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ESMA | PUBLIC STATEMENT ON SUSTAINABILITY DISCLOSURE IN PROSPECTUSES

On 11 July 2023, ESMA issued a public statement on the sustainability disclosure expected to be included in prospectuses in order to satisfy the requirements of Regulation (EU) 2017/1129 of 14 June 2017 on the prospectus to be published when securities are offered to the public or admitted to trading on a regulated market, and repealing Directive 2003/71/EC (the "**Prospectus Regulation**"), (the "**Public Statement**"). The purpose of the Public Statement is to set out ESMA's expectations on how the disclosure requirements under the Prospectus Regulation, with regard to sustainability-related matters in equity and non-equity prospectuses should be satisfied. ESMA have published this Public Statement, in support of the Environmental, Social and Governance ("**ESG**") transition in the hope that it will help to:

- ensure that national competent authorities ("**NCAs**") take a coordinated approach to the scrutiny of sustainability-related disclosure in prospectuses;
- provide issuers and their advisors with an understanding of the disclosure that NCAs will expect them to include in their prospectuses; and
- support investors' ability to make an informed investment decision considering the importance of disclosure relating to sustainability-related matters.

Main focus points for ESMA in respect of ESG disclosure in prospectuses

The Public Statement focuses on three main issues regarding disclosure in prospectuses:

Sustainability-related disclosure in equity prospectuses and consistency with non-financial reporting

In this section, ESMA clarifies that sustainability-related disclosures published in an issuer's non-financial reporting in accordance with Directive 2014/95/EU of 22 October 2014 amending Directive 2013/34/EU as regards disclosure of non-financial and diversity information by certain large undertakings and groups and Directive (EU) 2022/2464 of 14 December 2022 as regards corporate sustainability reporting, which are material in the context of Article 6(1) of the Prospectus Regulation, should be included in equity prospectuses.

Prospectuses relating to non-equity securities with a specific ESG component or objective

In relation to non-equity securities advertised as taking into account a specific ESG component or pursuing ESG objectives, ESMA clarifies the disclosure that is required in relation to both 'use of proceeds' bonds and 'sustainability-linked' bonds.

Consistency of sustainability-related disclosure in prospectuses and advertisements

This section sets out the expectation for sustainability-related disclosures in issuers' advertisements to be included in their prospectus, if the disclosure is material under Article 6(1) of the Prospectus Regulation.

Applicability of the Public Statement

While the Pubic Statement is principally addressed to NCAs, its contents is relevant for issuers and advisors and should be taken into consideration by them when drawing up prospectuses, including sustainability-related disclosure. ESMA will continue to monitor the market to determine whether this guidance should be modified from time to time.

EU SECURITISATION REGULATION – ESMA | UPDATED Q&A

On 13 July 2023, ESMA updated its questions and answers ("**Q&As**") in relation to Regulation (EU) 2017/2402 of 12 December 2017 laying down a general framework for securitisation and creating a specific framework for simple, transparent and standardised securitisation (the "**Securitisation Regulation**"), (the "Q&A"). This latest update was quite extensive in that it amended several of the existing Q&As, as well as adding an array of new Q&As.

In their update of 13 July 2023, ESMA modified existing Q&As in the following areas:

- Disclosure Requirements and Templates - Delegation and Prepayments;
- Underlying Exposures (Annex 2), Residential Real Estate - Collateral Item supporting an RMBS Loan;
- Underlying Exposures (Annex 3), Commercial Real Estate - Total Shortfalls in Principal & Interest Outstanding and Arrears balance; and
- Investor Reports (Annexes 12 and 13) - the types of tests/triggers that need to be reported.

