**Study on Aggressive Tax Planning**

*Specific contract No13 under FWC TAXUD/2012/CC116*

**Appendix 1 - Questionnaire to national tax experts**

**Filled in for Luxembourg**





**QUESTIONNAIRE**

**Luxembourg**

## Abbreviations

LIR – Loi concernant l’impôt sur le revenue (income tax law)

StAnpG – Steueranpassungsgesetz 1934 (Law on the modification of taxation)

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| --- | --- |
| Questions | Answers |
| *Corporate tax rate* | |
| 1. What is the standard rate of corporate income tax applicable for the fiscal year 2015? | 29.22 % (22.47% including 7% surcharge + averaged municipal business tax rate) |
| 1. Some states offer special offshore tax regimes, providing for corporate tax-exemption of certain mobile income types (e.g. royalty) from abroad. Does your MS offer such a tax regime? If yes, please briefly explain, including the conditions to be met. | No, there is no special tax exemption regime for certain foreign income in Luxembourg. |
| *Dividends received* | |
| 1. Is it possible for a company in your MS to receive dividends from a foreign company free of tax (or at a greatly reduced rate of tax, e.g. 95% tax-exemption)? | Yes. A full participation exemption regime and, where this is not applicable, a 50% exemption rule (from both corporate tax, and municipal business tax) apply. |
| 1. If yes to question 3: |  |
| 1. Does this apply regardless of the tax residence of the distributing company, e.g. Member State, treaty state, tax haven? | The full participation exemption (Art 166 LIR) regime applies if:   * The distributing company is subject to a tax comparable to the Luxembourg corporate income tax (tax rate of at least 10.5% and similar tax base), or * The distributing company is resident in an EU Member State and referred to in article 2 of the EU Parent-Subsidiary Directive.   The 50% exemption regime (Art 115 (15a) LIR) applies if:   * The distributing company is resident in an EU Member State and referred to in article 2 of the EU Parent-Subsidiary Directive, or * The distributing company is resident in a country with which Luxembourg concluded a tax treaty and that is subject to a tax comparable to the Luxembourg corporate income tax (as above). |
| 1. Does this apply regardless of the level of shareholding or voting rights held in the distributing company? | The participation exemption regime applies if the recipient holds, or undertakes to hold continuously, a minimum participation of 10% or with an acquisition price of at least EUR 1.2 million in the capital of the subsidiary during an uninterrupted period of at least 12 months.  The 50% exemption regime is not subject to any ownership requirements. |
| 1. Does this also apply if the dividends have been deducted by the distributing company in its taxable income? | Yes; there is no specific rule in Luxembourg tax law that links the taxation of dividends to their treatment in the source state. |
| 1. If yes to b, how will the recent amendment of Article 4 of the EU Parent/Subsidiary Directive, which requires Member States to tax dividends if they have been deducted by the subsidiary, affect your answer? | Luxembourg has not yet transposed the relevant amendment to the Parent/Subsidiary Directive. It is expected to do so before the deadline for implementation, which will affect the answer in a yet unpredictable manner. |
| *Dividends paid* | |
| 1. Is it possible for a company in your MS to distribute dividends to a foreign company without any withholding tax? | Yes (Art 147 LIR). |
| 1. If yes to 5, |  |
| 1. Does this apply regardless of the amount or percentage of shares, which the foreign company holds? | No. The participation exemption applies if the foreign shareholder company owns directly (or through a domestic partnership) a capital participation of at least 10% or a participation with an acquisition cost of at least EUR 1.2 million for an uninterrupted period of at least 12 months. (Art 147(2) LIR) |
| 1. Does this apply regardless of the tax residence of the foreign company, e.g. member state, treaty state, tax haven? | No. The participation exemption applies if the dividends are paid (directly or through a domestic partnership) to:   * A company resident in an EU Member State as referred to in article 2 of the EU Parent-Subsidiary Directive * A company fully subject to tax in an EEA country; * A company resident and fully subject to tax in Switzerland, without benefitting from any exemption; * A company fully subject to tax at a comparable level to Luxembourg in a country with which Luxembourg signed a tax treaty. |
| 1. Is the withholding tax exemption subject to a beneficial ownership requirement similar to that of the OECD model tax convention? | Yes (indirectly). The exemption applies to the “economic owner” as defined in Art. 11 *Steueranpassungsgesetz* and as interpreted by (German law inspired) doctrine, which is a similar criterion to the beneficial ownership concept found in the OECD MC. |
