued new recommendations for combating money laundering and the financing of terrorism. The revised FATF Recommendations integrate counter-terrorist financing measures with anti-money laundering controls and introduce new measures to counter the financing of the proliferation of weapons of mass destruction. They also strengthen the requirements for higher risk situations and allow countries to take a more targeted risk-based approach.

The main changes are:

1. An enhanced risk-based approach which enables countries and the private sector to apply their resources more efficiently by focusing on higher risk areas: Countries, financial institutions and non-financial professions are explicitly required to identify, assess and understand their money laundering risks.

2. Expansion of the scope of predicate offences to money laundering to include serious tax crimes: Tax crimes become an additional designated category of offences, but it is left to countries to define serious tax crimes.

3. Combating the financing of the proliferation of weapons of mass destruction through the consistent implementation of targeted financial sanctions when these are called for by the UN Security Council. This means freezing action as well as prohibitions on making funds available to designated persons and entities.

4. Improved transparency to make it harder for criminals and terrorists to conceal their identities or hide their assets behind legal persons and arrangements: When performing customer due diligence measures in relation to customers that are legal persons or legal arrangements, financial institutions should be required to identify and verify the customer and understand the nature of its business, and its ownership and control structure. They have to identify the beneficial owners of the customer and take reasonable measures to verify the identity of such persons. This also means requiring that there is reliable information available about the beneficial ownership and control of companies, trusts, and other legal persons or legal arrangements.

5. Stronger requirements when dealing with politically exposed persons (PEPs): The scope of the Recommendations is extended from foreign PEPs to domestic PEPs and international organisations PEPs in higher-risk situations. For family members and close associates the same measures are to be applied as for PEPs.

6. Additional requirements have been added to enhance the transparency of cross-border wire transfers: Financial institutions should include beneficiary information on wire transfers; Information should be included below the USD/EUR 1000 threshold but should not be verified unless there is a suspicion.

The FATF 4th Round of mutual evaluations is scheduled to start in the 4th quarter of 2013, and will place much stronger emphasis on effective implementation of revised FATF Standards.

2. The CSSF Regulation 12-02 on the prevention of money laundering and terrorist financing

The CSSF regulation N°12-02 of 14 December 2012 on the fight against money laundering and terrorist financing (AML/CTF) was published in the *Mémorial* of 9 January 2013. It was adopted on the basis of the law of 23 December 1998, which gives the CSSF a regulatory power. The Regulation applies to all professionals who are subject to article 2 of the AML Law of 12 November 2004 (as amended) and who are supervised by the CSSF.

It intends to remedy the deficiencies that were pointed out by the FATF towards the CSSF Circulars, due to the fact that they were non-binding instruments, and that they were not updated with the latest changes in the field of AML / CFT and often limited to recalling the legal obligations without specifying how to effectively implement them. The CSSF Regulation intends to clarify the existing regulatory framework following the adoption of the Grand-Ducal Regulation and the Law of 27 October 2010. To this end, it largely recalls and, if necessary, completes the topics in the CSSF Circulars 08/387 and 10/476, which were subsequently repealed by the CSSF Circular 13/556, issued on 16 January 2013.

The text gives clarifications as to the risk-based approach to be adopted by the professionals with a view to identifying and mitigating money laundering and terrorist financing risks they are exposed to. It also addresses customer due diligence obligations and internal organisation requirements:

Risk based approach: Professionals must perform an assessment of risks of money laundering and terrorist financing. The methodology set forth in the regulation comprises a risk assessment based on various criteria such as client risk, country risk, risk associated with products, transactions or distribution of the product. The risk assessment of each new client needs to be done prior to client acceptance and the risk score of each client must be kept up to date. The same is required for new products prior to the product launch.

Customer due diligence obligations: Each new customer relationship is subject to the written authorisation of the appropriate level of hierarchy and, when relevant, to the designated person in charge of AML. The information on the origin of funds must be part of the initial customer due diligence. Concerning the identification of beneficial owner, professionals shall take all reasonable measures to get the assurance of its real identity. A beneficial owner can, notwithstanding the 25% of ownership threshold, be a person who owns or controls less than 25% of a legal structure but who is nevertheless the person who ultimately controls this legal structure. The beneficial owner is no longer required to sign himself a declaration, but clients must sign a declaration concerning the beneficial ownership and must inform the professional in case of any change.

Internal organisation requirements: The AML/CFT policy of the professional must reflect all professional obligations, even if procedures, policies and control measures may be adapted to the activity, structure, size, organisation and resources available. The policies and procedures must be validated by the person in charge of AML/CFT and, if required, regularly updated. The monitoring process and screening controls shall be applied to all clients, beneficial owners and proxies for all accounts and, for all transactions, to the originator of a transfer in and the recipient of a transfer out of the client account. This control must be automated unless the professional can prove that the volume and nature of clients and monitor transactions do not require such automation.

At last, the person in charge of AML/CTF must have the professional experience, the knowledge of the Luxembourg law and regulations in AML/CTF, the hierarchy level and the necessary authority within the organisation and the availability to exercise effectively its responsibilities.

The new legal framework on the fight against over-indebtedness

The Law of 8 January 2013 on over-indebtedness has created a new legal framework applicable in Luxembourg.

The principle governing the adoption of this law lies in the Government's desire to better tackle the phenomenon of over-indebtedness. The law has a dual objective: on the one hand, to amend the procedures stipulated in the context of the Law of 8 December 2000 on over-indebtedness, and on the other hand, to introduce a regime of civil bankruptcy under Luxembourg law, by taking inspiration from existing regimes in neighbouring countries.

The ABBL considers, however, that the preventative component of over-indebtedness has been completely neglected. It was already absent from the Law of 8 December 2000, and the Law of 8 January 2013; even though the explanatory memorandum openly affirmed that the law was supposed to strengthen the preventative component of the fight against over-indebtedness, it only arises at a very late stage in the bankruptcy proceedings, i.e. only concerning people who are already in debt. In reality, the law does not contain any specific legal provisions concerning actual preventative actions, in particular in favour of young people in order to prevent one of the causes of over-indebtedness, which is often, according to the authors of the draft law, "*a careless attitude and inability to draw up a family budget*". Contrary to what may have been stipulated, situations of over-indebtedness are not routinely born out of lax policies by Luxembourg credit institutions when granting consumer credit. We cannot hold the banker responsible for the over-indebtedness of certain clients. The banker, when receiving a credit application, assesses the suitability of the loan in accordance with the borrower's resources at the time of the application. The subsequent development of the borrower's financial situation (often linked to personal events) cannot be taken into consideration. Bankers cannot be held responsible for failing to predict the events that may occur during the lifecycle of a loan.

The ABBL does not intend to defend the interests of banks over those of over-indebted persons, but aims to defend the interests of diligent borrowers over those who do not pay. It is the conscientious borrower who will *ultimately* have to sustain the cost of additional requirements imposed on professionals by recalcitrant debtors.

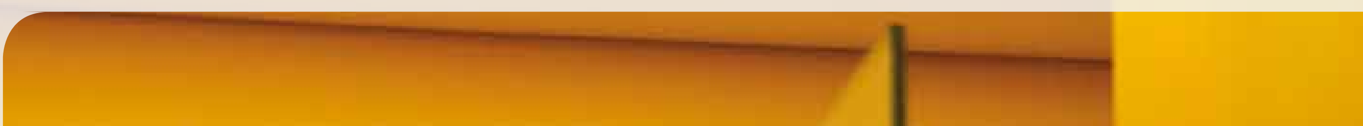
From now on, the collective debt settlement procedure will consist of three phases: the conventional settlement phase before the Mediation Committee; a judicial settlement phase before the first instance court; and the personal debt restructuring phase before the first instance court. This third phase is reserved for private individuals who are excessively indebted and whose situation is irreparably compromised. It consists

of wiping out non-professional debts with the liquidation of assets.