ESMA have also added new Q&As on the following matters:

- Disclosure Requirements and Templates in relation to Amended transaction documents, Self-Securitisation and Consumers' rights to access information;
- Underlying Exposures (Annex 2) - Residential Real Estate, specifically Allocated Losses and Cumulative Recoveries;
- Underlying Exposures (Annex 3) - Commercial Real Estate, in relation to Current Principal Balance, Original Principal Balance and Original Principal Balance At Securitisation Date, Non-Payments on prior ranking Claims and Unscheduled Principal Collections for non-performing exposures;
- Underlying Exposures (Annex 4) - Corporate, namely Current Principal Balance, Total Credit Limit and Balloon Amount;
- Underlying Exposures (Annex 8) - Leasing , specifically regarding the NACE Industry Code;
- Underlying Exposures (Annex 9) - Esoteric, namely the Collateral Information Section and the Reporting template for B2B BNPL assets; and
- Investor Reports (Annexes 12 and 13) - Weighted Average Life.

DRAFT LAW NO. 8291 ON THE DIGITAL OPERATIONAL RESILIENCE OF THE FINANCIAL SECTOR

On 4 August 2023, the draft law No. 8291 (the "**Draft Law**") aimed at (i) implementing Regulation (EU) 2022/2554 of 14 December 2022 on the digital operational resilience of the financial sector and amending Regulations (EC) No 1060/2009, (EU) No 648/2012, (EU) No 600/2014, (EU) No 909/2014 and (EU) 2016/1011; (ii) transposing Directive (EU) 2022/2556 of 14 December 2022 amending Directives 2009/65/EC, 2009/138/EC, 2011/61/EU, 2013/36/EU, 2014/59/EU, 2014/65/EU, (EU) 2015/2366 and (EU) 2016/2341 as regards the digital operational resilience of the financial sector; (iii) amending (a) the amended law of 5 April 1993 on the financial sector; (b) the amended law of 13 July 2005 on institutions for occupational retirement provision in the form of a SEPCAV and an ASSEP; (c) the amended law of 10 November 2009 on payment services; (d) the amended law of 17 December 2010 on undertakings for collective investment; (e) the amended law of 12 July 2013 on alternative investment fund managers; (f) the amended law of 7 December 2015 on the insurance sector; (g) the amended law of 18 December 2015 on the failure of credit institutions and certain investment firms; (h) the amended law of 30 May 2018 on markets in financial instruments; (i) the amended law of 16 July 2019 on the implementation of European regulations in the field of financial services, was submitted to the Luxembourg Parliament (*Chambre des Députés*).

The aim of Regulation (EU) 2022/2554, and incidentally Directive (EU) 2022/2556

The aim of Regulation (EU) 2022/2554 (commonly known as "**DORA**" or "**Digital Operational Resilience Act**"), and incidentally of Directive (EU) 2022/2556, is to harmonise and strengthen information and communication technology ("**ICT**") security requirements in order to achieve a high level of security and a high level of digital operational resilience across the financial sector.

Regulation (EU) 2022/2554 consolidates the different rules dealing with ICT risk in the financial sector and brings them together in a single legislative act to fill in the gaps and to avoid inconsistencies.

Directive (EU) 2022/2256 accompanies and complements Regulation (EU) 2022/2554 by providing for a series of targeted amendments to existing European directives in the field of the financial sector. These amendments are necessary in order to ensure, in the interests of legal certainty, that these sectorial directives are consistent with Regulation (EU) 2022/2554 as regards the application of digital operational resilience requirements that are currently scattered across the existing sectoral legislation.

Key points of Draft Law

As the provisions of Regulation (EU) 2022/2554 are directly applicable in the EU, the main purpose of the Draft Law is to give to the competent national authorities the responsibility of ensuring the application of Regulation (EU) 2022/2554. To give the supervisory and investigative powers they need to carry out their duties, their functions, within the limits defined by the said regulation, and to set an appropriate sanctions regime. To this end, the Draft Law amends the amended law of 16 July 2019 on the operationalization of European regulations in the field of financial services.

