Banking Regulation 2025

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Introduction

As a leading financial centre in the European Union (the **EU**), Luxembourg offers a diverse range of financial services that connect investors and markets around the world. Luxembourg is a cross-border centre in banking, being home to 117 international banks from 24 different countries as at 17 May 2024 providing direct jobs to more than 26,000 people. In the September 2024 Global Financial Centres Index, Luxembourg was ranked as having the 19th most competitive financial centre in the world. With approximately a quarter of Luxembourg's economy depending on financial services, the significance of the financial sector also results in the development of financial regulation being an important policy consideration for the Luxembourg legislator.

Geopolitical impact on banking sector

Geopolitical risks pose significant challenges to the banking sector, with the Russian invasion of Ukraine and ongoing conflicts in the Middle East raising concerns over financial stability.

Additionally, the lack of notable progress in addressing energy and climate change issues, coupled with the rise of nationalism and struggles with cross-border cooperation, led to geopolitical tensions and caused volatility in currency exchange rates, interest rates, and stock prices. It is important to note that the European Central Bank (the **ECB**) has identified strengthening resilience to immediate macro-financial and geopolitical shocks as a top priority for 2024–2026. It shows the importance of the financial sector remaining stable and robust against economic and political distributions.

Amid geopolitical instability, the EU and Luxembourg have implemented regulatory measures to mitigate economic risks. Political conflicts have significantly impacted cross-border investments and cooperation. Despite these challenges, Luxembourg ranks second in cross-border investment services and hosts 15% of the EU's cross-border investment firms. Many banks in Luxembourg have demonstrated financial resilience, achieving a record €3.1 billion in profit before provisions and taxes in the second quarter of 2024 – double the quarterly average from 2008 to 2021. This underscores Luxembourg's resilience in the face of ESG compliance regulations, geopolitical instability, and inflation.

Recent trends relating to digitalisation

The Luxembourg legislator's positive take on digital development has led to recent national legislative initiatives relating to the use of digital innovations in the financial sector. It is worth noting that in line with the positioning of Luxembourg as a Fintech hub and in order to face the challenges of technological innovation in the financial sector, the financial sector supervisory commission (*Commission de Surveillance du Secteur Financier*, the **CSSF**) has created an Innovation Hub, a dedicated point of contact for any person wishing to present an innovative project or to exchange views on the major challenges faced in relation to financial innovation in Luxembourg. In this context, the CSSF collects guidance and publications on a national and international level related to specific areas of Fintech, such as virtual assets, artificial intelligence (**AI**), robo-advice and crowdfunding. As a result of the Innovation Hub, the CSSF is in permanent contact with the Fintech industry as it is open to consultation regarding the development of the regulatory framework as well as the application of regulation to potential projects. The Digital Operational Resilience Act (**DORA**), which has applied since 17 January 2025 and is a new EU regulatory framework in the financial sector, imposes obligations on financial entities with the aim of better managing ICT risks and strengthening cybersecurity resilience. DORA brings harmonisation of the rules relating to operational resilience for the financial sector applying to 20 different types of financial entities and ICT third-party service providers. In Luxembourg, the CSSF and the insurance commission (the CAA, as defined below) will be responsible for ensuring that financial entities under their supervision comply with DORA and will have supervisory and enforcement powers.

Sustainable finance driving change in the financial sector

The banking sector plays a crucial role in sustainable finance. The recent adoption by the European Commission of delegated acts under the Taxonomy Regulation (as defined below) laying down technical screening criteria for determining whether an economic activity qualifies as environmentally sustainable, as well as the upcoming launch by the European Securities and Markets Authority (**ESMA**) of a Common Supervisory Action (**CSA**) on the integration of clients' sustainability preferences into suitability assessments and of sustainability objectives into product governance under MiFID II (as defined below), demonstrate the EU's emphasis on sustainable finance in addition to the global growing sustainability concerns and transition of the financial sector towards sustainability. The European Green Bond Standard (Regulation (EU) 2023/2631) entered into force on 20 December 2023, and its provisions apply from 21 December 2024. This regulation marks a significant milestone in the EU's efforts to promote sustainable finance by providing a clear and robust framework for bond issuers. It applies to all types of bond issuers, including public and private issuers, and provides them with a voluntary standard.

On 1 January 2024, the Corporate Sustainability Reporting Directive (the **CSRD**) and the European Reporting Directive (the **ESRS**) came into force. Publication of the first sustainability reports in accordance with the CSRD is foreseen in 2025. The directive is designed to enhance the evaluation and measurement of an entity's sustainability performance, reflecting how effectively it incorporates environmental, social, and economic factors into its operations to ensure long-term sustainability and to mitigate adverse effects on the environment, society, and the economy.

Being home to the Luxembourg Green Exchange, the world's first dedicated and leading platform for green, social and sustainable securities launched in 2016, and having the largest market share of listed green bonds worldwide, Luxembourg is a leading green finance centre, as confirmed by the last edition of the Global Green Finance Index published in October 2024, which ranked Luxembourg in second place in the EU and eight place globally.

Regulatory architecture: Overview of banking regulators and key regulations

National level

The national authorities responsible for the regulation and supervision of the banking sector in Luxembourg are the CSSF and the Central Bank of Luxembourg (the **BCL**), which are placed under the authority of the Ministry of Finance.

The CSSF

The CSSF is the authority responsible for the prudential supervision of the Luxembourg financial sector. Since 30 July 2021 and the entry into force of the so-called "Authorisation Law" of 21 July 2021, the CSSF is solely competent for granting, refusing and withdrawing authorisations of certain entities placed under its supervision (being, among others, mortgage credit intermediaries, credit institutions, investment firms, specialised professionals of the financial sector, support professionals of the financial sector, payment institutions and electronic money institutions, branches of foreign professionals of the financial sector other than investment firms, branches of third-country credit institutions, and third-country firms providing investment services or performing investment activities). Before the entry into force of the aforementioned Law, the granting, refusing and withdrawing authorisation for such authorised institutions was under the authority of the Ministry of Finance. The shifting of such competences reflects the evolution of the EU laws increasingly advocating the allocation of powers of approval to the national competent authorities in charge of prudential supervision. Further, the CSSF is the (i) national resolution authority for the resolution of credit institutions and certain investment firms in the framework of the Single Resolution Mechanism and the Single Resolution Fund under EU Regulation 2014/806 of 15 July 2014 establishing uniform rules and a uniform procedure for the resolution of credit institutions and certain investment firms in the framework of a Single Resolution Mechanism and a Single Resolution Fund and amending EU Regulation 2010/1093 of 24 November 2010, and (ii) resolution authority of failing national or transnational banks with the view to limiting their systemic impact as provided by the law of 18 December 2015 on the failure of credit institutions and certain investment firms (transposing EU Directive 2014/59 of 15 May 2014 establishing a framework for the recovery and resolution of credit institutions and investment firms, as amended by Directive (EU) 2019/879 of 20 May 2019 as regards the loss-absorbing and recapitalisation capacity of credit institutions and investment firms and Directive 98/26/EC (the **BRRD Package**)).