| 1. Is the withholding tax exemption subject to any other anti-avoidance requirements, e.g. based on substance of the recipient? If yes, please briefly explain. | While there is no explicit substance requirement in the relevant provision, the principle of applying tax laws in accordance with economic substance applies, which may result in disregarding formal recipients if they are not considered to be the true economic owner. |
| 1. Is any other tax levied upon a distribution of a dividend by a company in your MS? | No. |
| 1. Are dividend equivalents (typically a buy-back of shares, a capital reduction-payment or a payment of liquidation proceeds) treated in a similar way as dividends and subject to withholding tax when paid to a foreign company? Please refer to question 4 and 5 above. | Capital reductions, buy-backs of shares and payment of liquidation proceeds are normally not subject to withholding tax in Luxembourg. They may be subjected to withholding tax if they are not being made for genuine economic reasons (Art. 97(3)(b) LIR) |
| *Interest income* | |
| 1. Is interest income from a loan granted by a company in your MS to a foreign group member company taxable? | Yes. |
| 1. If such a loan is granted free of interest (i.e. on non-arm’s length-conditions), would the creditor company resident in your MS have to include any deemed interest income in its taxable income? When responding, please consider Model ATP-Structure no. 4 and assume that FinanceCo B is tax resident in your MS. | As of 1. January 2015, Art. 56 LIR provides that taxation of profits of related enterprises is to be ensured in line with the conditions that would prevail between independent enterprises. However, more detailed guidance on how this is going to be applied is still outstanding at this point, making it difficult to say what is going to happen in practice.  In principle, depending on the concrete structure, an interest-free loan will be recharacterised as equity contribution if no loan would have been provided by a third party in comparable circumstances. FinanceCo B would in that case be considered to make a hidden distribution to MNE Group in the amount of the appropriate arm’s length interest. Such hidden distribution would in principle be subject to withholding tax. |
| 1. Is it possible that an interest bearing financial instrument (hybrid loan) granted by a company resident in your MS to a foreign group member company could be qualified as an equity investment in your MS with the result that the return on the investment (treated as deductible interest in the state of the debtor company) is considered a tax exempt dividend or similar? When responding, please consider Model ATP-Structure no. 2 and assume that B Holdco is tax resident in your MS (regardless of the non-MS assumption in the description of the Model). | Yes. Luxembourg qualifies financial instruments and payments made under these in accordance with its domestic law, irrespective of the qualification of other countries. |
| 1. If yes to 11, |  |
| 1. Please briefly explain which requirements should be fulfilled. | Luxembourg considers financial instruments as debt or equity in accordance with the following criteria (the characterisation is based on a case-by-case analysis balancing the various elements):  Features for an instrument to be considered as equity:  – subordination of the instrument to the claims of all other creditors, including future creditors;  – repayment on the instrument possible only out of realized profits;  – the holder of the instrument has the right to participate in the company’s management;  – the company is thinly capitalized;  – return on the instrument cannot be paid if it would leave the issuer insolvent; an  – there are no creditor safeguards for the holder.  Features for an instrument to be considered as a debt:  – the return on the instrument is done by fixed or variable interest or the interest is computed at a specific rate;  – there are no conditions required for the payment on the instrument;  – the instrument is recorded as debt in the company’s books and records;  – the intention is to create a debt instrument;  – the holder of the instrument has usual creditor rights and there are realistic creditor safeguards provided to the holder;  – there are other alternative financial sources available |
| 1. How will the amendment of Article 4 of the EU Parent/Subsidiary Directive affect your answer? | As it has not yet been implemented in Luxembourg law, no clear answer can be provided.  In general, it can be expected that the result will be different to the extent that a given case is covered by the Parent/Subsidiary Directive. |
| *Interest costs* | |
| 1. Are inter-group interest payments on a loan granted by a foreign group member company tax deductible to a resident in your MS? | Yes. |