In addition to implementing Regulation (EU) 2022/2554, the Draft Law aims to transpose into Luxembourg law specific amendments to European financial sector directives relating to digital resilience and ICT security. The Draft Law thus makes a targeted adaptation of a series of national laws relating to the financial sector.

MIFID II AND MIFIR | ESMA AND CSSF UPDATES

Since our last newsletter, ESMA has published the following in relation to Directive 2014/65/EU of 15 May 2014 on markets of financial instruments ("**MiFID II**") and Regulation (EU) 600/2014 on markets of financial instruments ("**MiFIR**"):

- Final Report on the review of the technical standards for passporting under Article 34 of MiFID II (the "**Final Report**"); and
- Manual on post-trade transparency under MiFID II/ MiFIR (the "**Manual**").

Final Report

On 11 July 2023, ESMA published their Final Report on the review of the technical standards for passporting under Article 34 of MiFID II. This Final Report contains, in Annex III and Annex IV respectively, a draft commission delegated regulation amending Commission Delegated Regulation (EU) 2017/1018 of 29 June 2016 and a draft commission implementing regulation amending Commission Implementing Regulation (EU) 2017/2382 of 14 December 2017, which together, propose targeted amendments to the existing regulatory technical standards ("**RTS**") and implementing technical standards ("**ITS**"). ESMA's proposed amendments to the RTS and ITS will introduce new information requirements to the list of details investment firms have to provide at the passporting stage.

ESMA has submitted the Final Report to the European Commission.

Manual

On 10 July 2023, ESMA published the Manual on post-trade transparency under MiFID II/ MiFIR. The purpose of this Manual is to act as a convergence tool in order to promote common approaches and practices in the areas of post-trade transparency and the transparency calculations.

Section 3 provides an introduction to the Manual, including a discussion of its purpose and legal basis as well as its content. Section 4 addresses the different aspects of post-trade transparency for equity and non-equity instruments. Finally, Section 5 deals with the transparency calculations for equity and non-equity instruments.

Market participants and national competent authorities should rely on this Manual for guidance on how to apply the relevant MiFIR obligations in a consistent manner. The Manual will be updated on a regular basis going forward.

CSSF Circular adopting ESMA Guidelines on MiFID II product governance requirements

On 15 September 2023, the CSSF published a circular (the "**Circular**") informing that it will apply ESMA's new guidelines on MiFID II product governance requirements (ESMA35-43-3448) (the "**Guidelines**") from 3 October 2023 onwards. For more information on the content of these Guidelines we refer you to our previous newsletter articles available here.

VIRTUAL ASSET SERVICE PROVIDERS | NEW CSSF Q&A

On 17 August 2023, the CSSF published its first set of questions and answers on virtual asset service providers ("**VASP**") (the "Q&A"). In its Q&A, the CSSF provides clarity on some key questions, such as who has to register as a VASP with the CSSF and when that registration should be done.

Registration

The CSSF clarifies that any natural or legal person, who is either established in Luxembourg or providing virtual asset related services (the "**VA services**") in Luxembourg on behalf of or for its customers must register as a VASP in the CSSF register prior to offering such services. To assist in determining whether a person is subject to registration as a VASP, the Q&A provide detailed guidance on the analysis which should be conducted by such person. The Q&A also provide clarity on the internal criteria taken into consideration by the CSSF when determining if an entity not established in Luxembourg should nevertheless register as a VASP in case it provides VA services in Luxembourg.

Moreover, CSSF makes clear that credit institutions in Luxembourg can offer VA services, if they register as a VASP, while entities which solely provide the hardware and/or the software to support the offering of such services are not subject to registration requirements. The entities concerned should keep in mind that no passporting regime is available for VASPs under the current national or European legal framework.

