

Luxembourg

Branch Reporters
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Summary

Implementation of the base erosion and profit shifting (BEPS) project and other similar types of initiative launched by the OECD and the EU in the past has always been received and handled proactively on behalf of the Luxembourg governing bodies.

More recently, and further to Luxembourg's presidency of the EU in 2015, the Grand Duchy undertook what could be seen as a leading role in fostering the advance of BEPS within the EU.

Being a country with a worldwide recognized financial centre, Luxembourg companies are often in a position where their services are considered in a cross-border manner and where international tax, inevitably, always comes to play.

In this context, Luxembourg is well aware of the impact that BEPS (adopted either at an OECD or an EU level) may have on companies located therein, each of them at different levels. This is the main reason why Luxembourg's positioning as to the overall BEPS initiative has been one of full support (both from a political as well as legislative perspective).

Notwithstanding this support, Luxembourg's exposure to cross-border exchanges also obliges the country to be an observer on how BEPS is implemented elsewhere in the world (for the unique reason that a coherent and synchronized implementation of BEPS will be – in the long run – the main guarantee of its healthy evolution and implementation).

In this sense, and backed up by a solid history of compliance with international standards, Luxembourg sees BEPS as part of the normal evolution of international tax rules and supports its implementation as a means to sustain and foster the development of its financial market.

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1. Overview

1.1. Priorities

A proper understanding of which items of BEPS concern Luxembourg needs to be tied in with the success of its financial services industry. Luxembourg was always a front runner in matters concerning cross-border exchanges, due to its geographic location, and also its stable and consistent political environment.

Openness to cross-border exchanges has been one of the key driving forces behind Luxembourg's growth since the 1960s.

The examples below are a token of the exponential growth of Luxembourg's financial services industry:

- the Luxembourg Stock Exchange (LSE) was the first to issue and quote a Eurobond in 1963 and by 1969 it was already issuing international bonds in their issuance currencies. Today, the LSE is home to 20 per cent of all internationally listed securities;
- given the rising amount of global capital flows since the 1960s, Luxembourg saw the establishment of clearing houses in Luxembourg as of 1970;¹
- Luxembourg was the location of the first European sharia compliant insurance company in 1983;
- in the 1970s, Luxembourg was home to 37 banks, to 108 in the 1980s, and currently recent statistics indicate around 143 banks having their presence in Luxembourg;²
- the first Luxembourg investment fund was launched in 1966 for the US market.³ Luxembourg was the first European country to implement the Undertakings for Collective Investment into Transferable Securities (UCITS) framework in its domestic legislation. Today, Luxembourg is the first country in the world in terms of cross-border fund distribution, and the second largest investment fund centre in the world after the United States with €3,500 billion of assets under management.

Today's Luxembourg financial centre is split into four main areas, these being (a) banking and insurance, (b) wealth management, (c) capital markets, and (d) fund industry/asset management.

The growth of Luxembourg's banking and financial sector, as explained above, has prompted the development of the full range of financial services in offering by the industry. On the other hand, this growth is not typical of a target investment country, or of a country known for any other equally relevant economic activity/sector.

BEPS affects – at different levels – every financial services industry market player.

Accordingly, Luxembourg stands as an early adopter of many changes related to BEPS, but also as a supporter of a wider coherent implementation thereof. The

¹ CEDEL was incorporated in Luxembourg in 1970 and after its merger with Deutsche Borse Clearing, gave rise to Clearstream.

² <http://www.abbl.lu/en/mediatheque/media?media=47>.

³ The United States Trust Investment Fund.

functioning and efficiency of the financial services industry which is directly affected by the BEPS initiative is therefore the main concern of Luxembourg.

Signs of similar initiatives and standards having been adopted in Luxembourg can be found long before 2013 (when the BEPS Action Plan first saw light). This is a relevant element to understanding Luxembourg's current positioning towards overall BEPS progress and implementation.

As the OECD clarifies, "The implementation of the BEPS package will better align the location of taxable profits with the location of economic activities and value creation, and improve the information available to tax authorities to apply their tax law effectively".