It is clear that there is no compelling need to introduce such a regime in Luxembourg. However, it is advisable to weigh up the need for such a system with its negative effects and to evaluate the comparative nature of the measure as regards the actual needs of our society. On the one hand, over-indebtedness remains a purely marginal issue in Luxembourg. On the other hand, the introduction of the civil bankruptcy regime leads to the establishment of an exception regime having particular implications on common law and which is not without adverse effects: the solution of completely wiping out a person's debts undermines the principle of the binding power of contracts. Furthermore, the law stipulates that the guarantor and the co-debtor automatically benefit from the same measures as those provided to the over-indebted party when they have guaranteed the commitment of the over-indebted party. The protection measures for guarantors raise questions about the fundamental principles of our law, such as freedom of choice, the binding power of contracts and the implementation of good faith. The questions raised regarding guarantee contracts in this context undermines the judicial security of contracts concluded between parties.

It should also be noted that the ever-increasing intervention of public bodies in private lives increases the demands of the public with regard to a State which must be omnipresent and intervene to resolve all of society's ills. It is also of grave concern that the prospect of a total and definitive debt write-off would lead to the removal of the burden of responsibility on borrowers.

The law creates a directory centralising the appraisals and information established in the context of the procedure on the collective settlement of debts. According to the text of the law, the directory is an information source for creditors, guarantors and joint debtors of the over-indebted party on the state of progress of the procedure on the collective settlement of debts. The question arises as to the precise role of this directory as only natural persons can consult it. If the credit institutions are not given access to the directory, the objective sought is only partially fulfilled and does not adhere to its aim of informing all persons having an interest in the procedure on the collective settlement of debts. Moreover, if credit institutions are not given access to the directory, such a provision would violate the consti-



tutional principle of fairness before the law, under which all creditors should be treated equally.

Furthermore, the question arises as to whether this directory may or may not be used in the context of obligations resulting from Article L.224-10 of the consumer code. It is the obligation of the lender to assess the solvency of the borrower "*from a sufficient number of sources of information*". Therefore, the question arises as to whether potential lenders could also have access to this directory. Such broader access would ensure that an over-indebted person could not be granted a loan, as it would further exacerbate their financial situation.

While we commend the procedural improvements to the law on over-indebtedness, the ABBL is disappointed by its imperfections. This text provides no preventative measures relating to over-indebtedness. Furthermore, the text undermines the soundness of our law; the search for solutions to certain exceptional situations should not call into question the fundamental principles of our law. To conclude, the text is not without undesirable consequences, as over-indebted persons will now rely on the State to resolve their financial problems, by hoping for complete debt relief.

National VAT developments

Discussions with the VAT authorities

The ABBL is currently in discussion with the Luxembourg VAT authorities aiming to set up a more precise definition of the methods which could be used for the calculation of the input VAT recovery ratio, as well as more precise description of the VAT treatment of derivatives and precious metals. The aim is to obtain a higher degree of legal certainty and to ensure that the methods used by the banks are fair, reasonable and reflect the activities carried out by them. The clarifications should also enable VAT authorities to better control the methods used.

In fact, the current general VAT regime is not well adapted to deal with the highly complex derivatives and precious metals market. Providing a clear framework for the operations regarding VAT is essential in order to respond to the growing demands as a result of the development and generalisation of transactions for these kinds of products.

In this context it should be noted that some European countries, like the United Kingdom, have adopted an attractive specific regime which represent a competitive advantage over other countries.

AGDL – Deposit guarantee and investor compensation

The “Association pour la Garantie des Dépôts Luxembourg” (AGDL) was established in 1989 as a non-profit association. Its purpose is to set up a mutual guarantee scheme covering cash deposits of the customers of credit institutions. The structure of the AGDL could easily adapt to the European Directive 1994/19/EC. Since the European Directive 1997/9/EC, claims arising out of investment transactions in favour of investors with credit institutions and investment firms are also covered.

The ABBL and the AGDL are two separate and independent organisations, but they are closely linked, especially through a service level agreement by which the day-to-day administrative work of the AGDL is carried out by the ABBL secretariat and staff.

On 8 and 9 October 2008, the Tribunal d’Arrondissement of Luxembourg, together with the CSSF, declared three Banks in suspension of payment: 1) Glitnir Bank Luxembourg S.A., 2) Landsbanki Luxembourg S.A. and 3) Kaupthing Bank Luxembourg S.A.

The process of compensation of the clients was successfully managed by the AGDL on the basis of a long-standing outsourcing contract with a consultant firm and thanks to the fully efficient computerised system, developed in cooperation with this consultant and the substantial efforts made by its staff.

The Glitnir case was already closed in 2009 with a restructuring plan and the AGDL recovered its debt.

In July 2009, Kaupthing was split into two parts: 1) Pillar Securitisation S.à r.l., taking over the debts of Kaupthing and 2) creation of a new Bank “Banque Havilland S.A.” which took over the customers of Kaupthing with their deposits, while the customers of the Belgian branch were taken over by Keytrade Bank. The recovering process began in August 2009, and the AGDL receives reimbursement 4 times a year. This will continue in 2013.

The Landsbanki case has almost been closed since 2011 when the AGDL recovered its debt due to the consent by the Luxembourg Central Bank and Landsbanki Islands to restructure their claims against the estate of Landsbanki Luxembourg, which granted seniority to the claims of the other creditors of Lansdbanki Luxembourg.

After 9 October 2008, no failure of a member of the AGDL has been registered.

On the European level, most of the time in 2012 was spent on the reform of the deposit guarantee system. The efforts to improve the draft Directives for Deposit Guarantee Schemes (DGSD) and Investor Compensation Schemes (ICSD), issued in 2010, continued in 2012. The AGDL participated in many Working Groups at the European Forum of Deposit Insurers (EFDI), the European Banking Federation and the European Commission. The trialogue between the European Commission, the European Parliament and the European Council on the DGSD and the ICSD did not progress enormously in 2012. Moreover, new ideas and proposals concerning DGS appeared in other draft proposals of the European Commission, in particular in:

- the draft Capital Requirement Directive (CRD IV),
- the draft Bank Recovery and Resolution Directive
- the proposals concerning the Banking Union

The Council and the members of the AGDL were regularly informed of the evolution of the discussions at the European Institutions. The President and the Secretary of the AGDL also met some members of the European Parliament to let them know our opinion and concerns about these projects. This work will continue in 2013.

On a national level, as a consequence of all these European projects, the draft law on a “new” AGDL did not progress and remains postponed by the Luxembourg authorities.

On an internal level, the AGDL, in collaboration with its consultant firm and the CSSF, continued to improve the computerised payment system, especially regarding the adaptation to the 20-day pay out delay. Simultaneously, this team worked on the project of introducing the “Single Customer View” regulation, so that all members will have to be able to produce a single view of the assets of their clients. This work was concluded by the publication of the CSSF Circular 13/555.

In 2013, the AGDL will have to follow the further development of the European projects as well as the application of the “Single Customer View” Circular and provide assistance to its members in that matter. Another project is the remodelling of the AGDL’s website, together with its consultant firm.

5. The Private Banking Group, Luxembourg

The Private Banking Group, Luxembourg (PBGL) is the ABBL's first business line cluster and federates Luxembourg private bankers' interests within the ABBL's general policy. The PBGL is composed of high-profile representatives from ABBL members active in the field of private banking. Its missions include the definition and implementation of strategic measures to the benefit of Luxembourg private banking and its environment, a close cooperation with Luxembourg for Finance, the agency for the development of the financial centre, with regards to the definition and execution of financial centre development efforts, as well as the development of private banking training measures, certifications and standards. It counts 50 Members all directly active in the field of Private Banking.