ML/TF considerations

VASPs currently fall within the scope of the Luxembourg Law of 12 November 2004 on the fight against money laundering and terrorist financing, as amended (the "**AML/CTF Law**") and are required to comply with all professional obligations set out therein. In that context, the Q&A provides details on the level of information expected by the CSSF for the money laundering and terrorist financing ("**ML/TF**") risk assessments and ML/TF policies and procedures, which must be submitted as part of the VASP registration file. In addition, CSSF makes clear that VASPs should put in place an efficient process of transaction-monitoring, which, in principle, should be supported by automated tools, enabling prompt information by the VASP on its own initiative, to the Luxembourg Financial Intelligence Unit of any suspicious activities or transactions. Finally, VASPs must also comply with the applicable legal framework on financial restrictive measures.

CSSF role

The CSSF's role for the registered VASPs is currently limited to ML/CTF related registration, supervision and enforcement for AML/CTF purposes only. Once a VASP is registered with the CSSF, the CSSF has all the supervisory, investigatory and sanctioning powers provided under the relevant provision of the AML/CTD Law.

Going forward

Entities already registered as VASPs with the CSSF or intending to be establish or to offer VA services in Luxembourg should take into consideration and monitor any updates to these Q&A; the CSSF points out that these Q&A have been drawn up on the basis of the current legal AML/CTF framework applicable to VASPs and do not take into account the evolution of the framework related to VA at European level (i.e. the Regulation on Markets in Crypto-Assets ("**MICA**")).

PREVIOUSLY PUBLISHED IN BANKING & FINANCIAL SERVICES | CAPITAL MARKETS

- Sustainable finance | CSSF supervisory priorities
- Markets in crypto-assets (MICA) | EU framework
- DLT | Most recent developments
- Crowdfunding Regulation | New ESMA Q&A
- MiFID II and MiFIR | ESMA guidelines and FAQ

COURT OF JUSTICE OF THE EUROPEAN UNION CAST SHADOW OVER META'S BUSINESS MODEL

On 4 July 2023, in its judgment C-252/21 Meta Platforms Ireland and Others v Bundeskartellamt, the Court of Justice of the EU (the "**Court**") ruled on the interplay between the EU's competition and data protection regulations, as well as on the core of the business model of the worldwide leading social networks operator. The preliminary ruling was issued following a request lodged by the courts of the Federal Republic of Germany.

Background to the dispute

Back in 2019, the Bundeskartellamt, Germany's competition authority, found that Meta Platforms Ireland ("**Meta**"), the EU operator of Facebook as well as several other platforms, abused of its dominant position on the German social networks markets. The alleged abuse touched upon the very core of Facebook's financial engine, based on profiling users and sending them tailored-made advertisements.

When agreeing to Facebook's terms, users actually also have to subscribe to a data and cookies policy allowing the social network to track their movements on the web. It can then proceed to a wide-scale collection of personal data disseminated on off-Facebook websites and their combination to data provided by signing up to Facebook. The absence of competitors providing comparable services may push users to agree to these policies.

In light of this, the Bundeskartellamt forbade Meta from making the use of Facebook subject to processing user's data collected off-Facebook, as well as processing these without prior collecting the consent of data subjects. In reaching this conclusion, the authority considered that the processing of the data collected off-Facebook infringes upon the principles underpinning of the General Data Protection Regulation ("**GDPR**").

The issues at stake

The match played in the procedure before the Court was certainly important on both sides. On the one hand, prior to the Court's ruling, it was unclear whether a national competition authority ("**NCA**") could use the provisions of the GDPR as part of its assessment on an abuse of dominance, which made it uncertain whether the conclusions of the Bundeskartellamt would be well-grounded. On the other hand, this was a challenge to Meta's entire business model, key to the group's economic success.

The findings of the Court

On the first point, the Court acknowledged that, in competition law enforcement, NCAs may also need to examine whether the practices of an enterprise comply with the GDPR. Consequently, if required to establish the existence of an abuse of dominance, the Bundeskartellamt could conclude that Meta's data processing policies be incompatible with the GDPR. In application of the principle of (horizontal) loyal cooperation, NCAs need to abide by fellow data protection authorities' decisions (Article 51 of the GDPR) absent any precedent, they should consult and seek their cooperation.