Further, the CSSF is the competent authority for the application of Regulation (EU) 2017/1129 of the European Parliament and of the Council of 14 June 2017 on the prospectus to be published when securities are offered to the public or admitted to trading on a regulated market, and repealing Directive 2003/71/EC (**Prospectus Regulation (EU) 2017/1129**) and the law of 16 July 2019 on prospectuses for securities that implements certain provisions of Prospectus Regulation (EU) 2017/1129, and provides for other requirements covering the national prospectus regime.

Its field of competence also encompasses the control of professional obligations regarding anti-money laundering and combatting the financing of terrorism (**AML/CFT**).

The CSSF is also in charge of the supervision of markets in financial instruments and their operators.

The BCL

The BCL is part of the European System of Central Banks and is specifically responsible for, *inter alia*: (i) the supervision of liquidity of credit institutions, in cooperation with the CSSF; (ii) control over the smoothness and efficiency of payments systems; (iii) the empowerment of financial stability; and (iv) the implementation of monetary policies.

The CAA

Credit institutions that are authorised to pursue insurance-related activities are also supervised for such

activities by the *Commissariat aux Assurances* (the **CAA**), the authority that regulates and supervises the insurance, insurance mediation, reinsurance and management of complementary pension funds activities.

The influence of supra-national regulatory regimes or regulatory bodies

EU level

As part of the European Banking Union, the Luxembourg banking system is subject to the supervision of the ECB within the framework of the European Single Supervisory Mechanism (the **SSM**). The ECB is specifically responsible for: (i) granting and withdrawing banking licences; (ii) assessing banks' acquisitions and disposals of qualifying holdings; (iii) ensuring compliance with EU prudential and governance requirements; (iv) conducting supervisory reviews, on-site inspections and investigations; and (v) setting higher capital requirements ("buffers") in order to counter any financial risks.

Since November 2014, the ECB is exclusively competent for granting licences, approvals of qualifying holdings and appointment of key function holders in all significant credit institutions, established in the Member States participating in the SSM. The ECB's role in such significant credit institutions includes the supervision of solvency, liquidity and internal governance.

It is worth noting that the supervision of less-significant institutions incorporated under Luxembourg law and branches of non-EU institutions remains under the scope of competence of the CSSF. Further, the CSSF remains the main authority for the supervision of, among others, (i) compliance with professional obligations regarding AML/CFT, and (ii) regulations for consumer protection.

The key legislation and regulation applicable to banks in Luxembourg

The principal rules and regulations applicable to the financial and banking sector are embodied in the law of 5 April 1993 on the financial sector, as amended (the **LFS**), which implements, among others, EU Directive 2013/36 of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms (**CRD IV**), as amended by Directive (EU) 2019/878 of 20 May 2019 as regards exempted entities, financial holding companies, mixed financial holding companies, remuneration, supervisory measures and powers and capital conservation measures as amended by Directive (EU) 2021/338 (**CRD V**). Notably, the LFS regulates: (i) authorisation of credit institutions and access to professional activities in the financial sector; (ii) professional obligations, prudential rules and rules of conduct; (iii) prudential supervision of the financial sector; (iv) prudential rules and obligations in relation to recovery planning, intra-group financial support and early intervention; and (v) the power of the CSSF to impose fines and sanctions.

Directive (EU) 2024/1619 (**CRD VI**), which came into force on 9 July 2024, further harmonises the requirements for providing banking services to European Economic Area (**EEA**) clients and counterparties by third-country banks, including in particular the requirement to establish a branch within an EU Member State in which they provide certain core banking services. EU Member States are required to transpose CRD VI into national law by January 2026, followed by an additional 12-month transition phase, with the final compliance date being in January 2027. In addition, Regulation (EU) 2024/1623 of 31 May 2024, amending Regulation (EU) 575/2013 as regards requirements for credit risk, credit valuation adjustment risk, operational risk, market risk and the output floor (**CRR III**), has applied since 1 January 2025.

Further, the Directive of the European Parliament and of the Council on the mechanisms to be put in place by Member States for the prevention of the use of the financial system for the purposes of money laundering or terrorist financing and repealing Directive (EU) 2015/849 (**AMLD6**) was published on 19 June 2024, and entered into force on the 20th day following its publication; however, Member States have three years to transpose AMLD6 into their national legislation, as further described below.

In addition to the LFS, the main laws and regulations that govern banking activities in Luxembourg include the following:

- the law of 20 May 2021 transposing CRD V (the **CRD V Law**) and amending, among others, the LFS;
- EU Regulation 2013/575 of 26 June 2013 on prudential requirements for credit institutions and investment firms as amended by EU Regulation 2019/876 of May 2019 (**CRR II**, together with CRD V commonly referred to as the **CRD V Package**);
- EU Regulation 2019/2088 of 27 November 2019 on sustainability-related disclosures in the financial services sector (the **SFDR**);
- EU Regulation 2020/852 of 18 June 2020 on the establishment of a framework to facilitate sustainable investment, and amending EU Regulation 2019/2088 (the **Taxonomy Regulation**);
- the law of 30 May 2018 on markets in financial instruments transposing, among others, the MiFID Framework (as defined below) (the **MiFID Law**);
- the law of 18 December 2015 on the resolution, reorganisation and winding-up measures of credit institutions and certain investment firms and on deposit guarantee and investor compensation schemes implementing the BRRD Package, as amended;
- the law of 8 December 2021 on the issuance of covered bonds, which, among other things, (i) transposed EU Directive 2019/2162 of 27 November 2019 on the issue of covered bonds and the public supervision of covered bonds amending Directives 2009/65/EC and 2014/59/EU, and (ii) implemented EU Regulation 2019/2160 of 27 November 2019 amending EU Regulation 575/2013 as regards exposures in the form of covered bonds;
- the law of 10 November 2009 on payment services, as amended;
- the law of 12 November 2004 on the fight against money laundering and terrorist financing, as amended (the **AML/CFT Law**), which implemented the latest provisions introduced by Directive (EU) 2015/849 of 20 May 2015 and Directive (EU) 2018/843 of 30 May 2018 (commonly referred to, respectively, as the Fourth and Fifth AML Directives);
- the law of 23 December 1998 establishing the CSSF;
- the law of 17 June 1992 on annual and consolidated accounts of credit institutions, as amended; and
- the law of 30 March 2022 on inactive accounts, inactive safe deposit boxes and unclaimed life insurance contracts.