The PBGL's Executive Board acts as a steering organ for an array of working groups composed by practicing private banking specialists and executives. The Executive Board is composed of senior financial centre figures with direct responsibilities in leading Luxembourg private banking operations. Working groups are active in various fields linked to strategy, training and talent management, product and service innovation, business intelligence, international positioning, public relation and promotion efforts, as well as industry-related legal and tax expertise.

The Members' Meeting held in June was an occasion to review main PBGL achievements and announce priorities for the upcoming year. Delegates validated PBGL achievements and encouraged the Executive Board and affiliated working groups to continue their efforts.

Besides closely following and accompanying developments on the regulatory front, throughout 2012 Luxembourg Private Bankers took next steps with regards to strategic priorities identified in the strategic plan for Luxembourg Private Banking. A collection of strategic papers is available to Members upon request at the ABBL Secretariat.

PBGL Members are convinced that a constant adaptation of available solutions to the needs of increasingly sophisticated and international clients is necessary to remain recognised as International Private Banking centre of excellence. Some developments can be conducted at individual bank level, others need joint moves at financial centre level.

The adhesion to the principles and subsequent ratification of the ICMA Wealth Management Charter of Quality was an important milestone of the past year. On 4 October, on the occasion of an international event on quality in Wealth Management featuring high-level keynote speeches by Minister Luc Frieden and Mr Jean Guill, Director General of the CSSF, the ABBL was the first association to ratify the ICMA Charter of Quality. A video featuring the strongest messages of the event is available via the ABBL website. Since then, all Luxembourg based Private banks, as well as a number of PSFs, have ratified the Charter of Quality on an individual basis. In an environment where regulation and compliance for the wealth management industry are playing an increasingly important role in client relationships, the Charter of Quality sets out in a single document the overall guiding principles of the private wealth management industry in a straightforward manner which clients will find easy to understand. The Charter is designed to be consistent with relevant regulation at the European Union and national level, and to complement principles such as the Wolfsberg Principles on Anti-Money Laundering and the Global recommendations of the Financial Action Task Force.

The three main principles, which are of paramount importance to the nature of business relationships with clients, are the foundation of the charter, namely:

- Integrity - in business relationships; of markets, financial products and services; and of staff;
- Transparency – towards clients, and regarding the regulatory environment;
- Professionalism – regarding the primacy of clients' legitimate interests and efficiency.

The Advisory panel, a multi-lateral forum on strategic Luxembourg private banking issues, also continued its efforts. The Advisory panel is headed by Mr Luc Rodesch and composed of PBGL Members, as well as Advisory partners of Luxembourg-based consultancies. Representatives from other industries have joined the Advisory panel since the beginning of 2012. Subjects covered are of strategic nature and include the execution of a Voice of the Customer study at financial centre level and the upgrading of business intelligence available at sector level.

The recommendations of the Welcome to Luxembourg taskforce, which was set up in 2010, have been further developed inside the "Haut Comité de la Place Financière" (HCPF) in which the PBGL is represented. The HCPF is directly chaired by Minister Luc Frieden and composed of high-level industry representatives. Promising legal developments are indeed on their way or have come into place. The law on Family Offices voted in December 2012, the projects on Family Foundations and the Luxembourg Trust, as well as the expatriate regime in place since end 2010 are particularly noteworthy.

As the best strategy doesn't work without making oneself heard and understood, Luxembourg private bankers continued to invest in public relations and promotion efforts during 2012. In this context, private bankers intensified their cooperation with Luxembourg for Finance (LFF), the financial centre's promotion agency, and contributed to the definition and execution of private banking promotion efforts with regards to the choice of geographies to be covered by economic missions, speakers, subjects and messages.

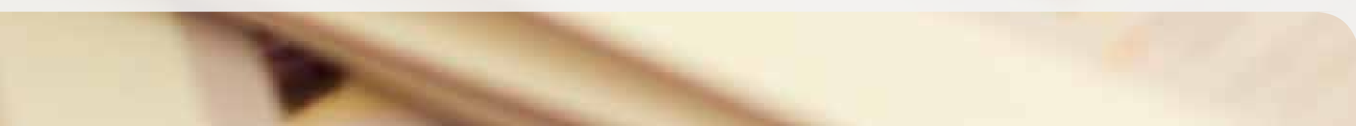
Furthermore, the PBGL was active in briefing international delegations on the state of play, strategy and current challenges to Luxembourg Wealth Management. Initiatives vis-à-vis delegations of Luxembourg Trade Investment Officers, ASEAN Ambassadors, the Moroccan financial authorities, representatives from the Strasbourg financial community and students from various universities should be mentioned in this context.

Finally, the promotional movie on Luxembourg Wealth Management including testimonials from a broad range of international wealth management clients banking in Luxembourg is now available in 10 languages. Copies of the movie are available at the ABBL Secretariat.

Getting a grip on Luxembourg private banking business intelligence continued to be a priority in 2012. In this context, the Statistics working group repeated its yearly data collection exercise in cooperation with the "Commission de Surveillance du Secteur Financier" (CSSF) and PBGL member banks. This yearly exercise is conducted in order to obtain reliable statistics on the weight of the Luxembourg private banking industry. One upgraded edition of the Luxembourg Private Banking Cockpit was furthermore published in 2012. The Luxembourg PB Cockpit is an inventory of statistics with regards to Luxembourg private banking, international

rankings, fundamental data on identified growth markets, as well as industry trends identified by local and international consultancy practices. The document is available to members only via the ABBL Secretariat.

In the area of training, the PBGL continued to invest itself in its preferred relationship with the IFBL. Over past years, the PBGL sponsored the development of an array of private banking related trainings and certifications. As such, tax planning modules focusing on Belgium and France, certifications for junior Private Bankers and Assistants are available. As a complement to vocational training initiatives conducted with the IFBL, the PBGL continued its cooperation with the University's Luxembourg School of Finance (LSF) in view of creating internationally recognized education programmes in Wealth Management. Working groups composed equally of industry representatives and academic professionals have finalised programmes design throughout 2012. Two complementary programs are to be launched during 2013. An Executive Programme in Wealth Management is launched in February 2013 and is open to experienced professionals aiming to upgrade their skill set. A Master II in Wealth Management programmes is to be launched in a full time and part time version as of September 2013. Registration to the Master II is open to international talent wishing to start a career in cross-border wealth management. The Masters programmes should contribute positively to Luxembourg's image as centre of excellence in international wealth management.



Payments

As in the previous years, during 2012 the Payments, Information Systems and Standardisation Committee (PISC) of the ABBL and its different working groups continued to deal with the many issues raised by the new legal frameworks decided at the level of the European Union.

SEPA

Throughout 2012, the achievement of SEPA remained the cornerstone of PISC's work. Especially since the entry into force of the so-called SEPA end date regulation prescribing the migration to SEPA compliant payment services for 1 February 2014, the ABBL has stepped up its efforts to help banks operating out of Luxembourg to migrate smoothly to SEPA payment instruments.

SEPA Migration Having been successfully launched on 28 January 2008, the SEPA project is about to celebrate its fifth birthday. As a reminder, in January 2008 more than 4300 banks in 31 countries representing roughly 95 percent of payment volume in Europe took a historical first step towards SEPA by launching the SEPA Credit Transfer Scheme (SCT) for euro payments.

The main challenge in 2013 will be the migration to SEPA direct debit.

On 1 February 2014, the current legacy direct debit system (DOM-2009) will stop and the only way to collect direct debit will be to use the SEPA direct debit scheme.

So, during the year 2012, the ABBL, together with banks active in the direct debit domain, have developed a migration scenario in order to simplify the migration process as much as possible for companies. With such a scenario, the migration of existing direct debit mandates will be "soft". Nevertheless, companies should of course not underestimate the impacts and the scope of the migration, which will require substantial changes to their existing systems.

In Luxembourg, banks have been ready for the migration since October 2012.

The role of the ABBL as NASO (National Adherence Support Organisation) is to coordinate the SEPA migration in Luxembourg and the challenges ahead.