On the second point, the Court considered essentially that the use of cookies or other storage technologies may entail the collection off-Facebook of personal data falling within special categories, revealing racial or ethnic origin, political opinions, religious or philosophical beliefs, etc. (Article 9.1 of the GDPR). Processing personal data of this kind is in principle prohibited under the GDPR but could be justified under the derogations per Article 9.2 thereof. In particular, data processing would be allowed if users manifestly made public their consent thereto (Article 9.2 (e) of the GDPR). However, the fact users visit the web and disseminate therein personal data (subsequently "captured" by cookies) is not equivalent to expressly providing such consent, which should have been given explicitly in advance.

Neither would Meta's processing operations be justified under the provisions of the GDPR allowing data processing *without* the data subject's consent. In particular, the Court was doubtful whether the processing of personal data is objectively indispensable to perform the contract to which the user is part (Article 6.1 (b) of the GDPR), as its purpose may be achieved without carrying out such action and referred to national courts to carry out this assessment.

The way forward

The Court intended to be clear: the fact that a data controller holds a dominant position, solely of itself, does not prevent users from validly giving their consent to the processing of their personal data. However, dominance may deter users from providing their consent freely, as, absent competitors providing comparable services, they need to adhere to an aggressive cookies policy aimed at profiling them, if they want to access to social network services.

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PREVIOUSLY PUBLISHED IN GENERAL COMMERCIAL

- General Court of the EU reaffirms primary substantive right of access to documents

NEW LUXEMBOURG DRAFT LAW ON BUSINESS CONCENTRATIONS

Aims of the Draft Law

The parliamentary process leading to the introduction of a new law on business concentrations (Draft Law No. 8296) (the "**Draft Concentration Control Law**") was started on 23 August 2023. Luxembourg is the only EU member state that does not have a national law on the control on business concentrations.

The new law aims to introduce for the first time in Luxembourg a procedure allowing the Luxembourg Competition Authority (*Autorité de la concurrence*) to verify *ex ante* whether a corporate concentration significantly restricts or distorts competition in Luxembourg, thus increasing legal security for businesses engaged in business concentrations.

At the present time those business concentrations that do not fall within the scope of application of Regulation (EU) 139/2004 of 20 January 2004 (the "**EU Merger Regulation**"), may in Luxembourg only be subject to controls *ex post* under existing competition rules provided that a concrete abuse of a dominant position by reason of the corporate concentration is demonstrated.

The EU Dimension

Concentrations are considered to have a European dimension, and are therefore caught by the EU Merger Regulation, where the combined aggregate worldwide turnover of all the concerned entities is more than EUR 5 billion and the aggregate European-wide turnover of each of at least two of the entities exceeds EUR 250 million.

In accordance with the EU Merger Regulation, where the above-mentioned thresholds are not met, concentrations may nonetheless reach a European dimension if a number of cumulative conditions is met, namely: (i) the combined aggregate worldwide turnover of all the entities concerned exceeds EUR 2.5 billion; (ii) the concentration affects at least three EU member states, in each of which the combined aggregate turnover of all the entities concerned exceeds EUR 100 million and the aggregate turnover of each of at least two of the entities concerned exceeds EUR 25 million; and (iii) the aggregate European-wide turnover of each of at least two of the entities concerned exceeds EUR 100 million.

In both cases, if the entities, taken individually, achieve more than 2/3 of their aggregate European-wide turnover within one and the same EU member state, the concentration is not considered having an EU dimension and, as such, in principle it will be considered under the national provisions.

Following the same logic, the European Commission (the "**Commission**") is entitled to refer the case to national competition authorities where it considers that a project may significantly affect the whole or a part of a market in an EU member state presenting the characteristics of a "distinct market". As such, in these cases, the project would be caught within the scope of the Draft Concentration Control Law.