Further, being a member of the Eurozone, regulation of the banking sector in Luxembourg is also subject to specific pieces of Eurozone legislation, including regulations and directives transposed into national law and guidelines provided by the European Banking Authority (the **EBA**). In this respect, EBA Guidelines EB/GL/2015/20, to be read in conjunction with CSSF Circular 16/647, on limits on exposure to shadow banking entities that carry out bank-like activities outside a regulated framework (and developed in accordance with article 395(2) of the CRR), should be mentioned. The EBA Guidelines apply to all institutions subject to part four (Large Exposures) of the CRR, which shall comply with the aggregate exposure limits or tighter individual limits set on exposures to shadow banking entities carrying out banking activities outside a regulated framework (including special-purpose vehicles engaged in securitisation transactions).

From the international level, Luxembourg is influenced by supra-national regulatory regimes and regulatory bodies. Moreover, Luxembourg is a Member State of (i) the Organisation for Economic Co-operation and Development (the **OECD**), establishing norms and better policies for a wide range of subjects, such as corruption and tax avoidance, and (ii) the Financial Action Task Force, which sets standards and recommendations and promotes effective implementation of legal, regulatory and operational measures for the fight against money laundering and terrorist financing (**ML/TF**).

In addition, the CSSF is one of the bank supervisors that are members of the Basel Committee on Banking Supervision, the primary global standard-setter for the prudential regulation of banks.

The European Commission, the ECB and the OECD are members of the Financial Stability Board (the **FSB**), which is an international organisation that monitors and makes recommendations for the global financial system and has a direct impact on domestic banking legislation.

Finally, the Luxembourg regulatory framework applicable to banks is complemented by Grand Ducal regulations, Ministerial regulations and CSSF regulations and circulars issued by the CSSF on various matters related to the financial sector with a view to providing more guidance on how legal provisions should be applied and issuing recommendations on conducting business in the financial sector. Of particular relevance is CSSF Circular 12/552 on the central administration, internal governance and risk management of banks and professionals performing lending operations, as amended.

Recent and proposed changes to the regulatory architecture in Luxembourg

Recent changes to the regulatory architecture

It is worth noting that changes to the regulatory architecture are mainly driven by initiatives taken at the EU and international levels. The following is an overview of the most recent changes affecting the banking regulatory architecture in Luxembourg.

Sustainability-related disclosures in the financial services sector

Commission Delegated Regulation (EU) 2022/1288 of 6 April 2022, supplementing the SFDR with regard to regulatory technical standards clarifying the content and presentation of sustainability-related disclosures in the financial services sector, has been adopted and applied as from 1 January 2023. Accordingly, banks that provide portfolio management shall make a statement that they consider principal adverse impacts (**PAIs**) of their investment decisions on sustainability factors and describe both the relevant PAIs together with the policies on the basis of which the identification of such PAIs is effected. In addition, banks that provide investment advice shall explain in their PAI statement, which is to be published on their website, whether they rank and select financial products on the basis of the PAI indicators, including how they use the information made available by financial market participants as well as any other criteria that are used to select, or advise on, financial products. In the context of the Taxonomy Regulation (as defined below), which establishes six environmental objectives, the European Commission has to provide lists of environmentally sustainable activities by defining technical screening criteria for each environmental objective through delegated acts. To that end, Commission Delegated Regulation (EU) 2023/2485 of 27 June 2023 amending Delegated Regulation (EU) 2021/2139 has been adopted, establishing additional technical screening criteria for determining whether an economic activity qualifies as contributing substantially to climate change mitigation or climate change adaptation. In addition, on the same day, Commission Delegated Regulation (EU) 2023/2486 was adopted, laying down technical screening criteria for economic activities that make a substantial contribution to the remaining four environmental objectives, namely circular economy, water and marine resources, pollution prevention and control, and biodiversity and ecosystems. From 1 January, the banks are required to disclose their exposures to Taxonomy-non-eligible and Taxonomy-eligible economic activities pursuant to the adopted texts.

On 23 October 2023, the European Council adopted a regulation establishing European green bond standards and optional disclosures for bonds marketed as environmentally sustainable and for sustainability-linked bonds, laying down uniform requirements for issuers of bonds that fund environmentally sustainable projects aligned with the EU Taxonomy (the **EuGB Regulation**). The EuGB Regulation entered into force at the end of November 2023 and became applicable from December 2024. Accordingly, an issuing bank can benefit from the designation "European green bond" or "EuGB" for its environmentally sustainable bond provided that it allocates the proceeds of such bond to eligible assets or expenditure. In addition, to avoid greenwashing in the green bonds market in general, the regulation also provides for some voluntary disclosure requirements for other environmentally sustainable bonds

and sustainability-linked bonds issued in the EU. With the same purpose of fostering transparency in the green market, in July 2023, ESMA issued a public statement on the sustainability disclosure expected to be included in both equity and non-equity prospectuses pursuant to the Prospectus Regulation. Among other things, ESMA recommends that issuers include statements according to which the issuer or security adheres to a specific market standard or label with a view to ensuring that the information contained in prospectuses is as objective as possible.

