

Tax controversy series

State of play of the Luxembourg tax environment and direction of travel

By Emilian LEBAS, Partner, Head of International Tax and Tax controversy & dispute resolution leader & Valentine PLATEAU, Manager, International Tax, KPMG Luxembourg

For about 15 years, tax has been a fast-paced area, and the tax environment in Luxembourg has therefore significantly evolved, especially recently.

On the one hand, this evolution is partly the result of initiatives taken by the European Union and the Organisation for Economic Co-operation and Development (OECD). The brand-new Pillar II law⁽¹⁾, which taxpayers and practitioners are currently trying to grasp, is a recent prime example of the increasing complexity of today's tax-related problematics. Beyond simply understanding the legal texts, it is also often challenging for taxpayers to navigate rules that are still being drafted and clarified by the OECD itself via a series of open-ended guidance, and be aware of all the subsequent tax obligations they are required to comply with.

On the other hand, the changing landscape may also be observed in a purely domestic environment, both at the level of the Luxembourg direct tax authorities (LDTA or ACD for *Administration des contributions directes*) in their interactions with taxpayers, and at the level of the administrative jurisdictions as the positions they take in the tax area sometimes give the impression of fluctuating.

In this article, we will highlight how these interactions between tax offices and taxpayers have evolved and attempt to identify emerging trends taxpayers and practitioners need to be wary of.

Post tax ruling era

Continuing a trend that began about 10 years ago and encouraged by high-profile decisions⁽²⁾ from European Union institutions, the granting of tax rulings has become rare in Luxembourg.

Tax Year	Total tax ruling granted by the ACD
2019	69
2020	44
2021	56
2022	46
2023	30

ACD, 2019-2023 annual reports, impotsdirects.public.lu

In comparison, the Luxembourg direct tax authorities granted close to 600 tax rulings in 2013, and more than 700 in 2014⁽³⁾. Overall, the number of tax rulings granted annually has decreased nearly 95% over the last ten years. The tax ruling practice, which used to be relatively common, has now become the exception, resulting in a noticeable increase in tax disputes.

The tax ruling procedure⁽⁴⁾, initiated by a request submitted by the taxpayer, enables the tax office to take a position regarding the tax treatment of a transaction (or series of transactions). Such a position would be binding on the tax office. However, these rulings are not easily obtainable as they remain contingent upon the taxpayer's commitment to execute the said transactions exactly as described. Consequently, any discrepancy observed between i) the facts and circumstances, and transactions, as presented to the competent tax office and on the basis of which the latter has issued its decision, and ii) the actual implementation could deprive the advance ruling of its binding effect on the tax office⁽⁵⁾.

In practice, advance tax agreements or tax rulings had the immense merit of clearly establishing the Luxembourg tax authorities' stance on certain topics and technical questions, promoting legal certainty and allowing taxpayers to organize their operations with a certain level of comfort, in accordance with these positions.

Additionally, these tax agreements typically led to preliminary discussions between the parties, thereby fostering mutual understanding and a certain level of cooperation between the tax administration and taxpayers. The gradual disappearance of this practice has thus contributed to blurring the tax authorities' positions on certain points from the perspective of the market and taxpayers in general, which, given the increasing complexity of current tax legislation, has led to a rising number of disagreements.

Tax audit – An emerging trend?

Conversely, tax audits (*contrôle approfondi*), whose frequency had decreased during the pandemic period, have been on the rise again since 2022. Given that they have proven to be an effective weapon based on the tax revenues they generate each year, we can expect



the Luxembourg tax authorities to rely on them more in the coming years.

The table below provides an overview of the number of tax audits concluded in recent years. It is important to emphasize that these figures represent only audits that have been finalized; a significant number of tax audits initiated and/or still ongoing during these years should also be taken into account.