Concentrations falling within the Draft Concentration Control Law

In line with the provisions of the EU Merger Regulation, the types of business concentrations that may be controlled by the Luxembourg Competition Authority are mergers, acquisitions (whether by way of purchase of capital, assets, contracts or by other means) or the creation of a joint enterprise (leading to lasting changes of control as regards mergers and acquisitions), if certain thresholds are exceeded.

The definition of "control" means (following closely the definition under the EU Merger Regulation) all rights, contracts or other means which confer individually or jointly and having regard to factual or legal circumstances the possibility to exercise a decisive influence on the activity of an enterprise (either its assets or the composition, deliberation, or decisions of corporate decision-making bodies).

Provided that the envisaged corporate concentration does not fall within the ambit of the EU Merger Regulation, the new law would apply if both of the following thresholds are exceeded:

- the total turnover (excluding tax) realised in Luxembourg by all the businesses concerned **exceeds EUR 60 million**; and
- the turnover (excluding tax) realised individually in Luxembourg by at least two of the enterprises

concerned **exceeds EUR 15 million**.

The Luxembourg Competition Authority can also examine the effect of a corporate concentration if the thresholds are not met but if the Luxembourg Competition Authority believes that the corporate concentration might have a restrictive effect on competition as regards the market of goods or services in Luxembourg or a part of Luxembourg. In such case, for legal certainty purposes, the Luxembourg Competition Authority must promptly take action, no later than 60 days as of the date it became aware of the concentration, or, at the latest, as of the date of the realisation of the concentration.

The relevant enterprises taking part in the corporate concentration do not need to be Luxembourg enterprises.

Concentration not falling within the Draft Concentration Control Law

All concentrations that fall within the ambit of the EU Merger Regulation are excluded (except if there is a referral by the Commission to the Luxembourg Competition Authority, as mentioned above).

The Draft Concentration Control Law provides that acquisitions carried out by investment funds, securitisation funds or vehicles and pension funds generally do not fall within the scope of the Draft Concentration Control Law except for certain operation defined as capital investment operations that lead to a lasting change of control exceeding the thresholds.

Furthermore, the following operations do not fall within the Draft Concentration Control Law as they are **not** regarded as concentrations:

- concerted practises by enterprises that stay independent of each other (such practises might, however, be caught by the Luxembourg Competition Law of 30 November 2022 (the "**Luxembourg Competition Law**");
- the temporary detention by banks, investment firms or insurance companies, whose business includes the trading and negotiation of financial instruments, of participations with the view of their re-sale within one year provided they do not exercise voting right with a view to determining the competitive position of the enterprise to but only in connection with the re-sale of the whole or part of the enterprise or its assets;
- if the control is exercised by a person mandated by a public authority under the legislation providing for a liquidation, winding up or similar bankruptcy procedure;
- if acquisitions are carried out by financial holding companies subject to such companies only exercising their voting rights in order to preserve the value of their investment rather than determining the competitive position of the enterprise;
- internal restructurings within a group of enterprises (e. g. increases in capital and creation of new group entities) if not leading to a change in the control structure; and
- internal group insurance or re-insurance schemes.

If the urgent rescue or re-organisation of a credit institution or certain investment firms becomes necessary to maintain or prevent a serious threat to the financial stability of Luxembourg or to protect the deposit holders or the investors, the CSSF will take over from the Luxembourg Competition Authority. The same will apply in the insurance and re-insurance sector with a possible transfer of responsibility to the Insurance Commission *(Commissariat aux Assurances*). In general, the Luxembourg Competition Authority needs to consult its fellow Luxembourg authorities where entities active on the financial and insurance and re-insurance markets are subject to a concentration.