In July 2024, the EU's Corporate Sustainability Due Diligence Directive (the **CSDDD**) entered into force. The aim of the CSDDD is to foster sustainable and responsible corporate behaviour and to anchor human rights and environmental considerations in companies' operations and corporate governance. The new rules ensure that companies respect human rights and the environment, including in their value chains inside and outside Europe. The CSDDD applies to large EU companies meeting certain thresholds in terms of number of employees and worldwide turnover and third-country companies active in the EU. It also imposes duties for the directors of the in-scope EU companies.

In March 2024, CSSF published a list of priorities in the area of sustainable finance. The integration of sustainability and adequate consideration of sustainability risks as key drivers of financial strategies has been identified as a long-term objective. Some supervisory priorities that the CSSF has specified with respect to credit institutions are transparency and disclosures, risk management and governance and MiFID rules related to sustainability. The CSSF will continue to supervise the financial disclosure that falls under the SFDR, as amended, together with CSSF Circular 22/821. Climate-related and environmental risk integration and mitigation will remain one of the priorities for the banking sector, as per the SSM's supervisory priorities for 2023–2025. In this respect, as from 2024, the CSSF intends to develop and carry out on-site inspections specifically focused on climate-related and environmental risks. In relation to MiFID, the CSSF will also keep conducting on-site inspections covering sustainability-related obligations in the areas of product governance, suitability assessments, conflicts of interest, information to clients and internal control functions.

Through the law of 15 July 2024, the Grand Duchy of Luxembourg implemented the NPL Directive aimed at regulating the sale, purchase, and servicing of non-performing loans (**NPLs**) originated by EU banks. The law introduced certain amendments to the Financial Sector Law (the **FSL**), the Consumer Code, the law of 23 December 1998 on the financial sector supervisory commission, the law of 22 March 2004 on securitisation, and the Resolution Law.

Regulatory developments relating to crowdfunding

Regulation (EU) 2020/1503 of 7 October 2020 on European crowdfunding service providers for business and amending Regulation (EU) 2017/1129 and Directive (EU) 2019/1937 (the **Crowdfunding Regulation**) entered into force on 10 November 2021. The Crowdfunding Regulation was incorporated into national law by the law of 25 February 2022, which entered into force on 8 March 2022. As stipulated by the Crowdfunding Regulation, the EBA developed draft Regulatory Technical Standards (the **RTS**) specifying, *inter alia*, the information to be considered by crowdfunding service providers when conducting the creditworthiness assessment of project owners and crowdfunding projects. Since November 2021, crowdfunding services have been subject to obtaining a licence as a European Crowdfunding Provider (**ECPS**) and fall under the supervision of the CSSF.

In May 2023, the European Commission proposed a substantial amendment to the RTS according to which personal data included in the creditworthiness assessment of perspective project owners could be kept for up to, instead of at least, five years following the loan repayment. Although the EBA accepted the amendment to the RTS, it noted the importance of enabling crowdfunding providers to improve their methods of credit risk assessment and loan valuation by gaining access to historical data, thus driving the development of the crowdfunding industry.

Proposed changes to the regulatory architecture

In May 2024, a new Bill of Law 8387 was submitted to the Luxembourg Parliament that aims to amend several pieces of Luxembourg legislation and implement recent regulations concerning crypto-assets, long-term investment funds, and European green bonds. Among these regulations, the bill seeks to implement MiCAR (as defined below) and designate the CSSF as a supervisory authority. It also defines the Luxembourg transitional regime, allowing virtual asset providers (**VASPs**) to convert to crypto-asset service provider (**CASP**) status within an 18-month period. Overall, the bill provides legal certainty regarding crypto-assets, issuers, and service providers and serves as a global benchmark for crypto regulation. The aforementioned bill is currently under discussion in Parliament.

Additionally, Bill 8370 was submitted to the Luxembourg Parliament in March 2024, with the purpose of implementing the CSRD into Luxembourg law. The bill covers the reporting and disclosure requirements of in-scope entities to address environmental, social, and governance (**ESG**) impacts. The CSSF will act as a supervisory authority overseeing the sustainability information within the CSRD requirements. In general, the bill aims to improve the quality, consistency, and transparency of sustainability reporting. It is currently under discussion in Parliament and expected to be adopted in early 2025.

Regulatory development related to DLT market infrastructures

On 2 June 2022, Regulation (EU) 2022/858 of the European Parliament and of the Council on a pilot regime for market infrastructures based on distributed ledger technology (**DLT**) (the **EU DLT Pilot Regime**) was published in the Official Journal of the EU. The Regulation has applied in Luxembourg since 23 March 2023 and was implemented by the law of 15 March 2023, which amended, *inter alia*, the definition of financial instruments set out in the LFS to reflect financial instruments using DLT, supplements the EU DLT Pilot Regime in Luxembourg and addresses a few points left open by the previous laws on DLT. The EU DLT Pilot Regime lays down requirements in relation to DLT market infrastructures and their operators with respect to, among other things, granting and withdrawing specific permissions to operate DLT market infrastructures, operating and supervising DLT market infrastructures as well as enabling such entities to be exempted from other requirements under EU directives or regulations, including MiFID II/MiFIR and the Central Securities Depository Regulation (**CSDR**).

Against this background and in the context of the Innovation Hub, applicants looking to operate a DLT market infrastructure may contact the CSSF to obtain regulatory guidance and to discuss the relevant legal requirements together with the technology aspects of the project or organise an exchange with the CSSF before submitting their application. In that regard, on 8 March 2023, the CSSF published CSSF Circular 23/832, integrating ESMA's Guidelines on standard forms, formats and templates to apply for permission to operate a DLT market infrastructure. Additionally, the adoption of the Blockchain IV Law (as defined below) has opened up a significant range of possibilities for using blockchain technology, particularly DLT, in the management of dematerialised securities, thereby enabling the use of DLT for issuing and transferring fund units.

Recent regulatory themes and key regulatory developments in Luxembourg

Change to the regulatory regime following the financial crisis

European banking regulation has undergone a continuous evolution since the financial crisis of 2008 and the adoption of a certain number of directives and regulations as a response to the financial crisis. The main legislation taken in this respect could be summarised as follows:

- CRD IV;
- the CRR;

- EU Regulation 2013/1024 of 15 October 2013 conferring specific tasks on the ECB concerning policies relating to the prudential supervision of credit institutions, and EU Regulation 2013/1022 of 22 October 2013 amending EU Regulation 2010/1093 of 24 November 2010 establishing a European supervisory authority (the EBA) as regards the conferral of specific tasks on the ECB pursuant to EU Regulation 1024/2013, together establishing the SSM; and
- EU Regulation 2014/806 of 15 July 2014, as amended, establishing uniform rules and a uniform procedure for the resolution of credit institutions and certain investment firms in the framework of a Single Resolution Mechanism and a Single Resolution Fund and amending EU Regulation 2010/1093, and the BRRD, together establishing the Single Resolution Mechanism.