Luxembourg's alignment to pre-BEPS OECD standards can be seen from the following facts:

- as regards the standard of exchange of information on request (EOIR), Luxembourg is a member of the Global Forum on Transparency and Exchange of Information for Tax Purposes;⁴ Luxembourg has adopted the standard on EOIR since 2009 and was deemed compliant with phase I of the Global Forum's peer review. Later, in November 2013, by occasion of phase II of the forum's peer review, Luxembourg received a non-compliant status; the result of phase II of the Global Forum's peer review was seen by the Luxembourg government as a severe rating,⁵ but one that – regardless – needed quick amendment. And indeed, by October 2015, upon an updated peer review of Phase II, Luxembourg was considered largely compliant as to the implementation of this standard;
- regarding the standard of automatic exchange of information (AEOI) following the implementation of the EU Savings Directive into domestic law in 2003, Luxembourg agreed – in 2014 – to apply the AEOI on savings income paid to an EU resident as of 1 January 2015. In October 2014, Luxembourg is one of the first countries to sign the CRS Multilateral Convention on Mutual Administrative Assistance in Tax Matters (MCAA), having committed itself to carrying out the first AEOI as of 1 January 2017;
- Luxembourg's presidency of the Council of the European Union between July and December 2015, set as key priority "placing European competitiveness in a global and transparent framework".⁶

The report of the Luxembourg Presidency of the Council of the European Union notes that during the course of the Luxembourg's Presidency "the work on the OECD BEPS initiative ... was finalized. At the meeting of Finance Ministers and Central Bank Governors of the G20 in October, the results of the BEPS initiative and the pioneering role of the EU were welcomed. The progress made on the exchange of information under the Luxembourg Presidency was hailed as an example to be followed".

In its "Council conclusions on corporate taxation – base erosion and profit shifting", dated December 2015, the EU Council defined the specific BEPS action plans that could be implemented EU wide, through which specific legislative instruments (later giving rise to the so-called Anti-Tax

⁴ <http://www.oecd.org/tax/transparency/>.

⁵ The Luxembourg reply to this rating, which can be found on the last pages of the phase II report.

⁶ Report of the Luxembourg Presidency of the Council of the European Union, p. 10.

LUXEMBOURG

Avoidance Directive) and with which type of monitoring efforts. Luxembourg effectively initiated the path which led to the July 2016 agreement reached by the EU Dutch Presidency on the proposed text for the so-called Anti-Tax Avoidance Directive.⁷

Other measures taken to date which are parallel to BEPS intentions are the following:

- the introduction of a revised general transfer pricing (TP) rule applicable since 1 January 2015 in line with the OECD model tax convention;
- changes to some double tax treaties which could prompt situations of double non-taxation regarding land rich companies;
- the formalization of the advance tax analysis procedure, as well as the possibility of electronically filing tax returns.

Further, there were recent law changes which aimed at aligning to BEPS:

- the adoption into Luxembourg domestic tax legislation of the revised version of the EU Parent–Subsidiary Directive (foreseeing rules applicable – within the EU – to hybrid mismatch arrangements and anti-abuse provisions);
- the repeal of the existing IP box regime, possibly in anticipation of implementation of the nexus approach as per Action 5 (chapter 4);
- AEOI on tax rulings, implementing the EU Directive on the automatic exchange of rulings (which was inspired by BEPS Action 5);⁸
- an amending protocol to the US/Luxembourg double tax treaty proposed to the Luxembourg Parliament in June 2016;
- a bill of law submitted to Parliament on 2 August 2016 to enact country-by-country reporting (CbCR), implementing EU Directive 2016/881 on the provisions of BEPS Action 13; and
- the bill of budget for 2017 includes amendments to the existing TP provisions in order to bring them into line with BEPS Actions 8–10.

Based on the above, Luxembourg's positioning towards BEPS has the far-reaching objective of understanding the impact that BEPS implementation will have on the Luxembourg financial services industry and its players, specifically when the strength and efficiency of this sector in Luxembourg depends on the coherent and balanced alignment of all countries in their implementation of BEPS.

1.2. Participation

The attributions of the Luxembourg direct tax authorities (*Administration des contributions directes*) comprise the determination and collection of taxes, the negotiation and development of double tax treaties, and also the representation of the Grand Duchy of Luxembourg at the different international working groups from the EU and the OECD.⁹

⁷ The existence of a specific reference in the directive to a monitoring procedure for the purposes of BEPS implementation is often credited to Luxembourg: http://taxandaccounting.bna.com/btac/display/batch_print_display.adp.

⁸ Law of 23 July.

⁹ <http://www.impotsdirects.public.lu/profil/index.html>.

Individuals from the Ministry of Finance observed the policy discussions on these action plans, but there is no written or public record of such meetings.

The Luxembourg Minister of Finance fostered most of the public interventions in Luxembourg.

The institutional and political role Luxembourg played in maintaining and promoting the overall progress of BEPS on the occasion of the 2015 Luxembourg presidency of the European Council was, to the best knowledge of the reporters, not followed up with any other specific – technical – involvement at the level of the OECD regarding any of the BEPS action plans.