| 1. If yes to 13, |  |
| 1. Does the tax deductibility depend on how the interest income is qualified for tax purposes in the creditor’s state? If yes, please briefly explain. | No. |
| 1. In particular, would your MS still allow a tax deduction if the creditor state treats the corresponding interest income as a non-taxable dividend or similar, i.e. if the loan is a hybrid loan? When responding, please consider Model ATP-Structure no. 2 and assume that C Holdco is tax resident in your MS. | Yes. |
| 1. Is the tax deduction of interest cost on inter-group debt subject to any thin capitalisation-rules or other interest deduction limitations-rules? | Yes. |
| 1. If yes to 15 |  |
| 1. Please briefly explain the general scope and mechanism of the rules. | Interest is, in principle, deductible as operating expense. However, interest (like other operating expenses) relating to exempt income is not deductible up to the amount of related exempt income derived during the same year. Interest exceeding the amount of exempt income will be deductible, but subject to recapture in later years when additional exempt income is realised.  Consequently, interest paid during a year on a loan contracted to acquire a shareholding that qualifies for the dividend participation exemption is only deductible to the extent it exceeds the exempt dividends derived from the shareholding during the same year and may lead to a tax loss that can be carried forward indefinitely. The amount of interest deducted may, however, be recaptured in the case of sale of the shareholding under the capital gains exemption regime.  In case loans are granted by related parties  or such related parties have guaranteed repayment of obligations under loans taken up from third parties, and these loans are used to finance exempt assets (e.g. exempt participations, real estate assets located in treaty countries), a debt-to-equity ratio of at least 85:15 is generally required in practice. The interest payments related to the debt exceeding this ratio will be treated as dividends, i.e. be non-deductible and (in principle) subject to withholding tax at a rate of 15%. |
| 1. In particular, do the rules apply only to interest costs on inter-group debt or more generally to all interest costs? | Generally to all interest cost. |
| 1. Do the rules take into account the worldwide debt ratio of the group of companies? | No. |
| 1. In general, how effective do you consider these rules in countering ATP? When responding, please consider Model ATP-Structures 1 – 4 and assume that C Holdco, B Hybrid and OpCo are tax resident in your MS. | The lack of rules targeting hybrid mismatches may raise concerns with regard to the effectiveness of anti-avoidance rules. Luxembourg still relies primarily on general anti-avoidance rules and the arm’s length principle.  With respect to the debt-to equity ratio, it does not appear to be extremely effective. Under current guidance, it only applies in certain circumstances and cannot thus be considered to be a comprehensive rule. |
| 1. If a loan is granted free of interest (non-arm’s length-condition) by a foreign group member company, could a debtor company resident in your MS claim any tax deduction for a hypothetical (deemed) interest cost? When responding, please consider Model ATP-Structure no. 4 and assume that FinanceCo D is tax resident in your MS. Moreover, please explain whether any deemed deduction would be contingent on a corresponding adjustment in the foreign state. | In theory this would be possible, as Art. 56 LIR now provides a legal basis for downward as well as upward adjustments in accordance with the arm’s length principle. There is no contingency on the tax treatment in the other state. However, an interest-free loan provided by a company within the same group will likely be re-characterised as equity contribution, to the effect that no deduction would be available. |
| 1. Would the benefit of such a loan compared to a normal interest-bearing loan on arm’s length conditions be taxable to the debtor company in your MS? If yes, how? | This will depend on the source of the benefit. For example, if the creditor is the parent company, as the lack of interest charged is not considered to be an asset to be contributed to the company, in accordance with the German law concerning *Nutzungseinlagen*, the benefit would not be taxable. If the tax-free loan is provided by the subsidiary to the parent company, an arm’s length interest amount would be included in the profits of the parent company, but may be exempt in accordance with the participation exemption of Art. 166 LIR. |
| 1. Does your MS levy any withholding tax on interest payments? | Yes – but rarely. As a general rule, payments of interests to non-resident companies are not subject to withholding tax, with the exceptions of interest paid on certain profit sharing bonds (profit shares paid to a silent partner (*bailleur de fonds*) and payments made under debt agreements that provide for variable interest related to profits on top of fixed interest) – Art. 146(1) LIR & Art. 97(1) LIR.  In both cases, the rate of withholding tax is 15%. |