These regulations were part of a logic of risk reduction in the banking sector within the EU and the Eurozone. The gradual establishment of a Banking Union at the EU level with its unique supervision and resolution mechanisms marked the starting signal for risk pooling through the establishment of euro area-wide safety nets, including the Single Resolution Fund.

Most of the above legislative texts have already been amended with the CRD V and BRRD II Packages and are subject to further amendments following the European Commission's adoption, on 27 October 2021, of a review of the EU banking rules. The CRD V Law amending the LFS, introducing novel concepts, is analysed in subsequent sections.

Regulatory developments relating to Fintech

The Luxembourg legislator has taken significant initiatives in the area of digitalisation of banking and financial activities and more specifically in the implementation of technological innovations in the field of capital markets. Two distinct laws passed in 2019 and 2021 allowed the use of new technologies in the issuance, holding and circulation of securities.

The law of 1 March 2019 (the **Blockchain I Law**) amended the law of 1 August 2001, as amended (the **General Securities Law**), allowing the use of secure electronic mechanisms for the holding and circulation of securities. The Blockchain I Law represented a milestone in the digitalisation of capital markets in Luxembourg as it acknowledged, for the first time, the issuance of security tokens, a specific category of crypto-assets defined in the parliamentary works as assets stored in a blockchain that represent the securities.

In an effort to extend and refine the scope of application of the Blockchain I Law, the Luxembourg Parliament passed the law of 21 January 2021 (the **Blockchain II Law**), which amended the law of 6 April 2013, as amended (the **Dematerialised Securities Law**) and the LFS, as amended. The Blockchain II Law extended the possibility to use secured electronic registration systems, such as DLT and databases, to the issuance of dematerialised securities. Following the Blockchain II Law, EU credit institutions and investment firms are allowed to take the role of central account keeper, and to hold and manage securities issuance accounts with such technologies through secured electronic registration systems such as DLT (e.g., blockchain) and databases.

The Blockchain I and II Laws filled a gap in a fundamental area of the Luxembourg legal framework, providing legal certainty to financial market participants and making the Luxembourg environment Fintech-oriented. By implementing the principle of digital neutrality, the legislator acknowledged not only the use of digital ledger technologies such as blockchain but created an open-ended system enabling the smooth introduction of future technological developments in the securities market.

The Blockchain III Law entered into force on 23 March 2023 and follows in the footsteps of previous initiatives taken by the Luxembourg legislator. Since the adoption of the Blockchain I and II Laws, the Luxembourg legal framework already explicitly recognises the possibility of using DLT for the issuance and circulation of securities. All of the blockchain laws, including the latest addition, aim to ensure a principle of technological neutrality.

Recently, the Luxembourg Parliament adopted the law of 19 December 2024 (the **Blockchain IV Law**), which amended the Dematerialised Securities Law and complemented MiCAR (as defined below) to broaden the possibilities for managing dematerialised securities. The Blockchain IV Law seeks to integrate and formalise the use of blockchain technology through DLT, including maintaining a security account and tracking the chain of securities ownership. The law introduced a new player, the control agent, that will be responsible for managing and verifying securities by leveraging DLT. Such a control agent may be a credit institution, clearing organisation, or investment company and is not required to obtain prior authorisation from the CSSF. The Blockchain IV Law provides new opportunities for the development of DLT-based activities in the financial sector and enables decentralised security transactions while maintaining regulatory integrity.

The CSSF also constantly monitors the Fintech sector, communicating the benefits and warning of the risks associated with the use of technologies in the financial sector. In this respect, on 3 May 2023, the CSSF published a thematic review on the use of AI in the Luxembourg financial sector that provides information on the usage of AI together with its related benefits and challenges, including use cases implemented by, among others, 117 credit institutions in Luxembourg. Out of a total of 158 use cases of which more than half are still in production, the top areas in which AI technology was reported are AML/fraud detection, process automation, marketing/product recommendation, customer rights and cybersecurity. Among the respondents, it appears that credit institutions are more advanced in the use of AI technology compared to other financial institutions by reference to the number of use cases. Overall, the results from the survey demonstrate that the usage of AI in the Luxembourg financial sector is still at an early stage but that investments in AI, in view of the reported general increase of such investments from 2021 to 2022 especially in the area of machine learning, are estimated to increase in the near future.

Furthermore, following the publication of the Markets in Crypto-Assets Regulation (**MiCAR**) in the Official Journal of the EU, the provisions of Titles III (Asset-Referenced Tokens, **ART**) and IV (E-Money Tokens, **EMT**) thereof relating to the authorisation and supervision of ART/EMT have applied since 30 June 2024. In that regard, credit institutions that carried out ART or EMT issuance activities before 30 June 2024 are encouraged to communicate such intention to the CSSF using the template that is available on the EBA's website, also having regard to the guiding principles included in the Annex to the EBA Statement.

On 16 January 2024, the EBA extended its guidelines on ML/TF risk factors to CASPs through the issue of guidance to CASPs to effectively manage their exposure to ML/TF risks. The new guidelines highlight ML/TF risk factors and mitigating measures that CASPs need to consider, representing an important step forward in the EU's fight against financial crime. MiCAR brings crypto-asset services and activities within the EU regulatory scope and ensures that CASPs become subject to EU AML/CFT obligations and supervision. By doing so, it prevents credit and financial institutions from engaging with providers of crypto-asset services, which will provide a stratified mitigation of risk.