Persons who can commence the procedure

The Draft Concentration Control Law provides for an **obligation to notify** the Luxembourg Competition Authority **in advance** of any proposed corporate concentration (as defined in the Draft Concentration Control Law) once the transaction is sufficiently concrete (notably if a memorandum of understanding respectively letter of intent has been signed or a public offer has been published) by:

- **any** physical or legal persons who **acquire** the control of the whole or part of an enterprise;
- in the case of a **merger or creation of a joint enterprise**, **all parties concerned**.

According to the comments to the Draft Concentration Control Law this does not preclude that informal and confidential **pre-notification** discussions with the Luxembourg Competition Authority are commenced beforehand, for example to clarify whether the transaction might fall within the competence of the

Luxembourg Competition Authority. The practice under the EU Merger Regulation shows that the exchanges among the Commission and the concerned entities, in the pre-notification phase, are essential to structure and streamline the later notification procedure.

The notification can notably be submitted in a simplified form in case the project does not appear to raise any major competition issues.

The **Luxembourg Competition Authority** may of its own accord start a procedure **within 60 days** of becoming aware of a proposed or realised corporate concentration, if the thresholds are not met and the Luxembourg Competition Authority believes that the corporate concentration might have a restrictive effect on competition as regards the market of goods or services in Luxembourg (or a part of it).

Furthermore, as mentioned above, the Luxembourg Competition Authority may also become active upon referral of a project by the Commission in case the Luxembourg market could be identified as a "distinct market", notwithstanding the turnover triggering the application of the EU Merger Regulation.

If the Luxembourg Competition Authority decides to open a procedure (or receives a referral), it will ask the relevant parties to proceed with a notification. A Grand-Ducal Regulation is to determine the modalities and the contents of notifications to the Luxembourg Competition Authority (including any simplified notification).

Procedure

Any notification or referral received will be published on the website of the Luxembourg Competition Authority.

Phase I

The Luxembourg Competition Authority will **within 25 business days of receipt** of a complete notification decide that either the transaction does not fall within the scope of the law, authorise the transaction or, if there are serious reasons to believe that the transaction will have a negative effect on competition, open a more detailed examination (the so-called **Phase II** procedure). It could also decide to refer the transaction to the Commission.

Phase II

If the Luxembourg Competition Authority decides to carry out a detailed examination, the Luxembourg Competition Authority will need to do so **within 90 business days**. It will notify its initial report and underlying documents to the parties concerned and give such parties 15 business days (which may be prolonged on demand by up to one month) to respond. If the parties wish to do, a hearing involving all interested parties may be convened thereafter.

At the end of the procedure, the Luxembourg Competition Authority will decide either (i) to authorise the transaction, (ii) to authorise the transaction subject to the parties' undertakings and/or any conditions that it may impose, or (iii) prohibit the transaction and, if relevant, ask the parties to take all measures necessary to re-instate a healthy competition.

The Luxembourg Competition Authority will analyse on a case-by-case basis the relevant market and have regard to the principles on the definition of markets for EU law purposes, as set out in the Commission Notice on the definition of relevant market for the purposes of Community competition law (published in the Official EU Journal on 9 December 1997, wrongly stated to be 9 February 1997 in the Draft Concentration Control Law), or any later revision of such notice.

Whilst the first duty of the Luxembourg Competition Authority will be to ensure that there is no significant distortion to competition in the Grand Duchy, notably by the creation or reinforcement of a dominant position which is not offset by a possible contribution to economic progress, it can, in view of its geographical characteristics, also look at concentrations affecting markets that extend beyond its borders.

Consistently with the design of the powers of the Luxembourg Competition Authority under the Luxembourg Competition Law, in carrying out any investigations, the Luxembourg Competition Authority will have wide powers to inspect premises and documents, obtain information from the businesses concerned and public authorities, convene persons for interview and put in place provisional measures. It can also engage experts. It can further impose daily penalties to enforce compliance and financial penalties for non-compliance (up to 10% of annual turnover during the last financial year of the businesses concerned).

