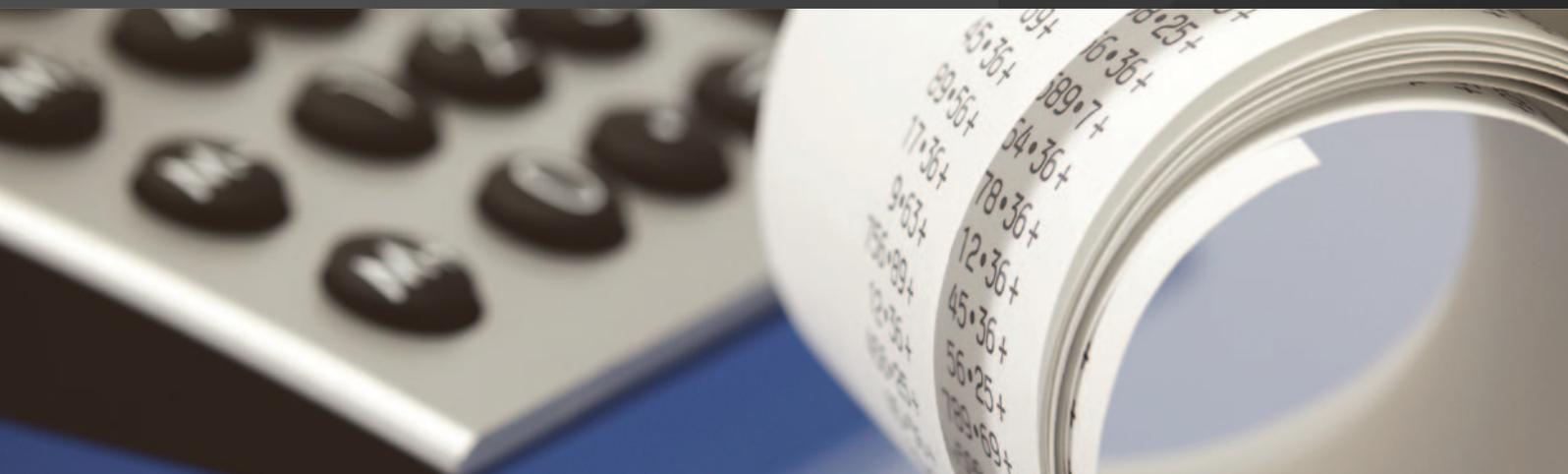


International Comparative Legal Guides



Corporate Tax 2020

A practical cross-border insight to corporate tax law

16th Edition

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16th Edition

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1.1 How many income tax treaties are currently in force in your jurisdiction?

As of August 2019, Luxembourg has 83 tax treaties currently in force and an additional 20 under negotiation.

1.2 Do they generally follow the OECD Model Convention or another model?

Tax treaties concluded by Luxembourg are usually based on the OECD Model Tax Convention (the “**OECD MC**”). Luxembourg has agreed with most of the treaty countries to implement a provision on the exchange of information in line with Article 26 of the OECD MC. The new tax treaty, signed with France on 20 March 2018 and entering into force as of 1 January 2020, reflects all the post-BEPS changes and the 2017 version of the OECD MC; *inter alia*, the treaty changes the definition of a permanent establishment to include *commissionaire* arrangements, and restricts the scope of the “preparatory and auxiliary” activities. It further changes the distributive rules for payments of dividends, interest and royalties in line with the 2017 OECD MC.

A few treaties signed by Luxembourg deviate from the OECD MC. A notable example is the treaty concluded with the USA which follows the US Model Income Tax Convention. A more recent example is the treaty signed with Senegal, which more closely resembles the UN model.

1.3 Do treaties have to be incorporated into domestic law before they take effect?

All tax treaties are incorporated into domestic law pursuant to the following procedure: the legislator adopts a consenting law (*loi d'adaptation*) that authorises the Grand Duke to ratify the tax treaty. Before the treaty takes effect, it is submitted for approval by the parliament (*Chambre des députés*). The parliament's approval takes the form of a law (*loi d'approbation*). After the aforementioned procedure is completed, the treaty will take effect once it is ratified by the Grand Duke. The treaty must then be published in the *Mémorial* in order to be in force in Luxembourg.

Tax treaties signed by Luxembourg generally specify an exact date on which the treaty enters into force.

1.4 Do they generally incorporate anti-treaty shopping rules (or “limitation on benefits” articles)?

As a general rule, tax treaties concluded by Luxembourg do not include anti-treaty shopping rules. However, a limitation on benefits

(“**LOB**”) clause is used in the treaties signed with *i.a.* Hong Kong, Poland, Senegal, Singapore, Trinidad and Tobago, and the USA. Interestingly, the new treaty signed with France contains a specific anti-treaty shopping rule in its new Article 28 (“Denial of benefits under the Convention”).