Noteworthy interventions of the Luxembourg government which occurred between the date of this report and the launch of the BEPS initiative in 2013, are the following:

- on the occasion of the ECOFIN meeting in Brussels, Prime Minister Bettel reiterated on 20 December 2013 his support for the overall implementation of the standards of transparency noting that Luxembourg's "objective is clear: achieving an automatic exchange as an international standard, in order to assure the same conditions to all great financial places from an international perspective";
- at an ECOFIN meeting in November 2014, Pierre Gramegna supported the changes to the EU Parent–Subsidiary directive in line with BEPS Action 2 by stating that "the result of the application of today's international, European and national law can sometimes lead to a result where companies are confronted with a very limited tax-rate, or even to non-taxation. ... This is the reason why our country has been actively participating to the works of the OECD, specifically the BEPS procedure with its 15 working groups";
- during the course of two publicly known visits to Luxembourg of Mr Pascal Saint-Amans, director for Tax at the OECD – 11 December 2014 and August 2015 – Mr Gramegna outlined Luxembourg's support to the overall BEPS projects, its willingness to address the sometimes morally questionable granting of tax rulings by European countries and the advancement of the BEPS project at EU level as one of the main objectives of Luxembourg's presidency;
- by the time the BEPS final reports were issued (5 October 2015), Mr Gramegna also outlined that "Le Luxembourg tient à ce que les nouvelles règles soient transposées par tous les États, dans le but d'établir un véritable 'level playing field' mondial en matière de fiscalité des entreprises" and, in an interview with Luxembourg newspaper *L'Écho* on 6 October 2015 that "la taxation est ma priorité numero un".

To the best knowledge of the reporters there is no public register of any specific statement or area of collaboration from the tax authorities to any BEPS working groups.

The Luxembourg government has not launched any specific public consultation on the OECD BEPS initiative.

1.3. Domestic context

The following are the measures that provide for tax relief for foreign investment promotion in Luxembourg:

LUXEMBOURG

- exemption on non-resident capital gains tax: any gain realized on the sale of shares held in a Luxembourg company by a non-resident are only taxable¹⁰ to the extent that such shares represent more than 10 per cent of the issued share capital of the Luxembourg company, and the sale occurs at a gain within six months of its acquisition. Gains of non-residents in respect of investments in venture capital companies (SICAR), private wealth management companies and any regulated Luxembourg investment fund vehicles are also not taxable in Luxembourg;
- tax credit for investment: Luxembourg offers tax credits for eligible assets that primarily consist of depreciable tangible goods other than buildings, livestock, deposits (fossil or mineral) and vessels operating in international traffic. Such tax credits are available under specific conditions;
- withholding tax (WHT): under domestic tax law, Luxembourg does not levy withholding tax on cross-border interest payments;
- WHT exemption on dividend distributions: Luxembourg levies a 15 per cent withholding tax on dividends; however, no tax is withheld where dividends are paid to a qualifying company under the EU Parent–Subsidiary Directive. Luxembourg has extended the benefit of this regime to Swiss capital companies subject to corporate income tax with no possibility of exemption, EEA capital companies and corporations located in a treaty country that are subject to a tax similar to the Luxembourg corporate income tax. As from 1 January 2016 the WHT exemption under the participation exemption regime will be denied if the transaction qualifies as an abuse of law following the common EU anti-abuse rule;
- Luxembourg does not levy WHT on royalty payments, service fees or liquidation proceeds;
- Luxembourg does not levy a branch remittance tax;
- distributions made by regulated investment vehicles are not subject to WHT;
- intellectual property (IP) box regime: until 1 July 2016, Luxembourg offered an IP regime. The provisions in Luxembourg law relating to the domestic IP regime were repealed, although “grandfathering” rules apply up to 2021, subject to the fulfilment of certain conditions.

Some of the measures described above originate from Luxembourg’s implementation of EU directives into domestic law, and so have not raised specific controversies.

Article 50*bis* of the Luxembourg Income Tax Law and paragraph 60*bis* of the Luxembourg Valuation Law provided for a partial exemption for income/gains and net wealth tax exposures, derived from certain IP rights.

Country tax regimes in the OECD started being analysed as of 2010. The reviews were based on the OECD 1998 report¹¹ as well as newly developed factors stemming from the BEPS Action Plan.

Since BEPS was launched, the review has extended to OECD countries as well as to G20 countries (under the same reviewing body, the Forum on Harmful Tax Practices (FHTP)).

