Tax controversy series

Administrative court of appeal judgments on the classification of a company's activities / NACE

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On 5 March 2024, the Luxembourg administrative Court of Appeal (*Cour administrative, 5 mars 2024, n°49365C, 49366C and 49367C)* rendered a series of judgements (together, the "three cases" or the "cases"), all relating to the same issue surrounding the statistical classification of economic activities in the European Community ("NACE"[1]) code assigned by the National Institute of Statistics and Economic Studies of the Grand Duchy of Luxembourg ("STATEC"[2]).

In all those cases, the Luxembourg administrative Court of Appeal (the "**Court of Appeal**" or the "**Court**") confirmed the position sustained by the Luxembourg Administrative Tribunal (the "**Tribunal**"), which ruled that the NACE code attributed to the company by STATEC was consistent with its object, hence rejecting the taxpayer's claim to have it replaced for another NACE code, supposedly more in line with its activity[3]. These three cases share the same fact pattern: As they have been pleaded by the same attorney, supported by the same arguments from parties, and resulted in the same conclusion from the Court, they will be analyzed jointly in this article. Differences, where noteworthy, will be highlighted.

Summary of the cases

In those cases, the taxpayers were, respectively, two alternatives investment funds (AIF) under the legal form of a *société en commandite simple* (SCS), and one investment fund under the legal form of a *société en commandite spéciale* (SCSp).

The companies contested the NACE number assigned by STATEC:
- In both cases involving AIFs under the legal form of an SCS, the procedure consisted of two steps:
1. Taxpayers initially contested the initial NACE code assignation 64.301 referring to "Mutual funds" (*Fonds communs de placement (FCP)*), following which STATEC reclassified them into category 64.309 referring to "Other collective investment undertakings" (*Autres organismes de placement collectif*)
2. Once again, they challenged the new classification, and requested via email the reclassification of their company under the category 64.202 "Financial holding companies" (*Sociétés de participations financières*, "**SOPARFI**"), which would benefit from the annual flat-rate contribution to the Chamber of Commerce of EUR 350. STATEC, however, maintained its position this time, which gave rise to the current disputes.
- In the case involving the SCSp, the taxpayer contested its classification in the category 64.309 *Other collective investment undertakings*, claiming it should fall into the category 64.202 *Financial holding companies* instead, which STATEC denied.

The taxpayers subsequently requested the STATEC director to review their classification, but without success. As per the director's explanations, any funds that do not take the form of investment companies with variable capital (SICAV), investment companies with fixed capital (SICAF), investment companies in risk capital (SICAR), or mutual funds (FCP) - whether regulated or not - should fall under the category 64.309.

For the sake of entirety, the director also added that the mere holding of financial assets on the balance sheet's assets side would not be sufficient to be classified as a SOPARFI. It would also be necessary (among other requirements) that the majority of the holdings be held at over 50% and belong to a clearly defined group of companies – which, he observed, was not the case here.

The cases were subsequently brought to the Tribunal, which ruled in favor of STATEC. Unsatisfied with the outcome, the taxpayers respectively lodged an appeal to the Court.

Context of the decision

To put things into perspective, it is important to understand that the NACE code provided to each company by STATEC allows the Chamber of Commerce to compute the yearly contribution. All entities registered as commercial companies in Luxembourg are obligated to pay a yearly fee to the Chamber of Commerce, regardless of whether they have legal personality. The Chamber of Commerce contribution is generally computed based on the commercial profit of the companies (of year N-2). However, entities classified as SOPARFI under NACE 64.202 are eligible to pay a minimum lump-sum fee of EUR 350.

In addition to the above, the fact that several judgments related to the NACE classification were published on the same day confirms our impression that the issue of which category a company falls into (and consequently, the amount of the contribution it will ultimately have to pay to the Chamber of Commerce) is far from clear for corporate taxpayers. Several companies recently approached us regarding this matter, and while these decisions leave many questions unanswered, they nonetheless allow us to provide some pieces of information in response.

As confirmed by both courts, the companies' objects - as mentioned in their respective articles of association and referred to in their financial statements - should be the first element upon which STATEC should base its assessment. As these are public information, they are deemed to be accurate and up to date; thus, STATEC is not legally compelled to go beyond those items to further assess the companies' situation and assign a NACE code accordingly.

The judges dismissed the taxpayers' argument, which linked the regulation of 12 November 2010[4], article 14 of the Luxembourg income tax law ("**LITL**") and Circular LITL No. 14/4 of 9 January 2015, to demonstrate that they failed to generate any commercial income and insisted that they should have provided evidence of the SOPARFI activity they claimed to have. However, the claimants' failure to demonstrate this does not render the NACE attribution operated by STATEC right. In particular, we would also think that, based on the aforementioned legal texts, an unrelated AIF with the legal form of an SCS or SCSp should not have any commercial profits, as defined by the LITL, hence making NACE 64.309, for which the Chamber of Commerce contribution is based on a proportional rate on the basis of a tax base constituted by commercial profits, incorrect.

These decisions contrast with another one, also published in 2023, which the taxpayers attempted to rely on[5]. In this case, the dispute revolved around the amount of the contribution determined by the Chamber of Commerce. The taxpayer, which was an AIF under the legal form of an SCS, attempted to lower the amount of contribution it would be liable to, on the grounds of the absence of any commercial income. It did so successfully, as the Tribunal concluded that it was not established that the taxpayer generated income that could be classified as commercial profits within the meaning of Article 14 LITL. It consequently ruled that the amount of the plaintiff company's annual contribution - computed by the Chamber of Commerce – was incorrect.