In addition, the MLI signed by Luxembourg contains a general anti-abuse provision in the preamble to all of its tax treaties, which includes the express statement to eliminate double taxation without creating opportunities for reduced taxation or non-taxation. Such provision is a minimum standard and cannot be opted out by any of the signatories to the MLI. In the context of Article 7 (prevention of treaty abuse), countries may choose to apply either the Principle Purpose Test (“**PPT**”) or the detailed LOB provisions. Like most of the signatories to the MLI, Luxembourg chose to apply the PPT.

1.5 Are treaties overridden by any rules of domestic law (whether existing when the treaty takes effect or introduced subsequently)?

Luxembourg applies the hierarchy of norms. The constitution is the highest source of law, followed by laws and regulations. It is worth noting that the relationship between international law and domestic law is governed entirely by case law. Such established case law states that tax treaties incorporated into internal legislation by a ratification law should constitute a superior law. Therefore, if a conflict between the provisions of an international treaty and those of a national law occurs, international law should take precedence over the national law.

Further to the above and under the general principles of Luxembourg public law, treaties are considered a “*lex specialis*” and therefore take precedence over the national provisions.

1.6 What is the test in domestic law for determining the residence of a company?

According to Article 159 of the Luxembourg income tax law (“**LITL**”), an entity is treated as a resident of Luxembourg for direct tax purposes if it has: (i) its registered office (*siège statutaire*) in Luxembourg; or (ii) its central administration (*administration centrale*, i.e. the place of effective management) in Luxembourg.

2.1 Are there any documentary taxes in your jurisdiction?

Under Luxembourg law, certain acts such as official acts, acts of estate agents and transfer of ownership of certain goods, are required to be registered with the Luxembourg *Administration de l'Enregistrement, des Domaines et de la TVA*. Registration duties are fixed or proportional, depending on the nature of the acts and transfers that are subject to them. A fixed fee of €12 is levied on all acts

which do not contain a movement of securities, while a proportional duty (ranging from 0.01% to 14.4%, depending on the transaction and the nature of the underlying asset) is levied on acts and conventions involving a movement of securities.

For instance, payment obligations are subject to a proportional 0.24% registration duty (which tax is calculated on the principal or highest amount stated in the document), if stated in a loan agreement physically attached to a deed subject to mandatory registration (such as a notarial deed).

2.2 Do you have Value Added Tax (or a similar tax)? If so, at what rate or rates?

Luxembourg applies Value-Added Tax (“VAT”) pursuant to the law of 12 February 1979 as amended (the “VAT Law”). Currently, four rates are applicable: 17% standard rate; an intermediary rate of 14%; a reduced rate of 8%; and a super-reduced rate of 3%. Annexes A, B and C provide for a detailed list of services and goods that are subject to the reduced rates. Such Annexes are to be interpreted strictly.

2.3 Is VAT (or any similar tax) charged on all transactions or are there any relevant exclusions?

Luxembourg as a Member State of the EU follows the partially harmonised VAT system and applies exemptions as prescribed for by the Council Directive 2006/112/EC, as amended (the “VAT Directive”). Such exemptions are granted *i.a.* in the context of financial services, fund management or medical services. An important point to highlight is that Luxembourg does not allow for an “opt in/opt out” mechanism for activities that are exempt – with the exception of rent, in which case the taxable person can choose whether to apply VAT or not.

2.4 Is it always fully recoverable by all businesses? If not, what are the relevant restrictions?

In accordance with EU VAT rules, companies registered for VAT can deduct input VAT to the extent it is linked with their output VATable economic activity. In the past, a *pro rata* deduction was used based on the percentage of VATable and non-VATable activities. However, after the judgment of the Court of Justice of the European Union (the “CJEU”) in *BLC Baumarkt GmbH & Co. KG* (C-511/10), the VAT directive must be interpreted as allowing Member States to use a more accurate method than the one of the general *pro rata*. In Circular n° 765 of 15 May 2013, the Luxembourg VAT authorities referred to a direct allocation or another key allocation method. The general *pro rata* deduction should not be used if a more precise allocation method can be applied.

As per Circular n° 765-1 of 11 June 2018, the VAT tax administration extended the regime applicable in Circular n° 765 to persons carrying out both economic and non-economic activities for VAT purposes. The former Circular referred only to persons carrying out an economic activity partially exempt for VAT purposes.

2.5 Does your jurisdiction permit VAT grouping and, if so, is it “establishment only” VAT grouping, such as that applied by Sweden in the *Skandia* case?

In its judgment of 4 May 2017, the CJEU ruled that the Luxembourg implementation of the VAT group regime was not compatible with the VAT Directive, as it extended the benefits of the exemption to taxable activities that were not directly necessary for the exempt or out-of-scope activities of the VAT group. In light of the above decision, Luxembourg has repealed its old regime and implemented a new VAT group regime as per the law of 6 August 2018 (in line with the *Skandia* case (C-7/13)).

The new VAT group regime treats all of the transactions between its members as “out of the scope” of the VAT. One of the major differences between the new and the former regime is that the VAT group regime is restricted to persons established in Luxembourg and Luxembourg branches of foreign companies, whereas the former regime allowed for grouping with other Member States of the EU. Companies wishing to benefit from the VAT group regime must generally meet three requirements proving their bond. There must be an: (i) economic; (ii) financial; and (iii) organisational link with the other company(-ies).