¹⁰ Absent any possible use of any double tax treaty concluded by Luxembourg which allocates the right to tax capital gain on shares to the country where the beneficiary of the gain is tax resident.

¹¹ <http://www.oecd.org/tax/transparency/44430243.pdf>. The 1998 report identified four “key” factors and eight “other” factors used to identify whether a regime is preferential.

As regards Luxembourg, the FHTP works identified the Luxembourg IP box regime as a harmful tax practice.¹² Indeed, as depicted in Table 6.1 of the BEPS Action 5 final report (pp. 63 and 64), all the IP regimes which are included therein were “considered under the criteria in the 1998 Report as well as the elaborated substantial activity factor. Those regimes are inconsistent, either in whole or in part, with the nexus approach¹³ as described in this report.”

BEPS Action 5 (and specifically in what regards its chapter 4 on “Revamp of the work on harmful tax practices: substantial activity requirement”), sets out a “minimum standard” based on agreed methodology to assess whether there is substantial activity in a preferential regime.

Luxembourg has not – to date – formally adopted the “nexus approach” as indicated by chapter 4 of BEPS Action 5.

However, the Luxembourg government presented the country’s state Budget draft law to Parliament on 14 October 2015 and it included a proposal to repeal the existing IP box regime. In terms of timeline, these measures were taken in a synchronized manner with the issuance of the reports on BEPS Action 5 (the Luxembourg 2016 Budget law proposal was presented to the Luxembourg Parliament on 14 October 2015 and the final BEPS Action 5 report was issued a mere nine days before that date on 5 October 2015).

Consequently, the Luxembourg IP box regime ceased to apply as from 1 July 2016 for the purposes of Luxembourg direct taxes and will cease to apply for Luxembourg net wealth tax purposes as of 1 January 2017.

The transition period which was suggested by some EU countries and later endorsed by the OECD and the EU on the final report of BEPS Action 5 was admitted, which means that until 30 June 2016, taxpayers who create, acquire or definitely improve qualifying IP rights before 1 July 2016 will be able to continue to benefit from this regime until 30 June 2021.

As regards other measures, no specific controversy has been raised.

Luxembourg undertook to understand and analyse the overall context and way in which BEPS is implemented in the largest world economies, as its financial services sector is to a great extent connected to it.

Luxembourg unregulated vehicles are often used as investment platforms for worldwide investments and by a range of different investors. These investments often involve the use of entities or instruments which may receive a distinct qualification under the tax and corporate law rules of both countries, therefore potentially qualifying as hybrid mismatch arrangements in the sense of BEPS Action 2. Luxembourg adopted the changes to the EU Parent–Subsidiary Directive on hybrid mismatch arrangements within the EU. An extension of that rule to non-EU countries is not yet foreseen.

Today, Luxembourg is recognized as being the largest investment fund hub in Europe. The magnitude of this sector in Luxembourg has been raising quite significant concerns and discussions with regard to the interpretation to be given to

¹² The SICAR as well as the SPF regime were also investigated but later concluded as being non-tax harmful regimes.

¹³ According to p. 14 of the Explanatory Statement for BEPS issued by the OECD on the 2015 final reports “OECD/G20 Base Erosion and Profit Shifting Project – Explanatory Statement” – “In the context of IP Regimes, such as Patent boxes, consensus was reached on the ‘nexus’ approach.”

LUXEMBOURG

BEPS Action 6, notably with regard to treaty eligibility for collective investment vehicles. In Luxembourg, the Association for the Luxembourg Fund Industry has been leading this discussion and participating in public consultations launched by the OECD on this end.

In the context of Action 6, the insertion of a full limitation on benefits (LOB) clause can further imply that Luxembourg companies quoted and traded in any worldwide “recognized stock exchange” may no longer benefit from double tax treaties.

1.4. Taxpayers’ rights and risks

The peculiar constitution of Luxembourg’s economy – mostly based on cross-border financial services exchanges – will imply that the contributors to such market sectors will be the main parties affected by the implementation of BEPS. The focus and attention that Luxembourg has been granting to a coherent implementation of BEPS is therefore quite understandable in these circumstances.

To date, the implementation of BEPS in Luxembourg has only been done further to the implementation of EU directives into domestic law.

Taxpayers in Luxembourg which decided to argue against this implementation into domestic law – and motivated by any specific infringement of EU law by Luxembourg – would be offered all the defence mechanisms available in the EU in such instances, notably by being given access to the EU Court of Justice to lay their claims.