The ABBL and Luxembourg banks have also communicated well with clients and companies on these issues to prepare them. A large set of document has been prepared for banks, companies and end-users in order to explain the migration and the new SEPA topics.

The ABBL is accompanying and informing companies in migrating via monthly info sessions, which were set up in different languages at the Chamber of Commerce during summer 2012 and which will continue in the first part of 2013.

SEPA Standards At the same time, the Standards working group of the PISC has developed, throughout 2012, several technical XML implementation guidelines for SCT and SDD initiations by companies; the latest being an implementation guideline for payment status reports issued by banks for the companies.

This work will continue in 2013, with other XML implementation guidelines from banks to companies, in order to be ready on 1 February 2014.

NASO activities In its role as NASO, the ABBL has also set up a process in order to generate and manage SEPA Creditor Identifiers on behalf of banks. This solution, available since July 2010, has really started to operate and to be used in 2012. With the Direct Debit migration in 2013, this activity will surely explode in the coming months.

Furthermore, as NASO, the ABBL provided support to banks and financial service providers in order to correctly fill the SDD and SCT adherence forms by the European Payments Council (EPC).

At the moment, 59 financial institutions in Luxembourg have adhered to SCT, 18 to SDD Core and 13 to SDD B2B.

Changing legal framework

In 2012, the European Commission started the revision of the Payment Service Directive, which was transposed into national law in 2009, as well as preparatory works for achieving an integrated European market for card, internet and mobile payments.

The ultimate goal set by the European Union to achieve an integrated payments market taking into account the needs of the various stakeholders is gaining momentum and new entrants are likely to be entitled to compete with banks in the payments market.

Additional challenges such as regulation on multilateral interchange fees or mandatory security levels payment instruments must reach were announced during 2012 and first consultations were finalised during the same year. First proposals of a revised legal framework should be tabled in the first half of 2013.

Security of payment systems and instruments

During 2012, the ABBL working group dealing with this issue of security of payment systems and instruments continued to monitor the various threats and attacks detected.

In general, we saw an increase of mobility of data with cloud services and BYOD (Bring Your Own

Device) providing new vectors of attack and challenging the IT and security procedures in place.

Yet the web remained the dominant source of distribution of malware (in particular malware using social engineering), but we also saw malware on smartphones that eavesdrop on incoming text messages, which means that authentication codes sent via SMS can be intercepted.

e-Invoicing

As an interested party in the e-invoicing value chain, the ABBL continued to chair the eifL (electronic invoice forum Luxembourg) in 2012, the national multi-stakeholder forum on e-invoicing, and to represent Luxembourg in the European Multi-Stakeholder Forum on e-invoicing, co-chaired by the EC DG-Internal Market and DG-Enterprise.

eifL members were essentially engaged in fact finding activities and discussed the draft bill transposing the so-called e-invoicing Directive into national law.

XBRL

As founding member of XBRL Luxembourg, the ABBL continued to monitor the use of the XBRL standard in regulatory reporting by Luxembourg banks to the CSSF and the Central bank, as well as the evolution of the reporting requirements. The ABBL closely followed various initiatives using the XBRL standard, particularly in Luxembourg and in Europe.

GLEI initiative

At the end of the year 2012, the Luxembourg Central Bank presented the GLEI (Global Legal Entity Identifier) initiative, which will lead to the implementation of a local operating unit managing the legal entity identifier database. The use of a LEI will be compulsory in April 2013 to trade in certain derivatives instruments in the USA. At the end of the day – following the decisions of the G20/FSB (Financial Stability Board) – the LEI shall be used on a global scale to identify counterparties in any kind of financial transaction.

Operational Crisis Prevention and Management

In 2012, the ABBL took an active part in the activities of the OCPG (Operational Crisis Prevention Group) and the OCMG (Operational Crisis Management Group). The ABBL liaised with the HCPN (Haut Commissariat à la Protection Nationale) and comented the draft bill submitted to Parliament in 2012, which creates a new legal framework organising Operational Crisis Prevention and Operational

Crisis Management. The financial sector is considered to be part of Luxembourg's critical infrastructures.

At the beginning of October, the ABBL monitored the second cyber security exercise organised by the European Commission. During this exercise, a cyber attack against infrastructures relevant to the financial sector was simulated. Building on the results of this test, the financial sector will be able to fine tune, together with the HCPN, its responsiveness to a large scale disruption scenario.

New ICT technologies – new opportunities

The ABBL contributed in 2012 to the review of the legal framework regulating the use of cloud computing solutions within the banking sector. One of the major outcomes is the draft bill regarding the issue of property of outsourced data and the right to access such data in case of insolvent service providers. The ABBL is also following basic research done by a PhD student at the University of Luxembourg on the legal issues raised by cloud computing.

In 2012, the ABBL continued the monitoring of the drafting of a bill on electronic archiving with value legal value, which is to be submitted to Parliament at the beginning of 2013.

This important piece of legislation will allow banks to review and improve the efficiency of their existing document management procedures. The draft bill foresees 2 new categories of PSF (Support PSF) which will allow banks to outsource these complex and expensive processes.

Finally, in 2012, the ABBL started to analyse the European Commission's proposal for a draft regulation on electronic identification and trust services for electronic transactions in the internal market, which is of high relevance to banks.

Innovation and Finance

Due to the increasing pressure resulting from regulation pushing for harmonisation of high quality payment services, a fierce competition from existing and new payment service providers, and due to the search for new revenue streams, banks have a keen interest in innovation, especially in the field of payments services based on new technologies combined with new business models. The ABBL continued to liaise with the Public Research Centre Henri Tudor and the SnT and took the lead of a LuxInnovation working group on e-payments and e-invoicing.

Employers' Representation,
Social Affairs and Human Resources

Pre-draft law on the social dialogue within companies

In April 2012 the Ministry of Labour and Employment seized the social partners with a pre-draft law on the reform of the social dialogue. After several rounds of negotiations with the social partners and two position papers by the Union des Entreprises Luxembourgeoises (UEL) the outlines of the pre-draft law in September were as follows:

- the creation of staff representatives at three different levels: at the level of the company, the economic and social entity and the establishment;
- an abolition of labour councils in companies above 150 employees and a transferral of the labour council's competencies to the staff representatives;
- an increase in the means and instruments for the staff representatives (external advisers, electronic means, increased spare time, etc);
- several changes in the protection of the staff representative.

Since September 2012, the employers' organisations have not been updated on the changes in the text.

According to the Ministry of Labour and Employment the draft law will be issued shortly and the law should be passed before the social elections of November 2013.

The Industrial Relations and Social Affairs Committee of the ABBL has created an "ad hoc working group" which will gather as soon as the draft law is passed to analyse the text.

Pre-draft law on the procedure of reintegration

At the end of August 2012, a pre-draft law was sent to the social partners on the procedure of reintegration (*procédure de reclassement*).

The main changes announced in the pre-draft law were the following:

- the abolition of quotas for employers of more than 25 workers;
- the strengthening of sanctions for employers refusing the reintegration;
- the introduction of a different procedure to seize the mixed committee (*commission mixte*) through the occupational doctor;
- the creation of a statute of an externally reintegrated worker;
- the re-evaluation of reintegrated workers by occupational doctors.

In autumn a meeting took place between the Minister of Social Security, the Minister of Labour and the employers' organisations, where the latter were very critical towards the pre-draft law.

Since that meeting in autumn, the employer's organisations have not received any news on the pre-draft law.