2.6 Are there any other transaction taxes payable by companies?

A fixed registration fee of €75 is due in some specific cases determined by law such as, but not limited to: upon incorporation or subsequent capital increase; and migration of a company to Luxembourg.

2.7 Are there any other indirect taxes of which we should be aware?

There are custom and excise duties applicable for certain goods.

3.1 Is any withholding tax imposed on dividends paid by a locally resident company to a non-resident?

Dividends paid to residents as well as non-residents are subject in principle to a 15% withholding tax (“WHT”) in Luxembourg. It is possible, however, to benefit from either a reduced rate, an exemption under a double tax treaty, or the domestic participation exemption regime.

Domestic participation exemption is granted if, at the time of the dividend distribution:

- the parent company is a fully taxable Luxembourg company, or a resident company of a Member State of the EU as defined in Article 2 of the EU Parent-Subsidiary Directive 2011/96, as amended (the “PSD”), or a Swiss-resident capital company that is subject to income tax in Switzerland without being exempt from tax, or a foreign joint-stock company which is subject in its country of residence to an income tax regime corresponding to the Luxembourg corporate income tax (“CIT”);
- said company holds or commits to hold a participation of at least 10% (or with an acquisition price of at least €1.2 million) in the nominal share capital of the distributing company; and
- such qualifying participation has been held for an uninterrupted period of at least 12 months.

If the shareholder is an EU company within the scope of the PSD, the exemption applies subject to the additional general anti-abuse rule (“GAAR”) below:

- the EU parent company is not used for the main purpose or as one of the main purposes of obtaining a tax advantage that defeats the object of the PSD.

Liquidation proceeds are not subject to dividend WHT. If properly structured, a partial liquidation may additionally not be subject to the WHT.

In addition, dividend payments made by a certain type of vehicle, e.g. SPFs, SICAV, SICAR and securitisation vehicles, are not subject to WHT.

3.2 Would there be any withholding tax on royalties paid by a local company to a non-resident?

There has been no WHT on royalties in Luxembourg since 1 January 2004.

3.3 Would there be any withholding tax on interest paid by a local company to a non-resident?

There is no WHT on arm's length interest payments in Luxembourg. Interest paid under certain hybrid instruments, or not at arm's length, may be subject to a 15% WHT if reclassified as dividend payments by the tax authorities.

3.4 Would relief for interest so paid be restricted by reference to "thin capitalisation" rules?

There is currently no legislation concerning the thin capitalisation ratio specifically but, in practice, the tax administration uses a debt-to-equity ratio of 85:15 for the intra-group financing of participations. In case a taxpayer fails to comply with this ratio, the surplus of interest may be requalified as a hidden dividend distribution. Such requalification would result in a lack of deductibility for those payments and possible application of a 15% WHT (subject to applicable tax treaty or participation exemption, if applicable). Back-to-back financing is not subject to the abovementioned ratio.

As of 1 January 2019, however, due to the transposition into Luxembourg tax law of the interest deduction limitation rule (article 168*bis* of the Luxembourg Income Tax Law ("LITL")), deduction of interest qualifying as "exceeding borrowing costs" is limited up to the higher of:

- (i) 30% of the company's EBITDA (defined as the total net income increased by the exceeding borrowing costs, depreciation and amortisation), or
- (ii) €3 million.

The €3 million threshold should also be calculated on the company level, not only on its compartment level.

Exceeding borrowing costs is defined as the amount by which the deductible borrowing costs of a taxpayer exceed taxable interest revenues and other economically equivalent taxable income of the taxpayer.

Interestingly, although borrowing costs are defined, there is no definition of "interest revenues and other equivalent taxable income". Based on the recommendation of the Luxembourg Chamber of Commerce, practitioners take the view that such term should be interpreted by analogy with the definition of borrowing costs and should encompass by symmetry the items listed under the latter definition (e.g., but not limited to: payments under profit participating loans; imputed interest on instruments such as convertible bonds and zero-coupon bonds; amounts paid under alternative financing arrangements, such as Islamic finance; the finance cost element of finance lease payments; capitalised interest included in the balance sheet value of a related asset, or the amortisation of capitalised interest; amounts measured by reference to a funding return under transfer pricing rules; notional interest under derivative instruments or hedging arrangements related to an entity's borrowings; certain foreign exchange gains and losses on borrowings and instruments connected with the raising of finance; guarantee fees for financing arrangements; and arrangement fees and similar costs related to the borrowing of funds).

Exceeding borrowing costs not deductible in a tax period can be carried forward indefinitely. The same applies to the excess interest capacity which cannot be used in a given tax period (however, for a maximum period of five years).

Exemptions to the interest deduction limitation rule have been introduced, as follows:

Grandfathering: debt instruments concluded before 17 June 2016 will not fall within the scope of the interest limitation rule to the extent that they have not been amended. The amount of exceeding borrowing costs shall be computed as if no amendments have taken place.