Some BEPS action plans could be viewed as being in contradiction with EU law and its fundamental freedoms, especially the freedoms of establishment and the free movement of capital.¹⁴ In this context, the ECJ has in the past challenged the enforcement of LOB clauses.¹⁵

The ECJ could therefore challenge the compliance of the Anti-Tax Avoidance Directive with EU treaties, but also treaties entered into in order to implement BEPS Actions 6 and 7 (given that any non-EU treaties entered into by an EU Member State must comply with EU law).

Luxembourg has been taking a coherent position on the implementation of BEPS, notably by only implementing BEPS when EU directives on these matters are duly concerted and approved at a European level, and by watching closely the developments on BEPS implementation in other countries.

It is the reporters’ belief that the Luxembourg government is also aware that a too hasty and ill-advised implementation of BEPS may cause serious damage to the Luxembourg financial services industry, mostly due to difficulty in compliance and potential commercial distortions in a post-BEPS era.

Given that Luxembourg’s financial services industry is significantly involved in cross-border exchanges, a post-BEPS implementation era will certainly generate concerns as regards compliance with newly adopted standards (which may be to some extent different standards depending on the countries with which relations are established).

¹⁴ *Itelcar* C-282/12 – 3 October 2013, SGI C-311/08.

¹⁵ Act iv GLO C-374/04.

To some extent, the difficulties in addressing these upcoming risks should be hedged (if not totally eliminated) by BEPS Action 15 and the negotiation of a multilateral treaty.

2. Responses to BEPS measures

2.1. Responses to mainly domestic action items (Actions 2–5)

2.1.1. Identification of priorities

All BEPS “mainly domestic action items” gravitate around and affect Luxembourg’s financial services sector and therefore, as such, have warranted the attention of the Luxembourg government.

Action 2 and Action 5 (chapter 4) were given more priority. This is due to the fact that – historically – Luxembourg was never an “investor” country (concerned about tax deferral mechanisms and thus implementation of controlled foreign company (CFC) rules) nor an “investment” country (concerned about significant FDI inflow and thus adoption of mechanisms able to address significant base erosion of the Luxembourg taxable base). This prioritization is not expected to change as Actions 3 and 4 are now well within the accepted version of the Anti-Tax Avoidance Directive (i.e. timing for implementation will follow the EU action plan and it is not foreseen that these action plans will be extended to other non-EU countries at any time soon).

Concretely, Action 2 has been implemented into domestic tax law but its reach is only EU wide. A non-EU implementation of the action plan is not yet foreseen.

The nexus approach, proposed in chapter 4 of BEPS Action 5 as the proxy most suitable to link tax benefits to profit-generating activities, has not yet been implemented into Luxembourg domestic tax law. However, the Luxembourg IP box regime (having been deemed as tax harmful by the OECD) was repealed with effect from 1 July 2016.

Study and interpretation of the impact of these measures were made in line with domestic law procedures involving the mandatory parties (notably the *Conseil d’Etat* as well as the *Commission des Finances et du Budget*, where applicable, were duly consulted).

On matters related to Actions 2, 3, 4 or 5 no specific tax legislation existed which was in line with the changes being currently proposed.

Luxembourg has so far implemented Action 2 (mainly focused on hybrid rules for EU countries) into domestic law, following the revised version of the EU Parent–Subsidiary Directive. To pave the way towards a likely implementation of the nexus approach, Luxembourg repealed (effective as of 1 July 2016) the previously existing IP box regime.

LUXEMBOURG

2.1.2. OECD participation

Individuals from the Ministry of Finance or the Luxembourg tax authorities observed or participated in policy discussions on these action plans, but there is no written or public record of such meetings.

To the extent of the knowledge of the reporters, no persons from Luxembourg drafted, reviewed drafts, or assisted in other capacities in the formulation of the relevant BEPS Action Plan.

2.1.3. Public consultation

To the extent of the knowledge of the reporters no officials from Luxembourg promoted or participated in public discussions about the topics underlying these action plans (whether the prioritized items or otherwise).

With respect to the actual implementation of the revised version of the EU Parent–Subsidiary Directive no specific attention point to any controversial item was raised.¹⁶ The adoption of the anti-hybrid rules raised some discussion from the *Conseil d'État*.¹⁷ However, the clause was finally adopted and it is currently in application.

As regards the repeal of the IP box regime reactions from the *Conseil d'État* were of concern as to the repeal without a replacement regime, notably in presence of similar regimes that exist in the EU and which could affect Luxembourg's competitiveness.¹⁸ No further stances were taken on this to the best knowledge of the reporters.

No policy guidance has been issued by the government on any of these topics.