Tax Year	Total tax audits closed	Tax increase	Total on-site audits closed	Tax increase
2019	33	4.128.339,25	14	4.768.186,19
2020	19	4.174.006,08	20	4.397.458,07
2021	16	5.923.330,56	40	3.449.271,52
2022	49	99.925.482,46	16	1.088.292,87
2023	48	1.351.188,27	2	20.436,00

ACD, 2019-2023 annual reports

The significant variation in tax revenue in 2022 mostly results from revisions relating to transfer pricing following the new legislation adopted, in line with the OECD's Base Erosion and Profit Shifting (BEPS) action plan.

To be fair, when appreciating the volume of additional taxes levied thanks to the increased number of tax audits, one should bear in mind that a significant amount of these audits have ended up in tax controversy cases in front of the administrative jurisdictions (first instance or appeal). In the Luxembourg direct tax procedure, the tax claim filed against a tax office's decision in front of the Director of the LDTA has in principle no suspensive effect, with only limited exceptions.

The same goes for the appeal against a negative decision from the Director of the LDTA on such a claim. In trivial terms, the general principle is therefore that a taxpayer has to pay first and can then try to challenge the decision they are not happy with. Based on the outcome of the ongoing tax controversy cases and the significant amount of taxes collected at stake, the final picture could theoretically be quite different from the one given by the above table. In principle, the LDTA enjoy complete discretion in the taxpayers they choose to audit, as the Administrative Court recently reaffirmed that they were not required to inform them regarding the reasons leading to their selection⁽⁶⁾. Hence, we would recommend being prepared for tax audits which are often complex, lengthy and stressful procedures. Depending on what the auditors are looking for, they may well last several months, if not more.

A recent study on this topic⁽⁷⁾ revealed that taxpayers (and sometimes even professionals) lack a clear understanding of tax audits and how they are conducted. One key issue is the general opacity of the procedures, with taxpayers usually unaware of their rights. Thus, in numerous instances, audited taxpayers have ended up either disclosing too much or not enough information, or not being informed in a timely manner of what their next move should be. Given the significant impact these procedures may have, it is, in our view, essential for individuals and corporate taxpayers targeted by a tax audit to seek assistance from experienced professionals who will be best equipped to protect their interests.

Tax Litigation – general overview/statistics

The litigation activity of the Luxembourg tax authorities, which had experienced a slight decline in the 2020-2021 period (mostly explained by the general slowdown caused by the COVID-19 pandemic) has started picking up again since 2022, even surpassing pre-pandemic levels. Overall, the Luxembourg direct tax authorities reported that the number of appeals submitted to their Director has steadily increased over the last decade, with a 57% rise between 2014 and 2023⁽⁸⁾. Thus, while around 1,200 administrative appeals were introduced in 2014, approximately 1,500 were lodged in 2018. In comparison, the Luxembourg

direct tax authorities reported having received around 1,700 and 1,800 claims respectively in 2022 and 2023.

In April 2024, a parliamentary question⁽⁹⁾ was put to the Ministry of Finance requesting certain details regarding these figures. The latter provided some interesting clarifications, helping to better contextualize the numbers and thus offer a clearer understanding of the evolution of tax-related litigation (both administrative and judicial).

Notably, the growing number of disputes is reflected, among other things, by a moderate but steady increase in the number of claims submitted to the Director of the LDTA involving multiple tax years (i.e., more than one tax year with respect to the same taxpayer). In other words, disputes increasingly seem not to be due to isolated errors in individual annual tax returns, but rather are the result of disagreements between taxpayers and tax offices on approaches or positions taken that are likely to be reiterated and have repercussions in subsequent returns.

Tax Year	Total number of appeals before the Tax Director ⁽¹⁰⁾	Appeals concerning more than one tax year
2018	1,503	275
2019	1,661	287
2020	1,388	231
2021	1,582	384
2022	1,710	363
2023	1,832	388
2024	592	53*

* The numbers for 2024 are provisional.

