Administrative Court of Appeal - Decision on exchange of information and legal professional privilege

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On 12 December 2024, the Luxembourg administrative Court of Appeal (*Cour administrative, 12 décembre 2024, n°48677Cb et 48684Cb*) (the "administrative Court" or the "Court") ruled that the provisions of §177 (2) of the Luxembourg General Tax Law (*Abgabenordnung*, "AO"), were not compliant with EU law and notably article 7 and article 52 (1) of the Charter of Fundamental Rights of the European Union (the "Charter") guaranteeing the confidentiality of legal advice given by lawyers.

Summary of the case

In the case at hand, the Luxembourg tax authorities received a request for an exchange of information from their Spanish counterpart based on the EU Directive on administrative cooperation in the field of taxation (the "**Directive**" or the "**DAC**")[1], regarding a Spanish taxpayer. This Directive establishes a comprehensive framework for the exchange of tax information among EU Member States. Complying with their request, the Luxembourg tax authorities issued an injunction decision ordering a Luxembourg law firm (which had advised the taxpayer in the past) to provide all available documentation and communications concerning the services they had provided to this taxpayer in connection with a restructuring operation under scrutiny.

The law firm however refused, arguing that it had acted as legal counsel of the group to which the taxpayer belonged, and that its legal professional privilege was protected based on §177 AO from communicating information concerning its client insofar as the services provided did not relate to tax matters. Further to several communications between the law firm and the Luxembourg tax authorities, the latter charged a fine to the former for failing to respond positively to the request for information. The law firm lodged an appeal seeking the cancellation of the decision, but it was deemed inadmissible *ratione temporis* by the administrative Tribunal on 23 February 2023[2]. A new appeal was subsequently filed with the administrative Court by the law firm.

In a first decision rendered on 4 May 2023[3], the administrative Court overruled the Tribunal's decision as it considered that the tax authorities had violated article 47 of the Charter (i.e., Right to an effective remedy and to a fair trial) as they failed to give the law firm access to the minimum information regarding the tax purpose for which the information was sought. The administrative Court further ruled that the sanction for such a violation was the suspension of the deadline for appeal, and hence considered the appeal admissible.

Regarding the dispute itself, the administrative Court observed that legal professional privilege was not defined in the DAC that the Luxembourg law had transposed, and that the domestic legislation did not provide any clear limitation in Luxembourg when considering the information that could be requested by the tax authorities from third party benefitting from such privilege. As the administrative Court questioned the compatibility of §177 AO with article 7 of the Charter protecting legal professional privilege, it opted to refer the case to the Court of Justice of the European Union ("**CJEU**") and requested a preliminary ruling regarding whether article §177 AO could be deemed compliant with the Charter.

The decision under review was rendered in light of the clarifications provided by the CJEU (CJEU, 26 September 2024, C-432/23).

Context of the decision

The exchange of information upon request procedure ("**EOI**") in the EU is based on the DAC and enables tax authorities from one Member State to request or provide information on identified taxpayers to tax authorities from another Member State. The EOI is aimed at addressing the tax-related complications resulting from the high mobility of taxpayers as well as the increasing number of cross-border operations carried out.

The transposition of the DAC in Member States' domestic laws and its application by their tax authorities (consisting notably of the requested tax authority's ordering a third party to provide "foreseeable relevant" information on specific taxpayers) regularly results in taxpayers and third parties who have been ordered to disclose information challenging those demands, both at national and EU level.

The Luxembourg rules on the EOI have already been challenged in the past on the grounds of its incompatibility with the Charter. In its early days notably, the requested tax authorities could only control the procedural regularity of the request, in contradiction with article 47 of the Charter. As a result of the landmark case "Berlioz"[4], the Luxembourg law of 25 November 2014 transposing the DAC was therefore amended, allowing the third party supposedly holding the requested information to challenge the injunction decision, hence requiring the domestic tax authorities to check whether the information requested by the tax authorities of the other Member State was foreseeably relevant.

In recent years in Luxembourg, most of the case law concerning the exchange of information upon request has revolved around the foreseeable relevance criterion. Despite the fair number of cases ending up being settled either by the Tribunal or the Court, the interpretation of this criterion by the administrative jurisdictions has remained constant. The case at hand deserves our attention as it challenges the legality of the Luxembourg law of 2014, this time in light of the provision of article 7 and article 52 (1) of the Charter. The CJEU acknowledges that the fundamental rights protected by the Charter are not absolute and that a limit in their exercise may be justified by the pursuit of public interest objectives, such as the effectiveness of fiscal supervision by Member States.