Since 2013 on many occasions, during the past three years, there have been public discussions on BEPS. These took mostly the form of preliminary impact assessments for the financial services industry made by tax practitioners in Luxembourg, typically with the participation of asset managers, banks and representatives of industry associations such as the ALFI,¹⁹ the LFF,²⁰ the LPEA²¹ and the ABBL.²²

¹⁶ The *Exposé de Motifs* notes that “L'utilisation d'instruments financiers hybrides qui ont à la fois des caractéristiques de dette et de capitaux propres a été identifiée comme un outil permettant aux entreprises d'obtenir un avantage fiscal injustifié”.

¹⁷ The *Conseil d'État* notes that “d'après le Conseil d'État, les règles contenues dans l'actuel paragraphe 6 de la loi ... pourront être considérées comme étant suffisantes et équivalentes aux dispositions de la clause générale anti-abus de la directive 2015/121/UE que le projet sous examen vise à transposer afin d'éviter de transposer en droit interne des définitions qui risquent de conduire à une situation d'inécurité fiscale et juridique pour les contribuables. Il s'impose de rappeler à cet égard que lorsque les objectifs fixes par une directive sont déjà atteints de façon non équivoque par des textes normatifs nationaux existants, il n'est pas requis de recourir à un texte nouveau dans le but de transposer cette directive.”

¹⁸ According to the *Conseil d'État* “les conséquences d'une telle abrogation sur l'activité de l'économie luxembourgeoise, notamment au regard de l'existence de régimes fiscaux similaires existant dans d'autres États membres de l'Union européenne, doivent être examinés avec soin”.

¹⁹ The Association of the Luxembourg Fund Industry.

²⁰ Luxembourg for Finance.

²¹ Luxembourg Private Equity & Venture Capital Association.

²² The Luxembourg Bankers' Association.

The discussions were organized mostly by top-tier tax practitioner firms. Professionals facilitating on such occasion were senior management representatives. The audience was usually composed of industry experts whose companies are expected to be exposed and affected by BEPS (i.e. typically asset managers, fund managers and banks with regard to their alternative investment strategies).

To the best knowledge of the reporters, the content of this type of document was never reflective of a significant legal or empirical analysis of BEPS, but rather a high level review and assessment.

The existence of wide public discourse on the matter of BEPS could have allowed the public sector to further define the course of action on BEPS implementation.

2.1.4. Post-BEPS processes and early assessments of progress to date

To date, and to the best knowledge of the reporters, the only processes identified as necessary to implement action plans on these topics were the European ones.

As far as Action 2 is concerned, progress has yet to start on implementation for non-EU countries. This is not expected any foreseeable time soon. As regards Action 5, a revamp of the former IP box regime is to be expected soon.

Actions 3 and 4 are expected to be implemented only further to adoption of the Anti-Tax Avoidance Directive into domestic tax law.

No controversies have arisen that have involved judicial review or alternative dispute resolution mechanisms.

Aside from the revised EU Parent–Subsidiary Directive encompassing the hybrid rules between EU countries and the repeal of the IP box regime, regarding Actions 3 and 4 there were no BEPS-related rule changes passed in Luxembourg during the BEPS consultation process that exist due to the initiation of BEPS.

Compliance should be limited to impact assessment on whether instruments in issuance require any change further to adoption of the EU anti-hybrid rule.

2.2. Responses to mainly treaty-based action items (Actions 6 and 7)

2.2.1. Identification of priorities

Luxembourg investment or pension funds are incorporated, administered and managed in Luxembourg but are essentially marketed to non-Luxembourg resident investors. The reason behind the creation the Luxembourg investment funds is, in most cases, not tax driven.

In addition, many other vehicles are established in Luxembourg due to specific aspects of market infrastructure or legislation (the lender friendly pledge and security package legislation, the recognized capital market facilities, and especially the EURO MTF and the LSE). Therefore, vehicles can be located in Luxembourg for non-tax reasons, but with a valid business rationale, in relation to investments outside Luxembourg, and without having any necessary Luxembourg direct or indirect resident investors or shareholders. In addition, Luxembourg entities can often be listed in various stock exchanges around the world.

LUXEMBOURG

Given the above, the impact of rules potentially limiting the access to double tax treaties may be significant for the entire financial services industry. BEPS Action 6 was therefore regarded as the most important action between those that are under analysis in this section. The avoidance of permanent establishment issues has a more limited impact in Luxembourg.

Very particular attention must therefore be paid to point 6 of the report on BEPS Action 6, whereby it is noted that: “these model provisions need to be adapted to the specificities of individual States and the circumstances of the negotiation of the bilateral conventions”.