As financial technologies continue to grow, the EU is implementing significant measures to align with financial stakeholders. The full application of MiCAR in 2025 aims to establish a uniform regulatory framework for CASPs and crypto-assets across the EU and mandates that CASPs comply with specific rules on authorisation, consumer protection, and transparency. From January 2025, digital asset issuers are required to publish white papers for each token, similar to a financial prospectus, including details on function, technology, and risk. Furthermore, CASPs will be subject to regulatory and reporting obligations and will fall under the supervision of ESMA and national authorities to ensure adherence to the regulatory framework. Overall, MiCAR marks a significant step towards integrating cryptocurrencies and digital assets into financial technologies, promoting a safer environment for investors, and facilitating the growth of digital financial instruments.

Bank governance and internal controls

Key requirements set out in the LFS relating to the central administration and internal controls of credit institutions are specified in CSSF Circular 12/552, as amended. In a nutshell, Luxembourg regulation requires credit institutions to have robust internal governance arrangements, effective risk management processes, adequate internal control mechanisms, sound administrative and accounting procedures, remuneration policies and practices allowing and promoting sound and effective risk management, as well as control and security arrangements for information processing systems.

More precisely, the following general requirements apply to boards of directors of banks, committees, remuneration and internal control.

Management and central administration

The central administration of a credit institution must be established in Luxembourg. The authorised management of credit institutions must be composed of at least two members (the so-called "four-eyes principle") who must be empowered to effectively direct the business. The managers must produce evidence of their professional repute. In addition, they must have already acquired an adequate level of professional experience through the performance of similar activities and assessed on the basis of a *curriculum vitae* and/or any other relevant evidence. The good repute of the members of the bodies performing administrative, management and supervisory functions is assessed on the basis of police records and any evidence that shows that the persons concerned have a good reputation and offer every guarantee of irreproachable conduct. The prudential approval procedure sets out the fit and proper approval process for the appointment of key function holders and members of the management body in credit institutions. Recent amendments to CSSF Circular 12/552 have enhanced the provisions with respect to the diversity and independence of the management body.

Committees

Banks may be required to put in place various committees, such as an audit committee or a risk committee, which oversee certain areas of the bank's operations. The obligations relating to committees depend on the size and scale of the bank, though a relevant point is the fact that their decisions must consider long-term public interest.

Remuneration policies

The aim of the procedures and arrangements implemented in relation to remuneration is to help ensure that risks are managed in an efficient and durable manner. Credit institutions must comply with the requirements concerning the governance arrangements and remuneration policies of CRD IV and CRD V, as transposed into the LFS, and will in due course have to comply with the requirements of CRD VI. Furthermore, credit institutions must comply with the disclosure requirements of the CRR, the criteria set out in the relevant EU regulatory technical standards, the EBA Guidelines on remuneration policies and best practices, and the applicable CSSF circulars. The CRD V Law introduced some novel provisions. Most importantly, the rules governing the remuneration policy may henceforth apply on a consolidated, sub-consolidated or solo basis, depending on specific parameters. Furthermore, the above rules apply to all employees whose activities have a material impact on the risk profile of a given credit institution, and not only to the management body. The content of the latter term is defined in article 38-5(2) of the LFS, which should be read in conjunction with Commission Delegated Regulation (EU) 2021/923. Smaller and non-complex institutions benefit from some waivers concerning the application of a limited number of remuneration requirements. At the same time, the CRD V Law recognised and implemented for the first time the gender-neutral nature of the remuneration policy.

Internal control environment

CSSF Circular 12/552, as amended, requires banks to have dedicated internal control functions, such as a risk control function, a compliance function and an internal audit function. The internal control functions are permanent and independent functions, each with sufficient authority. The degree of the measures required is subject to the principle of proportionality, meaning that more complex, riskier and significant institutions must have in place enhanced internal governance and risk management arrangements.

Luxembourg regulation requires that the organisation chart of the credit institution is established based on the principle of segregation of duties, pursuant to which the duties and responsibilities will be assigned so as to avoid making them incompatible for the same person. The goal pursued is to avoid conflicts of interest and to prevent a person from making mistakes and irregularities that would not be identified. In the context of mitigating conflicts of interest, the CRD V Law requires the management body of credit institutions to document data related to loans provided to the management body and share these data with the CSSF upon its request.

Outsourcing of functions is generally permitted under the conditions laid down in the LFS and relevant CSSF circulars. However, outsourcing must not result in non-compliance with the rules of CSSF Circular 12/552 as amended and, in particular, CSSF Circular 22/806 on outsourcing arrangements that includes both ICT and cloud outsourcing, by means of which the CSSF adopted and integrated, among others, the revised EBA Guidelines (EBA/GL/2019) on outsourcing arrangements (the **Circular OS**). Accordingly, all outsourcing arrangements have to comply with the general requirements laid down in Part I of the Circular OS, while ICT outsourcing arrangements also have to meet the specific requirements laid down in Part II thereof. The general outsourcing requirements include, *inter alia*, that the outsourcing institutions comply with the following requirements: (i) outsourcing arrangements, such as the concentration risk posed by outsourcing critical or important functions to a limited number of service providers, shall not create undue operational risks; (ii) the institution retains the necessary expertise to effectively monitor the outsourced services or tasks; (iii) the institution ensures protection of the data concerned in accordance with Regulation (EU) 2016/679 of 27 April 2016 on General Data Protection; and (iv) the institution applies the relevant provisions of the LFS on professional secrecy. Outsourcing does not relieve the institution of its legal and regulatory obligations or its responsibilities to its customers. Furthermore, the final responsibility or the management of risk shall lie with the outsourcing institution, while the institution shall establish an outsourcing policy and maintain an outsourcing register recording all outsourcing arrangements. In addition to the general requirements, Circular 21/785, amending Circular 12/552, replaced the obligation of prior authorisation with that of notification to the CSSF with regard to outsourcing of a critical or an important function while there are no specific formalities in place with regard to outsourcing of non-critical or non-important functions. In that regard, the CSSF released a new notification template that aligns the terminology and structure of the template with the Circular OS.