However, even though the CJEU took into account the general interest reason behind the exchange of information procedure, it made it clear that Luxembourg could not go beyond what was necessary to reach such an objective and that the restriction had to be proportionate.

As a consequence of the decision under review, §177 (2) AO is now unapplicable in the context of an EOI upon request from the Luxembourg tax authorities to a lawyer when falling within the scope the DAC. Hence it should be expected to be reformed sooner rather than later. It is up to the legislator to find the right balance to reconcile the safeguarding of the rights enshrined in the Charter with the continuation of effective cooperation between the Luxembourg tax authorities and those of other Member States.

Such an exercise may be tricky and, even though one may reasonably assume that §177 AO will be amended in a favorable manner for taxpayers and third-party lawyers alike, it should not, in our view, be interpreted as the final word on the matter. Not only is it uncertain at this stage to what extent the unlawful provision will be amended and whether such changes will be deemed sufficient to comply with EU law, the decision of the administrative Court is also likely to encourage those impacted by such procedures to further challenge its legality, invoking fundamental rights enshrined in the Charter. We will closely monitor developments regarding incoming reform in this area and what it means regarding the legal professional privilege of information holders.

Finally, this decision is also interesting from a strictly procedural point of view. Even though this is generally not the first approach that would come to mind when entangled in (pre-)litigation procedures with the tax authorities, this decision illustrates well that challenging the legality of the law itself may sometimes be a winning strategy.

Decision of the Court

The administrative Court requested a preliminary ruling from the CJEU to essentially **i)** clarify the scope of the protection of the communications between lawyers and their clients embedded in article 7 of the Charter and, **ii)** in light of those clarifications, to confirm whether the Luxembourg law on exchanges of information on request which transposes the Directive 2011/16 should be deemed in line with the Charter's provisions. As the CJEU ruled that the current §177 (2) AO constituted an infringement to article 7 of the Charter, the subsequent judgment of the Luxembourg administrative Court was also, unsurprisingly, viewed in that light.

Analyzing the provisions of §177 AO, the Court first observed that (1) provides for an attorney-client privilege which may be invoked as a defense against investigative measures conducted by the Luxembourg tax authorities. This legal professional privilege is general in nature as it may apply to all information related to the lawyer's clients, to the extent that such information has been obtained in the course of the lawyer's professional activity.

The Court highlighted however that the protection granted is not absolute, as §177 (2) AO introduces an exemption according to which legal professional privilege may not apply to information which would have been acquired by the lawyer while either:
1. Providing tax advisory services to the client; or
2. Representing the client in tax matters

In those two situations, the lawyer would be fully obligated to provide the requested information to the tax authorities, unless the information disclosed could potentially expose the client to criminal prosecution.

The administrative Court observed that the §177 (2) AO does not contain any restriction regarding the documents or information the tax administration may request from a lawyer. Although the injunction decision should in theory be successful only in limited cases, namely where the lawyer has provided advisory or legal representation services in tax matters to his client, the provision does not clearly specify which information, in those instances, should or should not be disclosed by the lawyer. In that regard, the Court pointed out that the only reliable limit on which the lawyer may rely to contest the injunction decision seems to be the foreseeable relevance criterion.

The Court reiterated the observation that made it opt for a preliminary ruling from the CJEU in the first place, outlining that this resulted from the current wording of the §177 AO that the legal professional privilege does not preclude the tax authorities from issuing an injunction decision in non-tax matters but rather constitutes a justification *a posteriori* for the lawyer not to comply with the request.

Considering that the CJEU concluded on the non-conformity of §177 (2) AO with article 7 and 52 (1) of the Charter, and based on the principle of the primacy of EU Law, the Court concluded the following:
- at least in the context of the exchange of information (based on the EU Directive 2011/16) the Court can no longer apply paragraph § 177 (2) AO as a legal basis for an injunction decision addressed to a lawyer;
- any limit to article 7 of the Charter should be mentioned in the local law (article 52 (1) of the Charter), and that currently § 177 AO does not provide for any particular limitation as to the nature and extent of the information that the tax authorities may require a lawyer to provide;
- hence, the only provision of domestic law that can be validly applied in the field of exchange of information in accordance with Articles 7 and 52(1) of the Charter, is §177 (1) AO.

Further to the above, the Court concluded on the cancellation of the litigious injunction decision as it had no legal basis in conformity with article 7 and 52 (1) of the Charter.

1) Council Directive 2011/16/UE dated 15 February 2011
2) Decision of the Administrative Tribunal dated 23 February 2023 n°48213
3) Decision of the Administrative Court dated 4 May 2023 n°48677C et 48684C
4) Decision of the CJUE dated 16 May 2017, C-682/15