| 1. If yes to 19 |  |
| 1. What is the rate of withholding tax (ignoring tax treaties)? | See under 19. |
| 1. Are there special withholding tax rules for interest paid on a loan from a group member company? | See under 19. |
| 1. Does this apply regardless of the tax residence of the creditor company, e.g. member state, treaty state, tax haven? | Yes. |
| 1. In connection with an exemption, reduction or refund of withholding tax under a tax treaty or the EU Interest/Royalty Directive, is it common tax practice to apply a beneficial ownership requirement similar to that of the OECD model tax convention? | As the exemption described above results from the fact that domestic law does not provide for withholding tax, no beneficial ownership requirement is applied. The exemption relate to the type of payments made irrespective of the recipient.  Domestic law generally relies on the concept of the “economic owner”, although this will be effectively overridden by the “beneficial ownership” condition where a withholding tax exemption/reduction is based on tax treaties including that requirement to the extent that the recipient of payments is the beneficial owner (but not the economic owner). |
| 1. Is such exemption, reduction or refund subject to other anti-avoidance requirements? If yes, please explain briefly. | No. |
| *Allowance for corporate equity* | |
| 1. Does your MS offer any tax deduction for a notional (fictitious) interest cost on the share capital of a company? If yes, please briefly explain and include any anti-avoidance provisions. In particular, can the deduction be claimed against financial income? | No. |
| 1. Does your MS offer any tax deduction for dividends declared or paid? If yes, please briefly explain. | No. |
| *Royalty and other income from intangible property* | |
| 1. Please consider Model ATP-Structure no. 5 and assume that Company B is tax resident in your MS. Does your MS offer any preferential tax regime (compared to the standard corporate income tax) for income from patents and other intellectual property rights? If yes, please briefly explain its main scope, characteristics and any anti-avoidance provisions. In particular, can the preferential tax treatment be applied to income from patents or other IP which has not been developed by the taxpayer (company) itself? Must the company have its own substantial R&D activities? Can the preferential tax treatment be applied also to income from other taxpayers in your MS? | Yes, Luxembourg offers a preferential tax regime for income from certain IP. Such income (including capital gains from the sale of qualifying IP and deemed income from IP that is exploited by the owner himself rather than licensed) may qualify for an 80% exemption. The rules are contained in Art. 50bis LIR.  The provision includes patents, copyright on software, trademarks, designs, models and domain names that have been created (i.e. legally constituted) or acquired after 31/12/2007.  To qualify, IP does not have to be developed by the taxpayer, nor is there a requirement of further development. IP acquired from (directly) associated companies is, however, excluded. |
| 1. Can a company in your MS obtain R&D tax credits (typically enhanced tax deduction or tax refund) for costs incurred, e.g. in developing IP rights? | Yes. |
| 1. If yes to 24, |  |
| 1. Please briefly explain the requirements which have to be met, e.g. requirements for certain activity or successful development, etc. | Three credits are obtainable:   1. declining balance depreciation (available for physical assets other than buildings used by the business) 2. 80% special depreciation for specified investment in “clean technology” 3. investment tax credit of 12% for additional investments in depreciable tangible assets other than buildings (exceptions apply, e.g. for cars or short-lived assets) 4. additional investment tax credit of up to 7% (in addition to the credit described in 3)) |
| 1. Can such credits also be obtained for costs that are ultimately reimbursed by a group member company to the company in your MS? | In case of such reimbursement, which would effectively lead to a non-qualifying group company to benefit from the credit, the doctrine of abuse of law would result in disallowing the benefit from the credit (administrative court decision 33123C from 18 March 2014) |