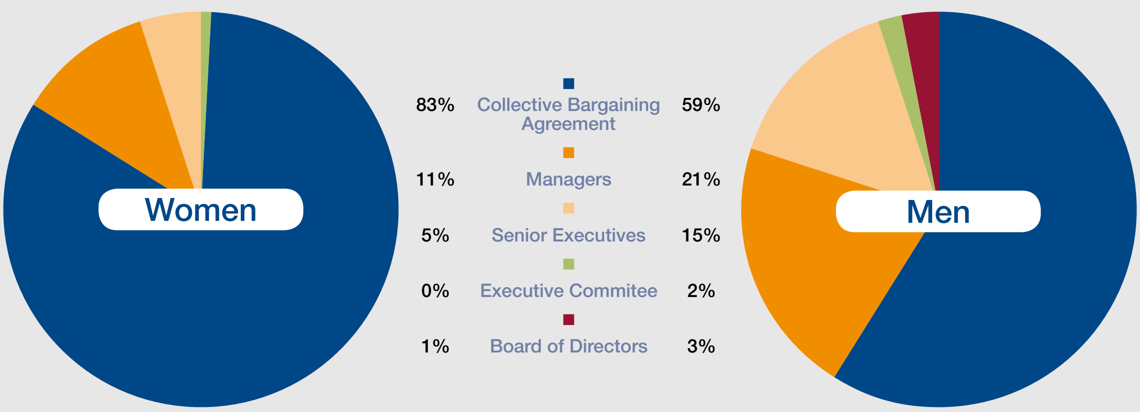
Actions in favour of diversity

In February 2012, in the presence of Minister Hetto-Gaasch, the ABBL launched its Charter in favour of diversity and equal opportunities in the financial sector.

The Charter is part of the ABBL's commitment towards Mrs Hetto-Gaasch to raise awareness on the benefits of diversity in companies as well as stimulate companies' efforts in increasing the number of women in higher positions.

The ABBL also committed itself to hold a survey amongst companies with more than 500 employees on the position of women in the financial sector.

The following figures are some of the results of this survey:



Whereas women and men are recruited almost at an equal level in the financial sector, they are more numerous under the collective bargaining agreement and their percentage diminishes rapidly from the level of managers upwards. The survey will be conducted again in 2014 in order to monitor the progress made by financial companies with regards to women's careers.

The survey shows that the financial sector is not exemplary when it comes to the issue of professional opportunities for women. It also demonstrates that a lot of efforts need to be undertaken to change mentalities and the ABBL is committed to tackling the subject, notably by creating an informal panel of exchange for diversity managers of the financial sector.

In September, the ABBL has signed a convention of cooperation with IMS, an association which published a national Charter on diversity to the attention of all sectors of the economy.

Senior workers

As a companion initiative to the pension reform, employers are urged to maintain senior workers longer in the workplace.

The topic has been on the agenda of the Permanent Labour Committee in 2011 and in 2012 and the Minister of Labour and Employment is shortly due to issue a draft law imposing an age management plan in companies above 150 employees.

In order to raise awareness on the subject of senior workers as well as on the responsibility and possibilities of employers, the ABBL, together with Fedil, organised a conference on ageing workers and the role of companies in October.

The Minister of Labour and Employment was one of the speakers of the conference, as was Dr. Geissler, a recognised expert on age management.

The practical implementation of age management within companies was illustrated by a round table assembling HR managers from industrial and financial companies, the industrial sector's health service, the IFBL as well as the association Perspective 45+.

Publication with Fedil and CLC: "Tomorrow's qualifications in the domain of information technology"

In March, the ABBL, Fedil and CLC, in partnership with the Adem, the Ministry of National Education, the Ministry of Labour and Employment and the Chamber of Commerce, have re-issued their brochure on "Tomorrow's qualifications in the domain of information technologies".

The brochure is updated on a two-year basis and attempts to evaluate companies' future needs in qualified staff in the area of information technology.

The brochure's objective is to asssist students in their professional orientation.

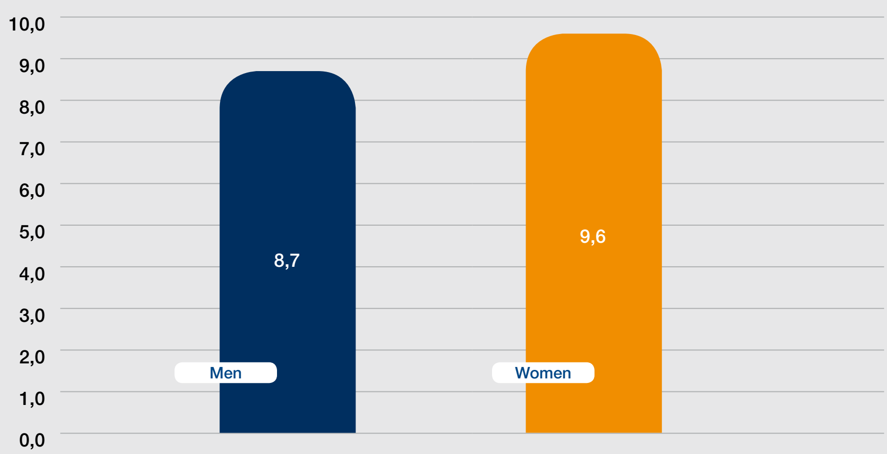
Survey on the social situation in the banking sector for the year 2011

Like every year, we collected data amongst our members on the social situation in the banking sector. This data enables us to have detailed information for the negotiation of the collective bargaining agreement starting in the year 2013.

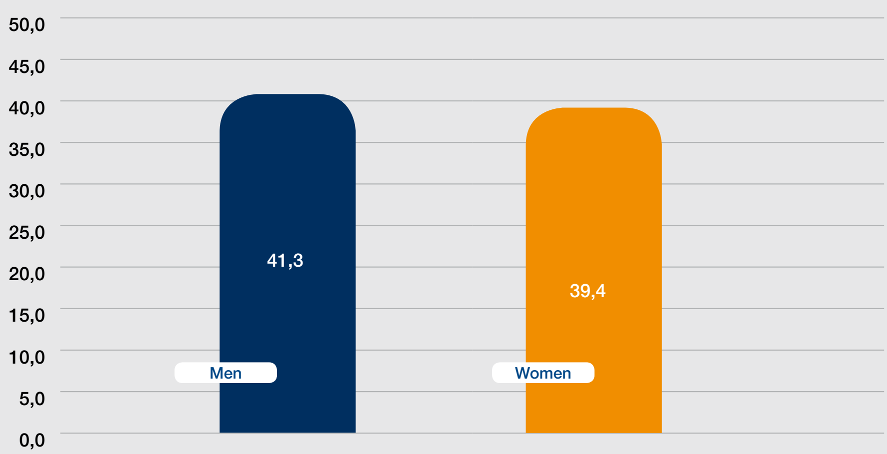
We would like to highlight the following data:

- While the participation rate decreased from 67.6% to 63.2%, this nevertheless covers 92.3% of the employees of the member banks, i.e. 21 468 people.
- The average seniority as well as the average age of all employees have increased.
- The distribution of men / women is the following: 53% men (i.e. 11 377 men) and 47% women (i.e. 10 091 women).