Decision of the Court

The three cases are structured in identical fashion.

Regarding procedural matters, the Court of Appeal rejects the invocation of Article 9 of the Grand Ducal Regulation - dated 8 June 1979 - by the taxpayers. This article essentially imposes an obligation on administrative authorities to inform taxpayers of individual administrative acts that have a negative impact on a legitimately acquired administrative status. As per its provisions, a minimum period of eight days must be granted to them so that they may present their observations. The Court observes that the due process outlined in said article had been duly adhered to, given that the situation of the taxpayer had not been altered *ex officio* by the STATEC officers. Instead, the taxpayers were able to engage with STATEC and its director, which moreover, resulted - for two of the cases - in a change of the initial classification.

The Court then notes the argument raised by the taxpayers according to which their classification in the category *Other collective investment undertakings* directly subjects them to the degressive contributions of the Chamber of Commerce, calculated based on commercial profits:
- In the cases where the taxpayers were AIFs, they raise that, as per Article 14 LITL supported by its related circular of 2015, where an AIF is constituted in the form of a limited partnership or a special limited partnership, it would be deemed not to carry out a commercial activity due to not having a commercial purpose, but an investment purpose.
- In the three cases, taxpayers emphasize that they primarily engage in intra-group transactions, so there would be no dealing with third parties outside the group. Their activity, insofar as it consists of the collective investment of all funds available to it in a wide range of securities and assets, mainly in stocks and interests, as well as in the holding and management of these interests, would not constitute a commercial activity as it does not exceed the scope of private wealth management.
- In the three cases, they also argue that in order to be considered as engaging in a commercial activity (i.e., commercially tainted, *théorie de l'empreinte commerciale*), their general partner would be required to be a capital company holding at least 5% of its interest units, which is not the case as the latter hold less than 5% of its interest units.
- In the three cases, they also invoke the fact that their entities are limited partnerships, fiscally transparent, and therefore their income would not be taxable in their name but only at the level of their partners, who are not residents in Luxembourg.

The judge recalls that the litigious question is **whether STATEC had appropriately classified the taxpayer under the NACE code number 64.309 referring to *Other collective investment undertakings*.**

In line with STATEC's and the Tribunal's stance, the Court maintains that the object of the companies, as outlined in their respective articles of association, should be the primary indicator for the category in which they should be classified. It further sustains that, as those status aim to inform both shareholders and third parties, they are deemed to be accurate, and a more in-depth analysis from STATEC to determine whether the companies actually engage in a different activity that would allow them to benefit from a more favorable status, should not be expected. In the cases at hand, the Court notes that, based on the object of the companies as stated in their articles of association (which was corroborated by some of the notes in the annual accounts), it does not appear that their activity consisted primarily of holding financial interests in other companies.

It further rules, albeit arguably, that the question of whether a commercial profit is actually realized is "*completely*" unrelated to the decision of the STATEC director not to classify those entities under the category *Financial Holding Companies – Soparfi*.

The Court thus rejects the taxpayers' claims and confirms STATEC's NACE classification.

Following this judgement, our immediate recommendation would be to draft with care articles of association when establishing an SCS or an SCSp, in particular those relating to its object, bearing in mind the potential implications they may have later on the annual contribution due to the Chamber of Commerce.

As mentioned above, the outcome of the decision is surprising, given the fact that the Tribunal ruled the opposite in a similar case (as referred to above)[6], where the Chamber of Commerce's computation of the contribution was challenged. When juxtaposed, it seems that the conclusion to be drawn from those judgments is that:
- Unlike STATEC when defining the NACE classification of taxpayers, the Chamber of Commerce is not allowed to conduct a cursory examination of the taxpayer's situation. Instead, it is incumbent upon the Chamber of Commerce to meticulously ascertain the companies' commercial profits, upon which the computation of their contribution shall be based.
- On the other hand, given that STATEC is only required to conduct a superficial review of companies' activities (i.e., as indicated to third parties in its documentation published on the Luxembourg Business Registers (RCS)), the obligation to prove that its actual activity differs lies with the company itself.

The fact that no appeal has been lodged by the Chamber of Commerce in the above case[7] suggests that the latter does not contest the heightened requirement imposed upon it by the Tribunal.

As a result, although the two issues (i.e. challenge on the computation of the contribution or challenge on the NACE classification) may be linked, it appears important to consider these cases when drafting articles of association for such entities. Moreover, it is advisable, in the event of a dispute, to challenge the assessment issued by the Chamber of Commerce rather than the NACE classification made by STATEC.

Nevertheless, exercising caution and awaiting future case law to hopefully provide clarity on this matter is recommended. Given the increasing number of challenges, the wait should not be too long.

1) Standing for Nomenclature statistique des Activités économiques dans la Communauté Européenne
2) Standing for Institut national de la statistique et des études économiques du Grand-Duché de Luxembourg
3) Respectively, Administrative Tribunal, 20 July 2023, n°47313, 47314, 47315
4) Règlement de cotisation de la Chambre de Commerce du 12 novembre 2010.
5) Administrative Tribunal, 20 July 2023, n°46566.
6) Decision of the Administrative Tribunal, 20 July 2023, n°46566.
7) Decision of the Administrative Tribunal, 20 July 2023, n°46566.