Stand-alone entity: stand-alone entities are exempt from the scope of application of the interest deduction limitation rule. A stand-alone entity is defined as a taxpayer that is not part of a consolidated group for financial accounting purposes and had no associated enterprise. The definition of "associated enterprise" encompasses any entity – and not company – which holds, directly or indirectly, more than 25% of the taxpayer. As a result, an orphan Luxembourg company held by a trust, a foundation or a *stichting* should not be considered as a stand-alone entity under the interest deduction limitation rule.

Financial undertaking: outside of the scope of the interest deduction limitation rule is any entity which falls within the definition of a financial undertaking (under article 168*bis* LITL). Included in this definition are, *inter alia*: (i) alternative investment funds in the meaning of AIFM Directive 2011/61/EU; and (ii) EU securitisation vehicles that fall within the scope of Article 2(2) of EU Regulation 2017/2402. With regard to the latter exemption, its current wording only covers STS securitisations.

3.5 If so, is there a "safe harbour" by reference to which tax relief is assured?

The only safe harbour rule is set out in the Circular n° 56/1-56*bis*/1 in relation to transfer pricing rules. The rule stipulates that for entities providing financial services to group companies and acting as a simple intermediary, a minimum return of 2% after tax is considered as a transaction performed at arm's length. It should be noted that the safe harbour rule applies only at the level of the Luxembourg tax administration, and other tax administrations may consider the transaction not to be at arm's length.

Also in the framework of the ATAD Law, the abovementioned limitation to deduct exceeding borrowing costs up to €3 million is considered as a *de minimis* rule.

3.6 Would any such rules extend to debt advanced by a third party but guaranteed by a parent company?

Debts guaranteed by a parent company (other than pledging the shares of the Luxembourg debtor to the creditor) are treated as a shareholder loan and as a result, in the absence of a transfer pricing report, the 85:15 debt-to-equity ratio will most likely be used.

3.7 Are there any other restrictions on tax relief for interest payments by a local company to a non-resident, for example pursuant to BEPS Action 4?

If the interest payments are not made at arm's length or are paid under a profit-participating debt instrument, there is a risk of re-classification of the interest payments as dividend payments, with the tax consequences set out above under question 3.4.

See also question 3.4 for further developments with regard to the interest deduction limitation rule as introduced under Luxembourg law since 1 January 2019.

3.8 Is there any withholding tax on property rental payments made to non-residents?

Luxembourg does not levy any WHT on property rental payments, whether they are made to non-residents or residents.

3.9 Does your jurisdiction have transfer pricing rules?

Luxembourg transfer pricing rules are embedded in the revised Article 56 and Article 56bis LITL, which incorporate the concept of the arm's length principle based on Article 9 OECD MC. The amended provision, however, goes further and reflects the spirit set out in BEPS actions 8–10, such as the concept of comparability analysis, and a GAAR that allows a transaction that has been made without any valid commercial or business justification to be disregarded.

On 27 December 2016, the Luxembourg tax authorities issued the *Circular n° 56/1-56bis/1*, which has reshaped the transfer pricing framework for companies carrying out intra-group financing activities in Luxembourg. The Circular provided additional guidance in terms of substance and transfer pricing requirements, in line with the OECD Guidelines. In particular, it provided substantial details on how to conduct the comparability and functional analyses in a way consistent with the OECD principles. Furthermore, the Circular requires the performance of a comprehensive risk analysis in order to determine the adequate level of equity capital.

4.1 What is the headline rate of tax on corporate profits?

As from the tax year 2019, income exceeding €200,000 is taxed at a rate of 17%. In addition, a 7% solidarity surcharge for the employment fund, and a 6.75% municipal business tax (“**MBT**”) for companies registered in Luxembourg City, are levied. For companies located outside of Luxembourg City, a different rate of MBT may apply.

The above amounts to an aggregate tax rate for Luxembourg-City domiciled companies of 24.94%.

Since 1 January 2019, two intermediary CIT rates have been introduced:

- 15% for taxable income up to €175,000, and
- €26,250 plus 31% of the tax base above €175,000, for taxable income between €175,000 and €200,000.

It is worth noting that in the past (from 1 January 2011 up until 31 December 2015) companies were subject to a minimum CIT in the amount of €3,210. However, since that provision was rendered as incompatible with the EU PSD, Luxembourg abolished minimum CIT and introduced a minimum net wealth tax as of 1 January 2016 which amounts to €4,815.

4.2 Is the tax base accounting profit subject to adjustments, or something else?

As a general rule, companies in Luxembourg follow Luxembourg general accounting principles (“**LuxGAAP**”) under which both upward and downward adjustments are allowed.