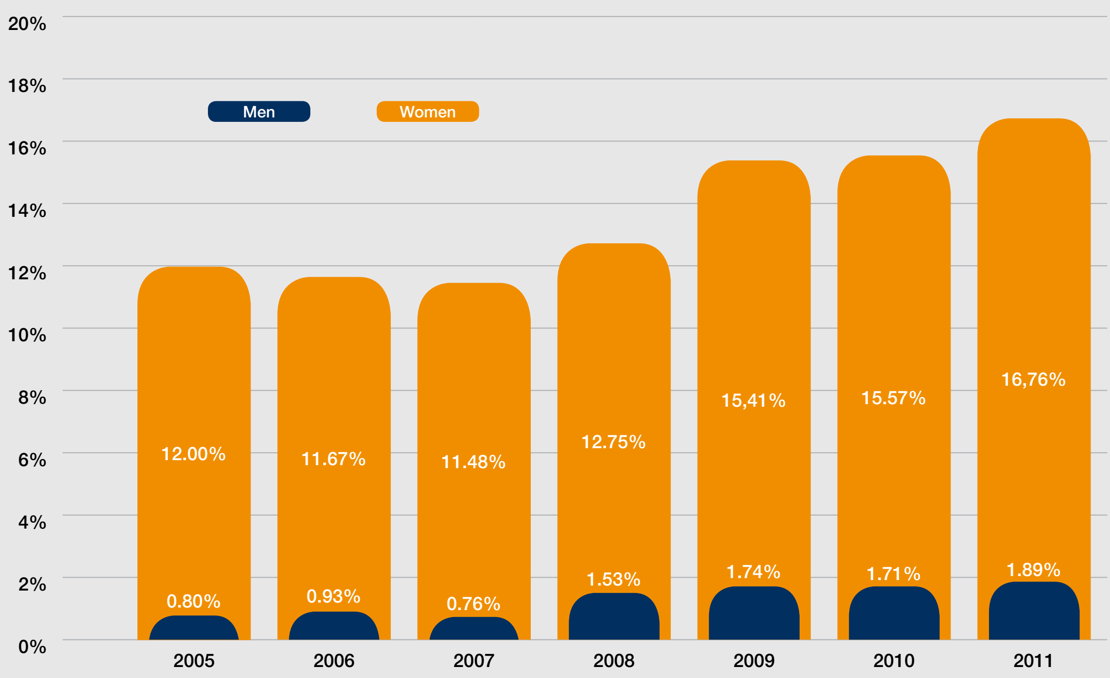
Average seniority



Average age

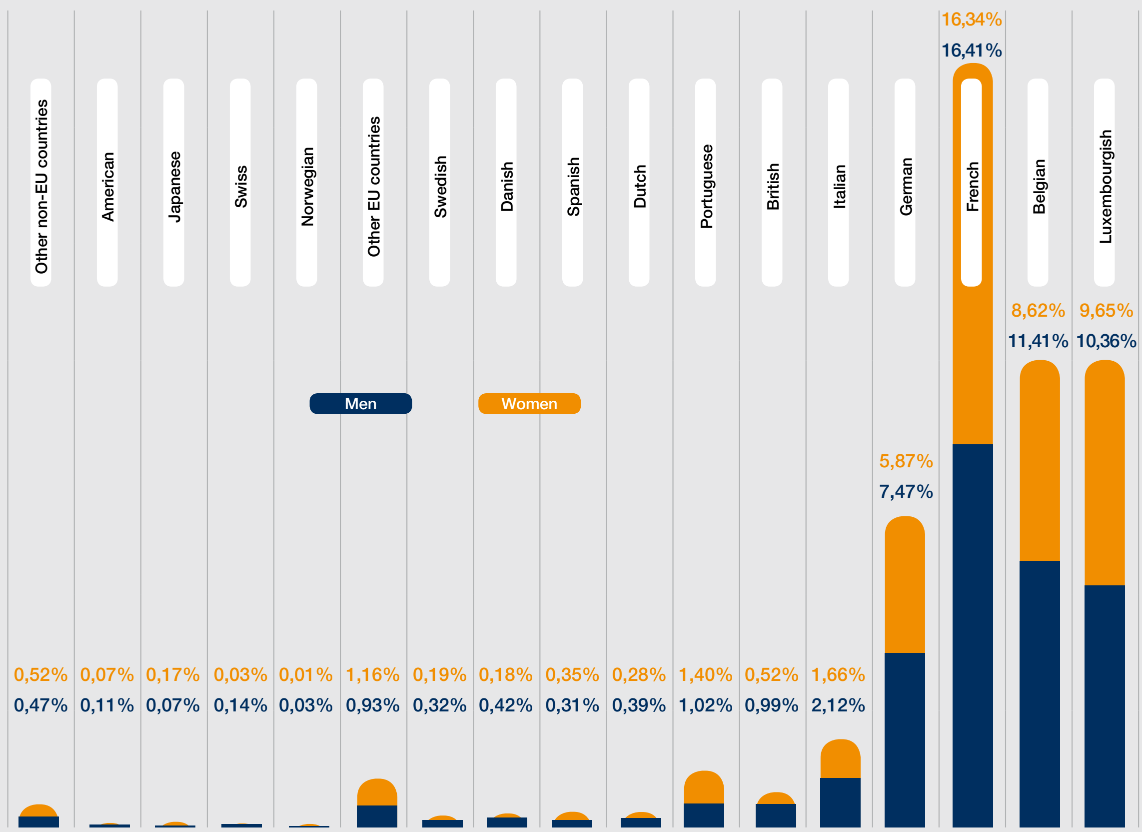


Part-time employees



- The percentage of people working part-time continues to increase slowly but steadily.

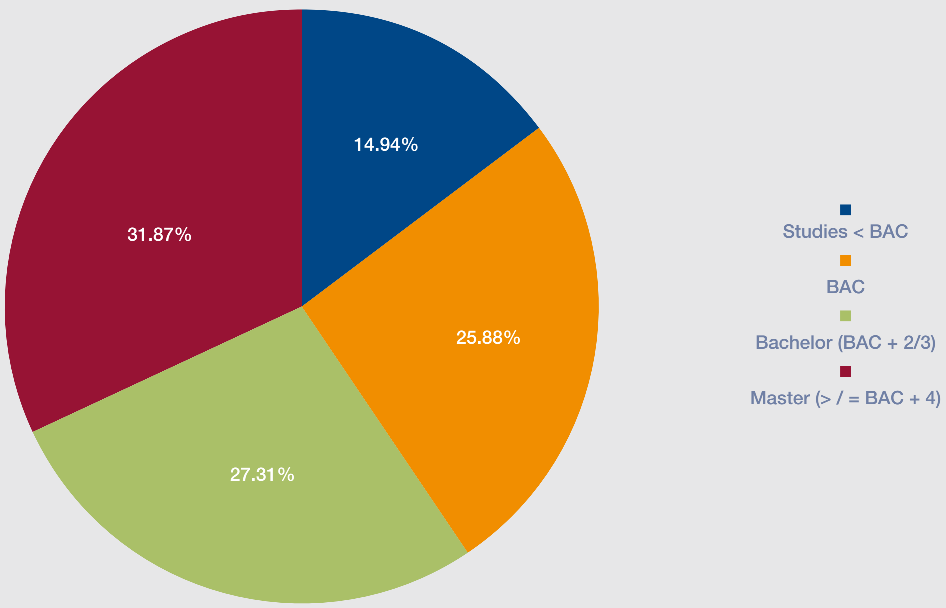
Nationality



- Among all employees the number of Germans, Belgians and Luxembourgers is decreasing while the number of French is increasing.

Regarding the distribution of employees within the duty groups of the collective bargaining agreement, it is worth mentioning that there is an increasing number of employees in groups IV to VI, whereas the population in groups I to III is diminishing.

Duty groups



Higher qualification continues to be important for the sector.

Joint Committee

The members of the Joint Committee were working on two main topics in 2012:

- Change in the regulation concerning leave for trade union purposes:

The members agreed on the principle of the extension of training according to Art. L. 415-10 of the Labour Code. Delegates may now participate not only in training courses of the EST (Ecole Supérieure du Travail) but also of the IFBL (Institut de Formation Bancaire Luxembourg) and the CFSL (Centre de Formation Syndicale Luxembourg). If the employer and the delegate decide by common agreement that a training course at the IFBL is useful, the delegate can be enrolled, subject to the acceptance of the trade unions. In this case, the enrolment costs are at the employer's charge.

- Sectoral procedure on moral harassment:

The parties are working, in collaboration with the ASTF, on a procedure on moral harassment for the financial sector; the discussions are well advanced and may conclude at the beginning of 2013.

Information will be provided as soon as an agreement has been reached by the parties.

Social Security

The ABBL, together with the other employer organisations belonging to the Luxembourg Employers' Association (UEL), is represented in the executive committees of the various tripartite social security organisations, such as health and retirement insurance schemes. It therefore bears the shared responsibility to promote constructive management and to efficiently manage the budgets financed by the joint contributions of employers, insured persons and the State.