Table provided in the context of the Parliamentary Question No. 559 – *Chambre des Députés du Grand-Duché de Luxembourg (chd.lu)*

Such an increase has also led to a corresponding rise in the number of cases subsequently brought before the Administrative Tribunal. While the proportion of claims referred to the Administrative Tribunal has not increased in itself (around 15%), the absolute number of appeals has followed the same upward trend.

In April 2022⁽¹¹⁾, in response to a parliamentary question, it was however revealed by the justice minister, Sam Tanson, that in the vast majority of tax-related cases, the Luxembourg direct tax authorities were proven right by either the Administrative Tribunal or the Administrative Court. Among the 1,181 cases that were referred to either of the administrative jurisdictions between June 2018 and April 2022, taxpayers were successful in only 168 of them (14.2%). It is difficult at this point to interpret this situation, given that the increase in tax controversies is a relatively recent phenomenon. What is clear, however, is that all parties concerned, including but not limited to taxpayers and their advisers, have had to learn how to navigate certain aspects of the procedures and how best to approach tax disputes in general. Probably even more importantly, they have had to learn how to anticipate possible questions and challenges by the LDTA on tax positions taken in the tax returns and ensure adequate documentation and the preparation of defensive files. At the end of 2022, around 8,700 claims were still pending at the level of the Director of the LDTA (12). Although we do not have more recent figures, it seems unlikely that the number of claims pending at this level has significantly decreased since then.

The need for adapting the organizing and developing tax expertise also became clear to administrative jurisdictions themselves.

Recent changes in the administrative jurisdictions' organization and procedure

Acknowledging the need for greater tax expertise as tax litigation continues to grow, the Administrative Tribunal established a new chamber in September 2023 specializing in tax litigation. The purpose of this chamber is to have judges better equipped to address tax problematics effectively, as those cases often involve highly complex financial structures.

Although it is too early to draw any conclusions about the effect of such a reorganization, and whether it will impact case processing times in the long term, it clearly demonstrates the judges' intention to establish a level playing field in handling tax disputes which is in itself very positive. As mentioned previously, the complexity of tax rules has dramatically increased in the last 10 to 15 years and this trend has not yet reached its peak. With 2024 being the first year of Pillar 2 law implementation, there is no doubt that complexity and uncertainty in tax matters is going to reach a new level with a likely rise in future volumes of tax controversy and dispute resolution cases.

When it comes to procedures, one important recent development concerned the bill of law 8186, initially proposed in March 2023⁽¹³⁾ by the former Luxembourg government to modernize and (supposedly) simplify certain aspects around tax procedures. The bill of law 8186 had been put on hold for a few months after the change of Government, due to opposition from the State Council, as well as the upcoming elections.

Many tax practitioners have expressed their concern regarding the text in its initial version, which is the one proposed in March 2023. Generally perceived as one-sided (i.e., largely in favor of the LDTA) as it effectively weakens taxpayers' rights (in particular in the exercise of their right to appeal) while tightening their obligations, the bill of law 8186 has been criticized by many professionals, who have argued that it should be re-drafted in a more balanced way. Although one appreciates the need to defend the integrity of the domestic tax system against tax evasion but also against aggressive tax planning, one may also wonder whether such a law, if it were to be adopted, may not have a counterproductive effect, by contributing to a continued deterioration in the relationship between the LDTA and taxpayers and, more broadly, in trust in the fairness of tax procedures.

The newly elected Government has thus decided to split the bill of law 8186 into two distinct bills.

Bill of Law 8186A includes the less controversial provisions of the initial bill and was approved by the State Council on 22 October 2024. It is expected to be voted on before year-end.

On the other hand, bill of law 8186B, that contains inter alia the aforementioned debated provisions regarding taxpayers' rights, has not been amended yet and is still pending at the Chamber of Deputies. The Government has mentioned its intention to carry out a more thorough assessment of its provisions.