| 1. Can a company in your MS transfer ownership of a patent, trademark or other IP right to a foreign group member company without incurring capital gains tax? When responding, please consider Model ATP-Structure no. 5 and assume that MNE Group is tax resident in your MS. Please also assume that the IP has no significant fair market value at the time it is transferred but it becomes highly valuable shortly (1-2 years) after. | No. Capital gains would be calculated on arm’s length basis; however, the company selling the IP may qualify for the 80% exemption on any gains. In case of previously deducted costs related to the IP that exceeded earlier profits, such costs would be recaptured at the point of sale. |
| 1. If no to 26, i.e. your MS would impose tax on the disposal, |  |
| 1. Is the relevant capital gains tax rate lower than the standard rate? | No, capital gains are taxed as income. However, in the specific case, the IP tax regime may apply as described (effective 80% exemption) |
| 1. Does taxation arise as a result of an anti-abuse provision or similar? | There are no specific anti-avoidance provisions that result in taxation. Arm’s length valuation applies. |
| 1. Would any R&D tax credits obtained in the past be reversed upon a disposal? | No, unless the above described recapture rule applies. |
| 1. Can a ruling confirming the value of the IP be obtained? | Generally yes; however, no rulings are currently being provided in the wake of the current investigation of the EU Commission into Luxembourg’s ruling system (also with respect to the IP tax regime) and the recent change of the procedure. |
| *Royalty and other IP costs* | |
| 1. Is royalty paid by a company in your MS to a group member company in another MS or for utilization of IP tax deductible? | Yes. Royalties are treated as deductible expenditures provided that the rates paid in respect thereof are reasonable and are not, in effect, hidden profit distributions. |
| 1. If yes to 28, |  |
| 1. Is the tax deduction dependent on whether the royalty income is taxed in the hands of the IP-licensor/IP-owner? | No. |
| 1. Are there types of royalty payments which cannot be deducted? | No. |
| 1. Does your MS levy any withholding tax on royalty payments? | No. |
| 1. If yes to 30, |  |
| 1. What is the rate of withholding tax (ignoring tax treaties)? | N/A |
| 1. Are there types of royalty payments which are not subject to withholding tax? | N/A |
| 1. In connection with an exemption, reduction or refund of withholding tax under a tax treaty or the EU Interest/Royalty Directive, is it common tax practice to apply a beneficial ownership requirement similar to that of the OECD model tax convention? | N/A |
| 1. Is the tax exemption/reduction/refund subject to any other anti-avoidance requirements, e.g. based on a test of the substance of the recipient? If yes, please explain briefly. | N/A |
| *Group taxation* | |
| 1. Does your MS allow for group taxation of local group member companies with the effect that profits and losses of different companies are set-off against each other? If yes, please briefly explain. (Please note that group taxation also includes other standard arrangements offered to replicate the benefits of group taxation, e.g. group contributions from a profitable company to a loss-making group member company). | Yes. Under the tax consolidation, each company participating to the regime has to determine its own taxable income on a stand-alone basis. The taxable income and losses of all the companies participating in the group are then aggregated and adjusted to take into account intercorporate dividends and transfers, and subsequently allocated to the parent company.  The parent company must be either a resident company fully subject to tax or a permanent establishment of a non-resident company fully subject to a tax comparable to the Luxembourg corporate income tax.  To qualify for tax consolidation, at least 95% of the subsidiary’s capital must be directly or indirectly held by the parent (article 164bis of the [LIR](http://online.ibfd.org.esc-web.lib.cbs.dk/linkresolver/static/cta_lu_abb_lir?WT.z_nav=crosslinks)). Subsidiaries indirectly held through a domestic transparent entity or through a foreign company fully subject to tax can be included in the consolidation.  Consolidation is also possible when the parent company holds less than 95% of the capital of the subsidiary, if the parent holds at least 75% of the capital of the subsidiary. In this case, the minority shareholders, representing at least 75% of the capital which is not held by the parent, must give their consent. In addition, the Ministers of Finance and Economics must deem the consolidation important for the structural improvement or expansion of the Luxembourg economy (article 164bis(3) of the LIR).  The consolidation is subject to permission from the tax authorities, granted upon joint application of the companies concerned, and must cover a period of at least 5 years. |
| 1. If yes to 32, is group taxation restricted in situations where a (holding) company has solely been inserted in connection with a leveraged acquisition of the operating company (so-called debt push-down)? When responding, please consider Model ATP-Structures no. 1 – 3 and assume that C Holdco and B Hybrid are tax resident in your MS. | No. |