Beyond their managerial role, employer organisations endeavour to support the government in its efforts to ensure the survival of the social security systems. It is all the more regrettable that the brave intentions of the political authorities and the minister in charge come to a halt as soon as they clash with electoral, regional or socio-professional expectations.

The budgetary forecasts for health insurance highlight a negative current account balance of EUR -7.5 million for 2013, which means that healthcare expenditure will exceed the financial year's revenue. Furthermore, multi-year estimates show that the negative trend will take hold in the coming years, even if the system is currently managing to survive thanks to its reserves.

The recent health insurance reform, adopted in 2010, was meant to raise awareness of health costs among the various stakeholders. This did not prevent the growth of spending in hospital investments or the surge of acts by healthcare providers. Expenditure dedicated to the hospital sector, the largest item, totals EUR 812.1 million (+3.5%) for 2013 and EUR 836.4 million (+3%) for 2014.

While employers welcome the fact that contribution rates remain unchanged in the context of the economic crisis, the effects of the anticipated savings in the medium and long term as a result of the health insurance reform remain elusive at this stage. Moreover, the various projects ('Agence E-santé', designated GP, hospital pooling) presented as the cornerstones of the new health insurance system prove difficult without the support of the stakeholders targeted. The solution to be avoided is having to regain financial stability by increasing contributions.

In December 2012, the pension insurance reform was adopted.

The ABBL, together with all of the employer organisations belonging to the UEL, have long insisted on a structural reform which guarantees the sustainability of the system.

Contrary to expectations, the adopted reform remains only a tentative sign of progress: it is based on somewhat unrealistic growth assumptions in terms of the economy (3%) and employment (1.5%), and alternative scenarios in case of weaker growth have simply not been considered. Moreover, the reform will only achieve its full impact as of 2052.

The lack of political drive and the desire to postpone the financing issue is justified given the current account balance and the fact that Luxembourg has succeeded, over the past 20 years, in doubling the number of jobs (and thus the number of contributors to the system) in order to fund pensions.

But sooner or later, the debate will have to be reopened. Above all, the issue of how to maintain the current level of services (which by far exceeds that of other countries) will need to be addressed, bearing in mind that Luxembourg will need over 700,000 inhabitants in 2060 and almost half a million cross-border workers (as opposed to 150,000 to date) to fund the system.

The ABBL has published an outline of the reform on its website. We also recommend reading the following publications on this topic: *A pension for everyone* or the press release *UEL launches an urgent appeal for politicians to assume their responsibilities.*

To conclude, it would appear that Luxembourg is suffering from a structural malaise in terms of its social expenditure management. Luxembourg's state budget for 2013 reflects a constantly declining social security surplus between 2008 and 2013 (EUR 647.2 million in 2013 as opposed to EUR 1,081.8 million in 2008). In light of this trend and given the political ambitions in the social sphere, the surplus will soon be depleted unless attitudes change and the focus switches to the true vocation of the social security system, i.e. covering social risks via minimum guarantees.

Communication and Corporate Secretariat

8. Events 2012

10/01/2012
Internet : The .brand and .bank Top Level Domain Issue

16/02/2012
Charter in favour of diversity in the financial sector

09/03/2012
ASTF/ABBL Conference on Burnout

20/03/2012
ABBL/FEDIL – Tomorrow's Qualifications in the ICT Sector

27/03/2012
ABBL/ALFI Walking Dinner in Brussels

26/04/2012
ABBL General Meeting

26/04/2012
ABBL Press Conference

12/06/2012
CSR 2.0 : Turn sustainability into benefits

18/06/2012
Private Banking Group Members' Meeting

03/08/2012
ABBL Summer Press Conference





28/08/2012
Information Session on SEPA Direct Debit

26/09/2012
Post-trade and T2S : Impacts for Luxembourg

27/09/2012
Information Session on SEPA Direct Debit

02/10/2012
ABBL/FEDIL Conference on Ageing Workers

04/10/2012
ABBL/PBGL and ICMA Private Banking Workshop

24/10/2012
Information Session on SEPA Direct Debit

13/11/2012
ABBL Chairman's Dinner

20/11//2012
ABBL/ACI Conference on the FTT

27/11/2012
Information Session on SEPA Direct Debit

28/11/2012
ABBL/Natural Le Coultre Conference on the Luxembourg Freeport

IFBL
L'INSTITUT

9. IFBL

In terms of man-days*, the IFBL has seen strong progress over the past three years (+31.34% between 2010 and 2012). In 2012, the figure of 13 000 man-days was exceeded for the first time ever. While this development may be explained in part by the wider, updated offer of courses, it also reflects the fact that the companies in the financial sector are conscious of the usefulness and necessity of training courses, even – and perhaps more particularly – during a crisis period.

* *One man-day corresponds to one person attending 8 hours of a course.*

A la carte sessions, certifications and customised training courses

Regarding our offer of "à la carte" sessions and certifications, the number of enrolments remained stable, on a par with the previous year's high level. Customised training courses made strong progress, however, as the Institute was asked both by companies in the financial sector and by various public bodies to devise training courses specifically addressing their requirements.

Concentration on the regulatory and prudential environment

Globally, all the training courses directly or indirectly connected with the regulatory and prudential environment of the financial sector saw noticeable progress in 2012. In the field of risk management, for example, the new professional qualification introduced in collaboration with ALRiM (Association des Professionnels du Risk Management, formerly known as PRiM) has been very well received, and more than 550 man-days of training courses were dispensed in this field in 2012. Similarly, the training courses in the field of compliance increased from 254 man-days in 2011 to 490 man-days last year. These pragmatic training courses, organised in collaboration with ALCO (Association Luxembourgeoise des Compliance Officers), cover every aspect of the job, taking local and international requirements into account. In 2012, 33 candidates were awarded the Certificate of Competency in the Field of Compliance after passing the examinations for the three modules of the training course and the assessment before a panel of qualified Compliance Officers of the financial centre.

Still in the field of understanding risks and responsible management, the IFBL introduced a new training course in 2012 based on the lessons to be drawn from the crisis. Entitled Capital Markets Crisis Management Initiative, this training, organised in collaboration with ICMA - Luxembourg Region, was fully booked as soon as it was launched, in December. It is directed at both trading room staff and internal auditors and Risk Managers with a good knowledge of financial products.

Insurance

In the insurance field, a new training course was set up as part of the IFBL's collaboration with ACA (Association des Compagnies d'Assurances de Luxembourg), on Freedom to Provide Services (FPS) in insurance. This pragmatic training course is intended for anyone carrying out cross-border insurance activities. Since 2012, the IFBL also offers sessions to prepare for the examination prescribed for anyone wishing to obtain approval as an insurance agent or sub-broker in the Grand Duchy of Luxembourg. Globally, 537 man-days were dispensed as part of this offer extended into the insurance field, compared with 132 in 2011.

Investment funds

With regard to fund training, developed in collaboration with ALFI, the environment was also one of significant change. The full range of courses was rigorously kept up to date in 2012, notably to incorporate the changes introduced by the law of 6 March 2012 concerning specialised investment funds subject to the law of 13 February 2007 and to keep the growing range of alternative fund courses in step with the developments regarding the AIFM directive. The progressive market shift from "low touch" to specialist processing activities and to high value added management tasks continued. Developments in this respect provided the opportunity to revise and re-align a number of legally orientated courses. This latter trend and the implementation in 2013 of a number of pieces of regulation (eg. AIFMD) will provide further significant development opportunities.