Due to the importance of the investment fund industry for Luxembourg, a key issue is the access of CIVs to double tax treaties. Accordingly, the Luxembourg investment fund association (the *Association Luxembourgeoise des fonds d'investissement* (ALFI)) officially took part in the consultation process and especially insisted on the fact that CIVs set up as UCITS or non-CIVs with similar characteristics, should automatically qualify as resident and be entitled to the benefit of treaties under the LOB clause.²³

In light of this, the Luxembourg tax authorities have issued a specific circular letter specifying from which double tax treaties the Luxembourg investment funds may benefit.²⁴ The Luxembourg tax authorities issue a certificate of residency for Luxembourg regulated investment funds.

Among the double tax treaties of Luxembourg, five double tax treaties directly include a specific LOB clause (United States of America, Trinidad and Tobago, Chinese Taipei, Russia, India). The treaties with the USA and Trinidad and Tobago include an LOB clause in line with the BEPS proposal, and the treaties with India, Russia and Chinese Taipei include only a principal purpose test (PPT) rule.

The double tax treaty with Poland specifies that treaty benefits may be denied if the considered income is paid in relation to an “artificial arrangement”, which therefore corresponds to a level of PPT.

The double tax treaties with Belgium, Germany, Hong Kong and India specify that the application of the treaty cannot prevent a contracting state from applying its own anti-abuse legislation.

Forty-two double tax treaties further specify that they do not apply to Luxembourg holding companies which are not subject to tax on their profits, and the Luxembourg tax authorities usually consider that such companies cannot qualify as resident for the benefit of a double tax treaty.

To make BEPS-related rule changes, negotiation by treaty or within the frame of the multilateral instrument under Action 15 will be necessary.

2.2.2. OECD participation

Please refer to section 2.1.2 above, and also for the participation of Luxembourg personnel in drafting and the impact of such participation on rule changes.

²³ ALFI report on BEPS Action 6, 8 January 2015.

²⁴ Circulars LG-A no. 61 dated 12 February 2014, and LG-Conv 52 dated 21 July 2015.

2.2.3. Public consultation

At this stage, there has not yet been any public discussion involving officials on these issues.

Regarding specifically access to treaties, the Luxembourg policy when negotiating new treaties aims at including Luxembourg regulated CIVs as beneficiaries. This is a general policy applied in practice; however, there has been no public announcement about it. The comments made in relation to BEPS Actions 2 to 5 are otherwise fully applicable in this section.

There are no domestic rules allowing a direct amendment of the content of tax treaties. However, Luxembourg further showed a pragmatic approach to resolving double non-taxation issues. This has particularly been the case when renegotiating the treaty with France, where double non-taxation has existed in the past on real estate profits, resolving together with France different cases of non-taxation.²⁵

A bill of law²⁶ is also with the Luxembourg Parliament to resolve certain possible double non-taxation issues in situations involving permanent establishments under the Luxembourg–USA double tax treaty (addressing point 71 of the report on BEPS Action 6).

As for other BEPS actions, working groups were organized at the level of the different industry organizations, including especially the ALFI, ABBL, Luxembourg for Finance and the Luxembourg Private Equity Association (LPEA). There are specific working groups at the level of the ALFI and the LPEA dedicated to BEPS.

Considering specifically the access to treaties for CIVs, discussions are also taking place at European level, with the European Fund and Asset Management Association (EFAMA) in the context of the TRACE project.

The working groups provided very technical analysis. Concerning specifically BEPS Action 6, they have a strong view, as previously mentioned. There has been much less discussion on BEPS Action 7 which has much less of an impact on Luxembourg industry.

The major publication is the ALFI report on BEPS Action 6, dated 8 January 2015.

The main discussions related to the access of the CIVs, and more generally investment funds to treaties, should normally be in line with the policy of the Luxembourg government when negotiating treaties. The industry, however, hopes that the documents and discussions will enhance the policy of the government in this respect.

2.2.4. Post-BEPS processes and early assessments of progress to date

The implementation of any processes should take place through the multilateral agreement.

As mentioned, considering a treaty perspective, the existing approaches are the pragmatic changes in the various treaties on a case-by-case basis.

²⁵ Amendment dated 24 November 2006. Amendment dated 5 September 2014.

²⁶ Bill of Law 7006.

LUXEMBOURG

There has been no controversy to date.

The existing changes rather relate to a general trend of collaboration, which accounts for their occurrence prior to BEPS finalization.