4.3 If the tax base is accounting profit subject to adjustments, what are the main adjustments?

Profits in commercial accounts differ from taxable profits mainly for the following reasons:

- tax-exempt profits (e.g. as per the participation exemption regime applicable for dividends and capital gains);
- add-back expenses (e.g. interest expenses on assets generating tax-exempt income);
- adjustment to the tax results from transactions that were not at arm's length (e.g. the interest rate set was not at market conditions, or interest payments were reclassified as hidden dividend distribution and hence no longer tax-deductible); and

- discrepancies between the application of different valuation rules in accounting and tax (e.g. amortisation, rollover relief).

Under certain conditions, a tax balance sheet may be prepared in a way which deviates from the statutory accounts.

4.4 Are there any tax grouping rules? Do these allow for relief in your jurisdiction for losses of overseas subsidiaries?

Luxembourg allows a group of companies to apply a fiscal unity (or tax consolidation). Under such regime, the respective taxable profits of each company in the consolidated group are pooled or offset to be taxed on the aggregate amount, which means that the group is effectively treated as a single taxpayer.

Generally, the conditions to qualify for a fiscal unity are as follows:

- each company that is part of the tax unity is a Luxembourg-resident, fully taxable company (the top entity may be a Luxembourg permanent establishment of a fully taxable non-resident company) (the “**Eligible Company**”);
- at least 95% of each subsidiary's capital is directly or indirectly held by an Eligible Company;
- each company's fiscal year starts and ends on the same date; and
- the fiscal unity is applied for at least five financial years.

The taxable income/loss of the fiscal unity is calculated as the sum of the taxable income/loss of each constitutive entity. The vertical fiscal unity regime has been extended since 1 January 2016 in accordance with the CJEU case law, in particular, to allow horizontal integrations. Eligible Companies (at least two Luxembourg companies) that are held by a common parent established in any EEA country and subject to tax comparable to Luxembourg's CIT in its country of residence are now also permitted to form a fiscal unity. Companies consolidated for CIT are also automatically consolidated for MBT. However, there is no tax consolidation for net wealth tax (“**NWT**”) purposes.

Securitisation entities and venture capital companies are excluded from the possibility to form a fiscal unity in order to prevent tax evasion schemes.

4.5 Do tax losses survive a change of ownership?

Companies resident in Luxembourg can carry forward their losses for 17 years if they are realised from the financial year closing after 31 December 2016 (before that, tax losses could be carried forward indefinitely; losses incurred between 1 January 1991 and 31 December 2016 are, however, grandfathered in) and offset them against any future profits if the following conditions are met cumulatively:

- the losses have not already been offset;
- the company has maintained proper accounting in the loss-making period; and
- the losses are offset by the company that incurred them.

Based on Luxembourg case law, companies should have a right to carry forward tax losses in case of change of ownership, unless an abuse of law has been established. Such condition should be interpreted in the meaning of corporate law and not solely on economic rationale. The right to offset the losses based on the hereinabove conditions should only be interpreted in light of the definition of a company based on corporate law. As a consequence, amendments to articles of association relating to sale of shares of the company do not lead to the creation of a new legal entity and hence do not prohibit that entity from the carrying-forward of losses.

However, application of the tax carry-forward may be denied if the transaction occurred purely for tax reasons; the so-called “*Mantelkauf*” theory.

It should be noted that the tax losses may be offset against CIT and MBT but not against NWT.

4.6 Is tax imposed at a different rate upon distributed, as opposed to retained, profits?

Luxembourg taxes retain and distribute profits in the same manner. However, distributed profits may be subject to withholding tax unless a domestic or treaty exemption applies. It should also be noted that undistributed profits may also be subject to NWT.

4.7 Are companies subject to any significant taxes not covered elsewhere in this chapter – e.g. tax on the occupation of property?

Yes, Luxembourg levies NWT on Luxembourg corporate tax residents. NWT is assessed on 1 January of each year on the basis of the estimated realisable value of the company's net operating assets (total assets minus total liabilities, the so-called unitary value). There is a possibility of reduction of the NWT up to the CIT paid for the previous fiscal year. NWT of 0.5% is levied on the unitary value of up to €500 million (inclusive) and 0.05% for the unitary value exceeding this threshold.

A minimum NWT of €4,815 is due by Luxembourg corporate taxpayers holding financial assets representing at least 90% of their total assets and having a balance sheet exceeding €350,000.

Exemptions are available for securitisation vehicles, SICARs, SEPCAVs, ASSEPs, and RAIFFs that invest exclusively into risk capital-related securities – which only pay the minimum flat NWT of €4,815. A Luxembourg resident company can also benefit from a NWT exemption on qualifying participations under the same conditions applicable for the participation exemption on dividend income, except that no minimum holding period is required.

5.1 Is there a special set of rules for taxing capital gains and losses?

In principle, capital gains arising from the sale of assets are treated as ordinary income and taxed as such, unless the participation exemption (as specified in question 5.2 below) applies.