At the time of this article, it is not known which parts of the bill of law 8186B are intended to be adopted as is (if any) and which parts could potentially be abandoned or partially re-drafted (and, if so, how). Recent signals sent to the market regarding legal certainty have been quite positive, for instance the increasing number of administrative circulars⁽¹⁴⁾ and the declared intention to promote dialogue between LDTA and taxpayers and, possibly, to revivify the tax ruling practice. As the saying is, don't cry before you are hurt. Let's wait and see and not anticipate too much. It is important to emphasize though that these matters need to be resolved, even more so in a country like Luxembourg whose economy significantly depends on attracting foreign investments. Among other things, investors highly appreciate legal certainty as well as quick, efficient and predictable administrative procedures. Collectively, we should do everything we can to ensure that the system in Luxembourg continues to offer these qualities.

1) Law of 22 December 2023 on Global Minimum Tax, *Loi du 22 décembre 2023 relative à l'imposition minimale effective en vue de la transposition de la directive (UE) 2022/2523 du Conseil du 15 décembre 2022 visant à assurer un niveau minimum d'imposition mondiale pour les groupes d'entreprises multinationales et les groupes nationaux de grande envergure dans l'Union*, *Mém. A / J.O.G.D.L. n° 864/2023 du 22 décembre 2023*.
2) CJEU, 8 November 2022, joined cases C-885/19 P and C-898/19 P, Fiat Commission, 31 July 2017, joined cases T-816/17 and T-318/18, Amazon (overruled by GCEU, 12 May 2021, C-457/21 P).
3) ACD, annual reports for 2013 (p. 15) and 2014 (p. 21), *impots-directs.public.lu*.
4) Article 8 of the law of 19 December 2014 introduced a §29a into the amended General Tax Law of 22 May 1931 as amended ("Abgabenordnung" also referred to as "AO"), aimed at formalizing the procedure applicable to tax rulings issued in direct tax matters (*Loi du 19 décembre 2014 relative à la mise en œuvre du paquet d'avenir – première partie (2015) modifiant (inter alia) la loi générale des impôts modifiée du 22 mai 1931 (« Abgabenordnung »)*, *Mém. A / J.O.G.D.L. n° 257 du 24 décembre 2014*, p. 5475).
This provision also established a tax ruling committee. Further clarification was provided by the Grand-Ducal decree of 23 December 2023, §29a AO defines a tax ruling as a written position taken by the tax office officer concerning the interpretation of certain provisions of tax legislation currently in force and their

application to one or more specific and concrete operations that the taxpayer plans to carry out.
5) E. Lebas, La gestion fiscale des entreprises et ses limites, *Collection l'entreprise et l'impôt* sous la direction d'A. STEICHEN, Legitech, 21 December 2021 – see chapter 2, section 2.
6) Administrative Court, 14 November 2023, n°47754.
7) *Cahiers de fiscalité luxembourgeoise et européenne, 2023/2, Le contrôle fiscal au Luxembourg : récit d'une pratique méconnue (introduction et méthodologie)*, 8 December 2023, Fatima Chouche, p. 93-114.
8) ACD, 2023 annual report, p.134, *impotsdirects.public.lu*.
9) Reply to parliamentary question n°559 by Finance Minister, Gilles Roth, 6 May 2024, *chd.lu*.
10) Including both administrative claims under §228 AO and formal hierarchical appeal under §237 AO and §303 AO.
11) Reply to parliamentary question n°5955 by Justice Minister, Sam Tanson, 15 April 2022, *chd.lu*.
12) Geneviève Montaigu, *Le Quotidien*, 5 November 2023.
13) Bill of Law n°8186 of 17 July 2024 modifying the General Tax Law of 22 May 1931 as amended.
14) For example, Pillar II FAQ published by the tax authorities on 25 March 2024 on minimum effective tax rate, or Circular from the Director of the ACD L.I.R. n° 170/1, 170bis/1, I.C.C. n° 44, I.Fort. n° 55 dated 19 July 2024 (Tax treatment of a simplified liquidation or dissolution without liquidation).