Bank capital requirements

The regulatory capital and liquidity regime currently applicable to banks in Luxembourg derives mainly from the CRD V Package and numerous underlying local regulations, circulars and circular letters adopted by the CSSF. It is worth noting that following the procyclical mechanisms that contributed to the origin of the financial crisis of 2008, the FSB, the Basel Committee on Banking Supervision and the G20 made recommendations to mitigate the procyclical effects of financial regulation. In December 2010, the Basel III Framework, which consisted of new global regulatory standards on bank capital adequacy, was issued by the Basel Committee on Banking Supervision. In June 2013, the Basel III Framework was implemented into the CRR/CRD IV Package and amended by the CRD V Package. In April 2024, the European Parliament adopted a new banking package, commonly referred to as CRR III and CRD VI, which will come into effect on 1 January 2025. This package will implement elements of the Basel III international framework for

banks, alongside measures for ESG risk mitigation and third-country financial access. Once CRR III becomes effective, it will substantially alter the provisions related to risk-weighted assets and capital requirements, significantly impacting the profitability of financial institutions and ICT reporting.

Capital and liquidity requirements

Share capital

Credit institutions in Luxembourg are required to have a subscribed and fully paid-up share capital of at least €8.7 million. The capital base cannot be less than the amount of the prescribed authorised capital.

Own funds

In addition to the share capital requirement, credit institutions must maintain and satisfy at all times a total capital ratio of 8% of their risk-weighted assets, composed of 4.5% of Common Equity Tier 1 capital (**CET1**) (as defined in the CRR), 1.5% of Additional Tier 1 capital (as defined in the CRR), and 2% of Tier 2 capital (as defined in the CRR). The above minimum capital requirements are part of the so-called Pillar 1 of the Basel III Framework (**P1R**). As specified in the LFS and CSSF Regulation 15-02, as amended, the CSSF is capable of imposing bank-specific capital requirements (Pillar 2 Requirements – **P2R**) that have micro-prudential considerations and apply in addition to, and cover risks that are underestimated or not covered by, P1R. Both P1R and P2R are binding and obligatory for credit institutions, which is not the case for the Pillar 2 Guidance rules (**P2G**), which constitute suggestions of the CSSF to the banks relating to their own funds. The CRD V Law has clarified the relationship between P2R and P2G.

In addition to other own funds requirements, credit institutions in Luxembourg are required to hold and maintain the following buffers:

- a capital conservation buffer of CET1 equal to 2.5% of their total risk exposure amount;
- an institution-specific countercyclical capital buffer of CET1 (equivalent to their total risk exposure). The CSSF is responsible for setting the countercyclical buffer rates applicable in Luxembourg on a quarterly basis. According to CSSF Regulation 24-06, a countercyclical capital buffer rate of 0.5% applied to credit institutions for the fourth quarter of 2024;
- a Global Systemically Important Institutions (**G-SII**) buffer, being a mandatory capital surcharge built up of CET1 and applied at the consolidated level of the identified banking groups' additional capital requirements for systemically important banks. The capital surcharge may vary between 1% and 3.5% depending on the degree of systemic importance of the relevant bank. According to publicly available information, there is no bank established in Luxembourg identified as a G-SII;
- an Other Systemically Important Institutions (**O-SII**) buffer applied on a consolidated/sub-consolidated or solo basis. In this respect, the CSSF takes its decisions after consultation with the BCL and after requesting the opinion of the *Comité du Risque Systémique*. The O-SII buffer may reach up to 3% or even surpass this threshold if the European Commission's authorisation has been granted. The CSSF and the BCL have jointly developed a calibration methodology designed to translate the systemic importance of the institutions into O-SII buffer rates; and
- a systemic risk buffer for systemic banks of at least 1% based on the exposures to which the systemic risk buffer applies, which may apply to exposures in Luxembourg as well as to exposures in third countries. The rationale of this buffer, as clarified in the CRD V Law, is the mitigation of systemic risks, to the extent that these are not already covered by the capital buffers for systemically important institutions (G-SIIs/O-SIIs) or the countercyclical capital buffer. No maximum limit applies to this buffer.

Liquidity and funding requirements

In order to ensure the stability of financial institutions, the following liquidity and funding standards

(adopted in the EU and designed to achieve two separate but complementary objectives) apply to credit institutions in Luxembourg:

- a Liquidity Coverage Ratio, which aims to improve the short-term resilience of a bank's liquidity risk profile by ensuring that it has sufficient high-quality liquid assets to survive a significant stress scenario lasting for 30 days. Financial institutions are required to hold liquid assets at all times, the total value of which equals, or is greater than, the net liquidity outflows that might be experienced under stressed conditions over a short period of time (30 days). Net cash outflows must be computed on the basis of a number of assumptions concerning runoff and drawdown rates; and
- a Net Stable Funding Ratio (the **NSFR**), which aims to ensure the resilience of financial institutions over a longer time horizon of one year by promoting a sustainable maturity structure of assets and liabilities. Financial institutions are required on an ongoing basis to raise stable funding at least equal to their stable assets or illiquid assets that cannot be easily turned into cash over the following 12 months. Following the amendment of the CRR by CRR II and now by CRR III, the NSFR is applicable to all credit institutions as of 28 June 2021. Liquidity and uniformity of institutional internal models are emphasised by CRR III to a greater extent, with the aim of reducing the risk of excessive capital reductions.

Compliance with the rules relating to bank capital and liquidity requirements is under the control of the CSSF and the ECB. In addition, financial institutions are subject to periodic reporting requirements.

This regulatory framework has substantially contributed to the strengthening of the regulations applicable to the banking system in the EU and rendered institutions more resilient to possible future shocks. Although comprehensive, those measures did not address all identified weaknesses affecting institutions. The European Commission adopted a review of the CRD V Package. Having gained important lessons from the COVID-19 pandemic and taking into consideration the necessity of approaching the CRD V Package from a greener perspective, the new framework will focus on strengthening the resilience of banking institutions to economic shocks, contributing to the green transition, mitigating ESG risk factors and ensuring sound management of EU banks and better protecting their financial stability. The CRD VI Package aims to strengthen the EU legal framework by mitigating the ESG-related risks in regard to the banking sector and harmonising the requirements for banking services provided by banks in the EEA and third countries.