5.2 Is there a participation exemption for capital gains?

Capital gains exemption is available under the following conditions. At the time the capital gains are realised:

- the Luxembourg company has held a direct participation representing at least 10% of the nominal paid-up share capital of its subsidiary (or if below 10%, a direct participation having an acquisition price of at least €6 million);
- it has held such qualifying participation for an uninterrupted period of at least 12 months; and
- the subsidiary entity is: (i) a Luxembourg-resident entity fully subject to Luxembourg income taxes; (ii) a non-resident capital company liable for an income tax in its country of residence comparable to the Luxembourg CIT; or (iii) an entity resident in a Member State of the European Union (as defined in Article 2 of the PSD).

It is important to note that the GAAR does not apply to capital gains deriving from qualifying subsidiaries benefiting from the Luxembourg participation exemption, regardless of their location.

5.3 Is there any special relief for reinvestment?

Yes, Article 54 LITL provides for a reinvestment relief if fixed assets consisting of a building or non-depreciable assets are disposed of during the course of operations, provided that certain conditions are

met. The purpose of this article is that the profit on the disposal of assets should not be taxed if the funds released are retained in the business and will be used to invest in other capital assets.

5.4 Does your jurisdiction impose withholding tax on the proceeds of selling a direct or indirect interest in local assets/shares?

Luxembourg does not impose WHT on the sale of a direct or indirect interest in local assets/shares, as such profits are taxed as capital gains.

6.1 What taxes (e.g. capital duty) would be imposed upon the formation of a subsidiary?

A €75 registration duty is due upon formation of a subsidiary; the same duty is paid in case its articles of association are amended.

6.2 Is there a difference between the taxation of a local subsidiary and a local branch of a non-resident company (for example, a branch profits tax)?

Branch is a corporate law term; therefore the classification of an entity/activities as a branch is not imperative for the determination of its tax treatment. Instead tax law uses the term *permanent establishment* to determine whether an entity is taxable in Luxembourg.

Branches and subsidiaries fall under the same tax regime. In addition, all transactions between the head office and the branch are disregarded for tax purposes, e.g. there is no WHT on any payments.

6.3 How would the taxable profits of a local branch be determined in its jurisdiction?

In principle, Luxembourg branches of foreign companies should be taxed the same way as resident companies (subject to the provisions of a relevant tax treaty), with the exception that transactions between a branch and a head office are disregarded.

6.4 Would a branch benefit from double tax relief in its jurisdiction?

It depends on the domestic law of the jurisdiction where the head office is located and the applicable double tax treaty. However, as a general rule, a permanent establishment is not considered as a resident under a tax treaty and cannot claim the benefits of such treaty on its own.

6.5 Would any withholding tax or other similar tax be imposed as the result of a remittance of profits by the branch?

No, transactions between the branch and the head office are not subject to WHT or any similar tax.

7.1 Does your jurisdiction tax profits earned in overseas branches?

As a general rule, in the absence of a double tax treaty, profits realised by an overseas branch would be included in the taxable basis of the Luxembourg head office (as it is taxed on its worldwide

income). However, within the framework of double tax treaties, Luxembourg generally exempts profits of a permanent establishment which are taxed in the other Contracting State.

It should be noted that profits of an overseas branch would not be subject to MBT, as this tax is applicable only to commercial activities carried on in Luxembourg.

7.2 Is tax imposed on the receipt of dividends by a local company from a non-resident company?

Yes, all dividends received from abroad are calculated in the taxable profits of a company.

Such income might be exempt under the applicable tax treaty or the domestic participation exemption.

Under the domestic participation exemption, dividend income (and liquidation proceeds) is exempt if, at the time the income is put at the disposal of the taxpayer:

- the subsidiary entity is (i) a Luxembourg-resident entity fully subject to Luxembourg income taxes, (ii) an entity resident in a Member State of the European Union (as defined in Article 2 of the PSD), or (iii) a non-resident capital company liable to an income tax in its country of residence comparable to the Luxembourg CIT;
- the Luxembourg company holds a direct participation representing at least 10% of the nominal paid-up share capital of its subsidiary (or if below 10%, a direct participation having an acquisition price of at least €1.2 million); and
- it has held (or commits itself to hold) such qualifying participation for an uninterrupted period of at least 12 months.

If the dividends are distributed by an EU subsidiary which is listed in Article 2 of the PSD, the exemption applies subject to the two additional conditions below:

- the EU subsidiary is not used for the main purpose or as one of the main purposes of obtaining a tax advantage that defeats the object of the PSD (GAAR); and
- the dividend/profit distribution from the EU subsidiary have not been deducted from its taxable base (anti-hybrid rule).

7.3 Does your jurisdiction have “controlled foreign company” rules and, if so, when do these apply?

CFC rules have been introduced into Luxembourg law as of January 2019 upon the implementation of the ATAD 1 with the above-mentioned ATAD law. The ATAD 1 CFC rules are the mere implementation of BEPS Action 3. In short, the CFC rule distributes to Luxembourg (i.e. under the jurisdiction of the controlling company) the income of a foreign subsidiary or permanent establishment 50% owned directly or indirectly by a foreign subsidiary or permanent establishment, if the effective corporation tax on the profits of that subsidiary or permanent establishment are less than half the CIT that would have been paid in Luxembourg. However, the rule excludes Luxembourg MBT from the scope of the CFC provisions.