The "Career and personal development" sector

In addition to its offer of training courses, the IFBL has extended the breadth of its services by publishing for the first time a catalogue entirely devoted to all the measures and tools proposed in the area of "career and personal development". With the aim of providing assistance to both companies in the financial sector and public bodies and private individuals in their efforts regarding employment, the Institute has created a range of programmes, measures and tools both up- and downstream of its training courses that constitute a worthwhile supplement to the courses. There are three objectives for this new area of activity: accompanying and supporting individuals in their professional careers right from the time they enter the employment market, assisting employers – particularly our members – in accompanying and supporting their employees in their careers, and participating in social actions as part of the national effort to combat unemployment.

10. Luxembourg for Finance

The business environment in 2012 was challenging. Poor economic growth in the developed countries, combined with a slowdown in the emerging markets, notably China, eroded the attraction of Europe as an investment destination. Meanwhile the financial sector was subjected to a continuing hailstorm of bad press, some of which (in the tax transparency sphere) targeted Luxembourg.

One positive outcome was the creation of the European Financial Centres Roundtable, bringing together the financial centres of Luxembourg (represented by LFF), Paris, London, Frankfurt, Munich, Madrid, Scotland and Amsterdam (the last as an observer) in order to promote European financial services to the rest of the world. In September, the association organised its first conference in Brussels under the presidency of Michel Barnier, European Commissioner, Internal markets and services. LFF also held three bilateral seminars, in Berlin, featuring a debate between the respective Ministers of Finance Dr Wolfgang Schäuble and Luc Frieden; with the City of London, where Minister Frieden spoke of the importance of sustainable finance; and with Paris Europlace, where the focus was on a return to growth and funding the European economy. In November, LFF was the only non-UK city with a promotional stand at the Financial Times Global Summit on International Financial Centres, where Minister Frieden gave the opening speech.

During 2012 the partners in LFF decided to focus on three geographical areas where existing business links offer the opportunity for expansion: Asia, Latin America and the Middle East.

In Asia, attention focused on China. With Bank of China and ICBC already present in Luxembourg, and an announcement of similar plans by CCB, Luxembourg is well positioned to take a share of the emerging renminbi market. In January 2013, for the third year running, LFF took a stand at the Asian Financial forum in Hong Kong.

The focus in the Middle East fell on Dubai and Qatar. A cooperation agreement with the Dubai International Financial Centre (DIFC) exists since 2010 and a joint seminar was held by LFF and the DIFC in 2012. A joint financial seminar was also held in Qatar, where an MoU exists since 2011.

In Latin America, the financial centre has strong ties with Chile but is relatively unknown in Brazil and Mexico. The unwinding of foreign investment restrictions and strong economic growth, driving the creation of private fortunes, make these two markets a priority for Luxembourg - and its competitors. In 2012, the agency organised a series of financial seminars with ProMexico in Mexico City and with Brazil Investment and business (BRAiN) in Sao Paulo and Rio de Janeiro.

In recent years, the agency has also signed co-operation agreements with the Financial Agency of the City of Moscow (2010) and Qatar Financial Centre Authority (2011). During the year under review, two further MoUs were signed with the Central bank of Kazakhstan and the Moroccan Financial Board at Casablanca. A financial delegation from Morocco visited Luxembourg in November.

Closer to home, LFF continued to organise financial seminars in European financial centres in cooperation with local professional associations, providing delegates with an update on products and services and an opportunity for networking.

At the product level, LFF took part in the first ACG European Capital Tour organised by the US Association for Corporate Growth, to promote Luxembourg venture capital vehicles. LFF likewise took part in Expo Real in Munich (real estate investment vehicles), the GAIM conference in Monaco (alternative investment funds), the European Captive Forum in Luxembourg (captive reinsurance) and the London "City Week" forum.

Islamic finance continued to be a particular focus. Financial seminars in Doha and Dubai were followed by meetings with key banks. LFF took a stand at the IFN Asia Forum in Kuala Lumpur and, for the third year, at the World Islamic Banking Conference in Bahrain. Opportunities to write articles, speak at conference and meet business prospects cropped up throughout the year. Meanwhile, the backlog of projects began to unwind, with several innovative product launches. 2012 saw the founding of the Islamic Finance Professionals' Association (IFPA) and continued participation in Islamic finance diploma courses run by the banking training institute, IFBL, and the Luxembourg School of Finance.

A major project in 2012 was the redesign of the LFF website, reflecting a more client-focused logic and a new corporate look. Technical changes include online registration for LFF events, podcasts and a new URL - www.luxembourgforfinance.lu (formerly "lff") - to assist search engines and increase awareness. The new design facilitates the use of social media (LinkedIn, Facebook, Xing, Viadeo and Twitter), enabling LFF to increase its social network and engage with a wide circle of correspondents of all ages.

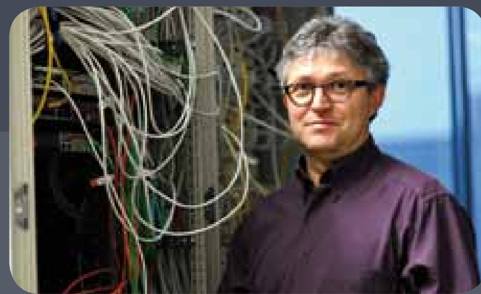
At the same time, LFF redesigned and updated all its publications, issuing the general brochure in seven languages. New technical brochures were produced on Luxembourg Life Assurance and the SOPARFI and the technical guides entitled “How to set up …” extended to include Professionals of the Financial Sector (PSF status). In addition to the quarterly LFF newsletter, three special edition newsletters (Asia, Latin America and Islamic Finance) were produced to accompany promotional events.

LFF actively supported LuxFLAG, the responsible investment fund labelling agency, and the ALFI Responsible Investing working group.

Looking back over its first five years of activity, LFF has succeeded in positioning Luxembourg as an innovative and professional financial centre and itself as a privileged and energetic partner in the development of new business. The agency is widely recognised as an authentic voice of the financial centre.

Much work lies ahead, including the need to position Luxembourg to make the most of the AIF passport, renminbi trading, portable personal pensions, responsible investment (impact investing, microfinance and social investment companies) and widening activity in the Islamic finance sphere. Challenges will include the need to manage expectations and concerns as upcoming legislation drives changes that may not be visible to us now.

Support Services



11. Membership of the Board of Directors (as at 31 December 2012)

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Vice-Chairman

Carlo THILL BGL BNP Paribas

Elected members

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Rima ADAS	PricewaterhouseCoopers
Gerard-Jan BAIS	Erste Europäische Pfandbrief- und Kommunalkreditbank
Michel BIREL	Banque et Caisse d'Epargne de l'Etat
Angelo BRIZI	UniCredit Luxembourg (until 27 September 2012)
Sébastien DANLOY	RBC Investor Services Bank (as of 27 September 2012)
Chris EDGE	J.P. Morgan Bank Luxembourg
Jean-Marc FANDEL	CETREL
Falk FISCHER	Commerzbank International
Frédéric GENET	Société Générale Bank & Trust
André MARC	Allen & Overy Luxembourg
Eric MARTIN	BGL BNP Paribas
Bernard MOMMENS	Banque Internationale à Luxembourg (until 27 September 2012)
Jhon MORTENSEN	Nordea Bank
René MOTTAS	UBS (Luxembourg)
François PAULY	Banque Internationale à Luxembourg
Jacques PETERS	KBL European Private Bankers
Fouad E. RATHLE	Garanti Bank
Robert SCHARFE	Bourse de Luxembourg
Hajime USUKI	Nomura Bank (Luxembourg)
Rik VANDENBERGHE	ING Luxembourg

Co-opted members

On behalf of the ABBL/ALFI Depositary Bank Forum

Martin F. DOBBINS State Street Bank Luxembourg

On behalf of the ABBL Retail and Commercial Banking Group

Benoît HOLZEM Banque Internationale à Luxembourg (until 23 November 2012)

On behalf of the ABBL Private Banking Group

Luc RODESCH Banque de Luxembourg

On behalf of Clearstream Banking

Jeffrey TESSLER

IFBL representative

Fouad E. RATHLE Garanti Bank

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