| *CFC rules* | |
| 1. Does your MS apply CFC rules to foreign subsidiaries of a parent company in your MS? | No. |
| 1. If yes to 34, please briefly explain the rules and their scope. | N/A |
| 1. Please consider the attached Model ATP-Structures no. 1, 2 and 4 - 6. Assuming that MNE Group is tax resident in your MS, would your MS’s CFC-rules be applied to the structures? If yes, what would be the likely effects? | N/A |
| *Mismatch in qualification of legal entities* | |
| 1. Does your MS’s tax qualification of a foreign legal entity (e.g. a partnership) follow that of the foreign state, or does it apply its own criteria? Please briefly explain. When responding, please consider Model ATP-Structure no. 3 and assume that MNE Group is tax resident in your MS. | Luxembourg’s qualification depends on its own analysis of a foreign entity’s features under applicable corporate law, such as the existence of a board of directors independent of/responsible to shareholders, limited liability, fixed/variable capital, rules on distribution of profits, existence and criteria for a change of ownership of shares etc. (no fixed set of criteria, case by case analysis required) |
| 1. Does your MS apply rules to counter another state’s mismatch in tax qualification of a legal entity (company) resident in your MS? If yes, please briefly explain the rules and their scope. When responding, please consider Model ATP-Structure no. 3 and assume that B Hybrid is established and tax resident in your MS. | No. |
| 1. Does your MS apply rules to counter another state’s mismatch in tax qualification of a transparent entity (partnership or similar) in your MS? If yes, please briefly explain the rules and their scope. | No. |
| *Tax residence of company* | |
| 1. Based on domestic tax rules, without the application of any tax treaty, can a company incorporated in your MS be considered non-tax resident if its management and control is situated in another state? If yes, please explain under which circumstances. | No. |
| 1. If yes to 40, please consider Model ATP-Structure no. 6. Would the Structure work if Company B1 is incorporated in your MS but managed and controlled abroad in an offshore-state? | N/A |
| *Tax ruling practices* | |
| 1. Some states offer tax rulings (incl. so-called APAs) that confirm non-arm’s length-transactions or the amount of spread between interest or royalty income and cost in various international flow through-structures. As an example, please refer to Model ATP-Structure no. 1. Does your MS offer this form of tax ruling practices or APAs? | No. |
| 1. Do your local transfer pricing-rules allow for the stripping of income from a domestic company by taking away legal ownership of functions, assets and risks? In other word, is it accepted that relatively small amounts of the group’s income is taxed in your MS on the basis of low risk, few assets held and only few functions performed in your MS? | Yes, in accordance with existing OECD guidance on the application of the arm’s length principle, which has been explicitly implemented in Luxembourg law as of 2015.  Note that concrete administrative guidance on the application of the new provision to that effect is not yet available. |
| 1. Can a company in your MS obtain a ruling or APA that a) provides for tax exemption of profits considered to exceed an arm’s length-income or considered to have been left to the company by its shareholders (capital contribution), or b) provides for the deduction of deemed expenses that would have been due under arm-‘s length conditions? | As the law has recently undergone significant change and no administrative guidance has been issued, it is not clear at the moment whether such ruling can be obtained in practice. |
| *GAAR/SAAR* | |
| 1. Please consider Model ATP-Structures no. 1-7. Are you aware of any general or specific anti-avoidance rules or practice in your MS which could impede or counter the ATP objective of any of the structures? If yes, please describe briefly the scope of the rules/practice and how they could be applied to each of the structures. | Luxembourg applies a GAAR that is capable in principle of countering any of the structures to the extent that they cannot be justified by economic reasons other than taxation, i.e. where they are inadequate to achieve a genuine business purpose in the absence of a tax benefit and are thus considered to be “abusive”. (§ 6 StAnpG)  There are justified doubts, however, whether such GAAR can, by itself, effectively address all aggressive tax planning structures. |
| *Other ATP indicators* | |
| 1. Are you aware of any tax rules, tax practice or lack of tax rules (loopholes) – other than those discussed in the preceding answers - which could facilitate your MS’s role in ATP? If yes, please briefly explain. | No. |