8.1 Are non-residents taxed on the disposal of commercial real estate in your jurisdiction?

Yes, non-residents are subject to capital gains tax upon disposal of a real estate located in Luxembourg, as per domestic law. Such position might be overruled under double tax treaties signed with Luxembourg.

8.2 Does your jurisdiction impose tax on the transfer of an indirect interest in commercial real estate in your jurisdiction?

Luxembourg does not impose such tax unless the sale is done by a tax-transparent entity from a Luxembourg point of view; then the non-resident company directly above the tax-transparent entity is taxable on capital gains realised on the sale of the real estate in question.

8.3 Does your jurisdiction have a special tax regime for Real Estate Investment Trusts (REITs) or their equivalent?

No, Luxembourg does not have any special tax regime for REITs.

9.1 Does your jurisdiction have a general anti-avoidance or anti-abuse rule?

Luxembourg has GAAR embedded in its legislative framework (Article 6 *Steueranpassungsgesetz*, “StAnpG”), which applies to any Luxembourg taxpayer (capital companies, individuals and partnerships).

Specific GAAR were also introduced to implement the provisions of the Directive 2014/86/EC of 8 July 2014 amending the Parent-Subsidiary Directive introducing a GAAR on the participation exemption regime.

More recently, Luxembourg modified its existing GAAR under Article 6 StAnpG to align it with the GAAR provided for by the ATAD 1. According to the amended rule, a misuse of forms and institutions of law (i.e., an “arrangement”) which has been effected for the main purpose, or one of the main purposes, of achieving a tax advantage, and which is not commercially genuine, should be ignored. An arrangement is considered not to be genuine if it has not been put into place for valid commercial reasons which reflect economic reality.

However, one should remember that the GAAR are still subject to EU law and its interpretation by the CJEU. In this context, the CJEU *Cadbury Schweppes* case-law and the notion of wholly artificial arrangements should be taken into account when applying the GAAR.

9.2 Is there a requirement to make special disclosure of avoidance schemes?

In accordance with DAC 6 (the fifth amendment to the Directive 2011/16/EU as regards mandatory automatic exchange of information in the field of taxation in relation to reportable cross-border arrangements), cross-border arrangements indicating a potential risk of tax avoidance should be disclosed to the tax authorities. The directive entered into force on 25 June 2018, and must be introduced into national law by 31 December 2019. It is expected that this directive will be soon transposed by the Luxembourg legislator, as a draft bill was introduced on 8 August 2019 to the Parliament.

9.3 Does your jurisdiction have rules which target not only taxpayers engaging in tax avoidance but also anyone who promotes, enables or facilitates the tax avoidance?

According to DAC 6, intermediaries, i.e. persons who design, market, organise or make the arrangement available for implementation, are responsible for filing the information on report-

able cross-border arrangements to the tax authorities. National law may give the intermediary the right to a waiver from filing information if the reporting obligation would breach the legal professional privilege. For example, lawyers have a legal obligation to maintain professional secrecy under the Luxembourg Criminal Code. As per the draft bill, Luxembourg lawyers would be covered by the professional secrecy. However, in that event, they have to inform the other intermediaries adequately and concurrently therewith to provide the Luxembourg tax administration with certain information relating to the transaction to be disclosed, on an anonymous basis.

9.4 Does your jurisdiction encourage “co-operative compliance” and, if so, does this provide procedural benefits only or result in a reduction of tax?

A corporate entity may approach the tax administration and request an advance tax ruling, which constitutes a binding agreement with the tax authorities and a confirmation of the tax treatment.

10.1 Has your jurisdiction introduced any legislation in response to the OECD’s project targeting BEPS?

Luxembourg has implemented many changes to align its law with the BEPS Action Plan:

- Action 1: Implementation of the EU VAT directive addressing VAT on business to customers’ digital services.
- Actions 2–4: Implementation of ATAD 1, which deals with CFCs and interest-limitation rules, which have been implemented into Luxembourg law as of 1 January 2019 (hybrid rules under ATAD 2 are to be transposed into Luxembourg national law by the end of 2019, aiming to neutralise the effects of hybrid mismatch arrangements).
- Action 5: Luxembourg introduced a BEPS-compliant new IP box regime as of the fiscal year starting 2018.
- Action 6: On preventing the granting of treaty benefits in inappropriate circumstances. Action 6 will include minimum standards to combat contractual abuse.
- Action 7: Prevention of the artificial avoidance of permanent establishment status.
- Actions 8–10: Introduction of the new Article 56*bis* to the LITL (please refer to question 3.9 above).
- Action 12: As per the introduction into domestic law of DAC 6 (please refer to question 9.2 above).
- Action 13: Transfer pricing documentation as requested by the new transfer pricing rules (please refer to question 3.9 above); country-by-country reporting (“CbCR”) which is applicable in Luxembourg for financial years starting on or after 1 January 2016.
- Action 14: Luxembourg chose to opt for mandatory arbitration under the MLI, which will be improved due to the new BEPS-MLI.
- Action 15: Luxembourg signed the MLI.