Rules governing banks' relationships with their customers and other third parties

Regulation relating to customers

Banks' relationships with their customers and third parties deriving from deposit-taking, lending activities and investment services are mainly governed by:

- the law of 30 May 2018 on markets in financial instruments, as amended, transposing, among others, Directive 2014/65/EU of 15 May 2014 on markets in financial instruments (**MiFID II**) and amending Directive 2002/92/EC, Directive 2011/61/EU, and Regulation (EU) 600/2014 of 15 May 2014 on markets in financial instruments (**MiFIR**, together with MiFID II commonly referred to as the **MiFID Framework**), as well as several delegating acts, which provide for harmonised protection of (retail) investors in financial instruments;
- Regulation (EU) 1286/2014 on key information documents for packaged retail and insurance-based investment products (the **PRIIPs Regulation**) applicable since 1 January 2018. The PRIIPs Regulation requires that all packaged retail and insurance-based investment products (**PRIIPs**) manufacturers provide a key information document to retail investors in order to enable retail investors to understand and compare the key features and risks of the PRIIPs;

- the law of 17 April 2018 on key information documents for PRIIPs implementing the PRIIPs Regulation designates the CSSF and the CAA as the competent supervisory authorities regarding supervision and compliance with the requirements of the PRIIPs Regulation; and
- the provisions of the Luxembourg Consumer Code related to the protection of consumers, which also affect banks' dealings with their customers. Following these provisions, banks must, among others, comply with obligations relating to information that should be provided to customers, rules on advertising, the content of credit agreements and the prohibition of unfair business practices. Before granting a credit, the solvency of the customer needs to be evaluated.

Customer complaint handling

In addition, the CSSF is competent to receive customer complaints against the entities subject to its supervision. Provided that, *inter alia*, the customer complaint has been previously dealt with by the relevant professional without a satisfactory result, the customer may request for an out-of-court resolution from the CSSF. The CSSF then acts as an intermediary with the parties in order to seek an amicable solution. The CSSF acts in its capacity as alternative dispute resolution entity, and Luxembourg courts remain competent to handle litigations relating to consumer protection.

Protection of depositors and investors

Following the entry into force of the law of 18 December 2015 on the failure of credit institutions and certain investment firms, the following compensation schemes have been created:

- an Investor Compensation Scheme (*Système d'Indemnisation des Investisseurs Luxembourg*), being the recognised Luxembourg Investor Compensation Scheme as referred to in Directive 97/9/EC and chaired by the CSSF. The main purpose of the Investor Compensation Scheme is to ensure coverage for the claims (funds and financial instruments that its members hold, manage or administer on behalf of their clients) resulting from the incapacity of a credit institution or an investment firm. In case the relevant criteria are met and the institution holding the investor's assets is no longer able to fulfil its commitments, investors are repaid by the Investor Compensation Scheme. The repayment covers a maximum amount of €20,000 per investor; and
- a Deposit Guarantee Fund (*Fonds de Garantie des Dépôts Luxembourg*), being the recognised Luxembourg Deposit Guarantee Scheme referred to in Directive 2014/49/EU of 16 April 2014 on Deposit Guarantee Schemes. The main purpose of the Deposit Guarantee Fund is to ensure compensation of depositors in case of unavailability of their deposits. It collects the contributions due by participating credit institutions, manages the financial means and, in the event of insolvency of a member institution, makes the repayments as instructed by the *Conseil de protection des déposants et des investisseurs*, the internal executive body of the CSSF in charge of managing and administering Luxembourg compensation schemes. It is worth noting that membership to the Deposit Guarantee Fund is compulsory for all credit institutions and Luxembourg branches of credit institutions having their registered office in a third country. In case the relevant criteria are met and the institution holding the depositor's assets is no longer able to fulfil its commitments, depositors are repaid by a Deposit Guarantee Scheme. The repayment covers a maximum amount of €100,000 per person and per bank.

Restrictions on inbound cross-border banking activities

Any person wishing to conduct inbound cross-border banking activities in Luxembourg that fall under the rules of the LFS must obtain the necessary authorisation as stipulated in the LFS. However, credit institutions authorised by a competent authority within the EU/EEA may rely on the European banking passport mechanism. Pursuant to the principle of mutual recognition of authorisation, these authorised institutions are allowed to carry out a number of activities in Luxembourg, subject to having completed the necessary formalities with their home state authorities, which in turn will notify the CSSF.

The regulatory framework on AML/CFT

Banks must comply with the professional obligations arising from the AML/CFT Law and other applicable regulations, and more specifically customer due diligence obligations, adequate requirements relating to internal management and cooperation requirements with the authorities. Luxembourg has also strengthened its obligations relating to AML/CFT by transposing certain provisions of the Fourth and Fifth AML Directives, aiming to prevent ML/TF through the implementation of (i) a register aiming to identify ultimate beneficial owners of companies registered with the Luxembourg Trade and Companies Register, which has been effective since 1 March 2019, and (ii) a central register of beneficial owners of fiduciary and similar arrangements, which entered into force on 10 July 2020. These laws require, *inter alia*, that companies registered with the Luxembourg Trade and Companies Register, trustees, and fiduciary agents, obtain and retain data relating to beneficial owners and to certain other persons specified in the respective laws. Registration of certain data collected by the relevant company, trustees and fiduciary agents to the relevant central register is mandatory; failing this, criminal sanctions are provided by these laws.

In June 2024, a new AML Package was published, consisting of three legal texts: (i) Regulation (EU) 2024/1624, also known as the EU AML Single Rulebook (the **AMLR**), on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing; (ii) Regulation (EU) 2024/1620, establishing the Authority for Anti-Money Laundering and Countering the Financing of Terrorism (**AMLAR**); and (iii) AMLD6. The main purpose of the adopted package is to harmonise AML/CFT measures across the EU through the AMLR, mitigate the abuse of financial systems, and establish a supervisory body for the implementation of AML/CFT provisions. The AML/CFT Law also enacts the core principle of a "risk-based approach" whereby professionals have to take appropriate measures to identify and assess the risks of AML/CFT with which they are confronted, taking into consideration risk factors such as those related to their customers, countries' geographic areas, products, services, transactions or delivery channels.

The CSSF has the supervisory and investigatory powers to carry out its statutory mission to ensure that all entities subject to its supervision comply with the professional AML/CFT obligations. In addition, the CSSF has broad sanctioning powers. It may, for example, issue warnings or administrative fines against persons subject to its AML/CFT supervision. Monitoring risk in relation to anti-money laundering continues to be a high priority of the CSSF's supervision, and the CSSF staff in charge of the AML/CFT supervision is constantly increasing. Recent changes to the AML/CFT legislation also provide for a stronger cooperation framework between different supervisory authorities both on a national and an international level.

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