Considering BEPS Action 6, the main change will be the insertion of an LOB clause, and will mainly depend upon its wording in respect especially of CIVs. If, as has been requested by the Luxembourg ALFI, CIVs either in the form of a UCITS or any other form with comparable characteristics, qualify as resident for the benefit of double tax treaties, this will be a positive development for the industry.

The same conclusion applies to all the vehicles used for the financial services industry which are related, as mentioned above, to capital market transactions, security package implementation for financing, and other industry areas.

2.3. Responses to TP measures (Actions 8–10 and 13)

2.3.1. Identification of priorities

The bill of budget for 2017 includes a restatement of Luxembourg TP rules with a view to implementing Actions 8–10. A bill of law was passed in July 2016 to propose implementation of Action 13.

An EU Directive 2016/881/EU has been passed on 25 May 2016 in order to implement CbCR (BEPS Action 13) at a European level. On 2 August 2016, a bill of law was lodged with Parliament in order to implement this directive into Luxembourg law.

2.3.2. OECD participation

Individuals from the Ministry of Finance or the Luxembourg tax authorities observed or participated in policy discussions on these action plans, but there is no written or public record of these meetings.

To the extent of the knowledge of the reporters, no persons from Luxembourg drafted, reviewed drafts, or assisted in other capacities in the formulation of the relevant BEPS action plan.

2.3.3. Public consultation

To the extent of the knowledge of the reporters, no officials from Luxembourg promoted or participated in public discussions about the topics underlying these action plan items.

To the extent of the knowledge of the reporters, no specific policy guidance was released on these topics.

Since 2013 on many occasions there have been public discussions on BEPS. These took mostly the form of preliminary impact assessments for the industry (made by tax practitioners in Luxembourg).

Any discussions were organized mostly by top-tier tax practitioner firms. Professionals facilitating on those occasions were senior management representatives.

To the best knowledge of the reporters, the content of such documents was never reflective of a significant legal or empirical analysis of the topics, but rather a high level review and assessment.

To the best of the knowledge of the reporters, for the specific action items at stake, the public discourse has had no impact on Luxembourg's involvement so far.

2.3.4. Post-BEPS processes and early assessments of progress to date

To the best of the knowledge of the reporters, for the specific action items at stake, no processes were employed to date to determine the steps required for implementation.

No significant role was played by the various stakeholders on these action plans.

On 2 August 2016, a bill of law has been lodged with the Parliament in order to implement EU Directive 2016/881/EU (BEPS Action 13) into Luxembourg law.

There are no significant obstacles or challenges to implementation.

3. Conclusion

As already mentioned, Luxembourg is keen to be an early adopter of BEPS legislation. The legislative process is expected to be undertaken through:

- implementation of the Anti-Tax Avoidance Directive (Actions 3 and 4);
- implementation of the EU Directive 2016/881 introducing CbCR (Action 13), to be implemented by 4 June 2017, and for which a bill of law already exists;
- a negotiation process treaty per treaty or multilateral instrument BEPS (Actions 6 and 7);
- purely domestic legislation (notably implementing Actions 8–10).

It is not possible at this stage to be otherwise specific on the time line to be adopted. Furthermore, once the appropriate regulations have been adopted, it will be necessary to implement in practice the necessary measures, which are technical and complex. It is probable that a practical implementation will be made following a cooperative process between public and private sectors.

Considering that in parallel with the OECD process the EU action plan to implement BEPS at a European level is also currently going on, a key issue will be to ensure that the two processes remain consistent. In this respect, the European law-making process has shown more of a will to be at least as demanding as the BEPS actions, and therefore, it can be expected that the EU legislation implementing BEPS will comply with BEPS requirements.

Luxembourg has already clearly stated its intention to implement BEPS in Luxembourg but also to ensure that BEPS is implemented with a view to creating a level playing field. Consequently, for all the actions involving also an EU legislative process, it is foreseeable that Luxembourg will implement the actions once the relevant EU directives have been adopted and in line with these directives.

There is a need for an international instrument as far as BEPS Actions 6 and 7 are concerned, by way of a treaty by treaty approach or through the multilateral instrument, which would need to be in the form of an international treaty. Here also, it is foreseeable that Luxembourg will implement the actions in good time

LUXEMBOURG

in order to remain an early adopter. Considering specifically the international context of the Luxembourg financial services industry, it is probable that Luxembourg will focus more on PPT provision than on implementing the full LOB clause in all its double tax treaties.

Given that the BEPS actions are largely still to be implemented, it is too early at this stage to provide meaningful input on possible BEPS problems.

To the extent of the knowledge of the reporters, individuals in Luxembourg did not want to see any other issues covered.