10.2 Has your jurisdiction signed the tax treaty MLI and deposited its instrument of ratification with the OECD?

Luxembourg has signed and ratified MLI. For Luxembourg purposes, the MLI entered into force on 1 August 2019. Hence and as of now, each tax treaty signed with Luxembourg will have to be interpreted in line with the MLI, and the application of the MLI will have to be checked on a case-by-case basis.

10.3 Does your jurisdiction intend to adopt any legislation to tackle BEPS which goes beyond the OECD’s recommendations?

No, Luxembourg is implementing all the mandatory measures which derive from the EU Parliament initiative. However, as a competitive jurisdiction, it does not plan to impose measures that would go beyond other recommendations of the BEPS report. The interesting exception to that is the introduction of the mandatory binding arbitration, which is not required under the MLI instrument. Also, it is worth noting that the Luxembourg law on transfer pricing expressly makes reference to the OECD transfer pricing guidelines when interpreting the national law.

10.4 Does your jurisdiction support information obtained under Country-by-Country Reporting (CbCR) being made available to the public?

Yes, Luxembourg has transposed the EU Directive 2016/881 concerning automatic and mandatory exchange of tax information by the law of 23 December 2016 concerning the CbCR. The law requires the annual filing of a CbCR declaration by every ultimate parent company residing in Luxembourg for tax purposes (or a designated reporting entity). The CbCR must be filed within 12 months from the last day of the fiscal year in question. There is also an obligation to submit a notification stating whether the entity is either the ultimate parent of the group, a substitute parent or the designated reporting entity, and if it performs none of these functions, the notification shall clearly state the identity and fiscal residence of the reporting group entity no later than on the last day of the fiscal year of the group. The notification is submitted electronically.

Information obtained under CbCR is not public. In this respect, Luxembourg implemented measures to ensure the appropriate use of information.

10.5 Does your jurisdiction maintain any preferential tax regimes such as a patent box?

Yes, the law dated 22 March 2018 replaced the IP box regime that was abolished in 2016. In addition, the Luxembourg tax authorities published a circular on 28 June 2019, L.I.R. n° 50*ter*/1, clarifying the IP box. The Law introduced a new Article 50*ter* LITL that provides for an 80% exemption on income derived from the commercialisation of certain intellectual property (“IP”) rights, as well as a full exemption from NWT. The new rules are applicable as from the fiscal year 2018. Qualifying assets include the following IP rights:

- patents (broadly defined) and functionally equivalent rights that are legally protected by utility models, extensions of patent protection for certain drugs and phyto-pharmaceutical products, plant breeders’ rights, and orphan drug designations; and
- copyrighted software.

In line with the BEPS – Action 5 recommendations, marketing-related IPs can no longer benefit from the IP box regime.

Qualifying income includes the following:

- income derived from the use of, or a concession to use, qualifying IP rights (i.e. royalty income);
- IP income embedded in the sales price of products or services directly related to the eligible IP asset. The principles of Article 56*bis* ITL must be used to separate income unrelated to the IP (e.g. marketing and manufacturing returns);
- capital gains derived from the sale of the qualifying IP rights; and
- indemnities based on an arbitration ruling or a court decision directly linked to a breach of a qualifying IP right.

The regime applies on a net income basis, meaning that expenses relating to the qualifying IP assets need to be deducted from the gross qualifying income. The proportion of qualifying net income entitled to the benefits will be determined based on the ratio of qualifying expenditures and overall expenditures (nexus ratio). The previously-qualifying IP assets can continue to benefit from the old regime during the grandfathering period, running until 30 June 2021.

11.1 Has your jurisdiction taken any unilateral action to tax digital activities or to expand the tax base to capture digital presence?

No, as any digital service tax would be detrimental to the fiscal politics of Luxembourg.

Although France has now introduced a digital tax, such actions are not to be expected in Luxembourg.

It is worth noting that the Luxembourg VAT Authorities issued Circular n° 787 of 11 June 2018 to extend the VAT exemption

applicable to financial transactions to virtual currencies (which follows the CJEU's position in the *Hedqvist* case (C-264/14)).

Concurrently therewith, the Luxembourg direct tax administration issued Circular n° 14/5-99/3-99bis/3 of 26 July 2018 which classifies virtual currencies as intangible assets for CIT, MBT and NTW rather than a currency. It is an interesting point to note that the French and Luxembourg tax administrations have a diverging interpretation on the assessment of cryptocurrencies.

11.2 Does your jurisdiction favour any of the G20/OECD's "Pillar One" options (user participation, marketing intangibles or significant economic presence)?

Given the short period of time that has elapsed since the proposal in June 2019, Luxembourg has not particularly commented on any of the options. In general, Luxembourg was in favour of the taxation of digital giants. However, Luxembourg finance minister Pierre Gramegna said that the initiatives should be taken with the consensus of the OECD countries (or G20), so it is to be expected that Luxembourg might be in favour of the "Pillar One" options.



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