Appeal/ Reversal of Decisions

Decisions taken by the Luxembourg Competition Authority may be appealed before the administrative courts **within three months** of the publication, notification, or knowledge of such decision.

The Luxembourg government may, by way of a cabinet

decision decide to overturn a Phase II decision of the Luxembourg Competition Authority within **35 business days** of such decision, by pointing to the general public interest of a corporate concentration including progress in industrial, economic or financial developments, the increased competitiveness of the enterprises concerned in the face of international competition or the creation or maintenance of employment.

Date of Effect

The Draft Concentration Control Law will now go through the parliamentary process and will only enter into effect on the 4th month following its publication in the Luxembourg Official Gazette (*Journal Officiel*).

The new law will not affect business concentrations in relation to which an authorisation or a publication has already taken place, or which were realised before the date of effect.

DIGITALISATION OF CORPORATE PROCEDURES

The law of 14 July 2023, transposing Directive (EU) 2019/1151 20 June 2019 amending Directive (EU) 2017/1132 (the "**Directive**") as regards the use of digital tools and processes in company law (the "**Law**") was published in the Luxembourg Official Gazette (*Journal Officiel*) on 18 July 2023 and entered into force on 1 August 2023.

The Law introduces a legal framework for establishing authentic instruments in electronic form (except for wills), as well as a notarial electronic exchange platform, as part of the national digitisation strategy of the Grand Duchy of Luxembourg and the digitalisation of the notarial profession.

1. Scope of application

The main purpose of the Law is to facilitate the incorporation of companies by the use of digital technologies. The Law creates the possibility for the parties to pass notarial deeds in electronic form, with or without physical appearance of the parties.

The Law will enable:

- the online incorporation of companies;
- the improved exchange of information via the system for the interconnection of commercial and company registers; and
- easier access to information relating to branches.

2. Notarial deeds and instruments in electronic form

Parties will now be able to pass notarial deeds in electronic form, which was already available for documents under private seal. This possibility applies broadly to all "documents of title and authentic instruments", except for wills, which require the physical presence of the testator. Examples of the deeds in electronic form include various modifications to the articles of association, i.e. increase of decrease of the company’s capital, change of company’s form, etc.

The documents in electronic form will have the same evidentiary value as documents in paper form.

The Law allows, in particular, companies like public limited company (*société anonyme*, “**SA**”), limited liability company (*société à responsabilité limitée*, “**SARL**”) and partnership limited by share (*société en commandite par actions*, “**SCA**”) to be incorporated by electronic notarial deed without the physical appearance of the parties, whereas previously these companies needed to be constituted by notarial deed in the presence of the founders or their proxy holders.

For online incorporation, the parties can use standard articles of association provided by the Chamber of Notaries.

Authentic instruments in electronic form can be drawn up either in the presence of the parties or remotely.

The following procedures would usually be followed when an authentic instrument is adopted remotely:

- the parties connect to the notarial electronic exchange platform;
- identification of the parties including by way of audio-visual means;
- use of electronic signatures (e.g. qualified electronic signature) by the notary and the founders;
- parties can also arrange for an online payment for cash contributions to the account opened by the company that is undergoing the formation process.

The notary can refuse to draw up a notarial deed for the constitution of SARLs, Sas or SCAs remotely in these two cases specified by the Law:

- when the notary has reasons to suspect identity fraud, non-compliance with the rules on the legal capacity of a party or the power of representation of a company by a party to the authentic instrument; and
- when the company's share capital is fully or partially paid up in kind.

3. Registration of branches

The Law introduces requirement for Luxembourg and EU branches of companies governed by Luxembourg law to have a separate registration number. Such branches are assigned a registration number by the administrator of the trade and companies register (“**TCR**”), who creates an individual file for them, using the information contained in the TCR database.

This change will be implemented without any intervention by the Luxembourg company, based on the information available to the TCR. Therefore, this new obligation will not impose any direct burden on the Luxembourg company concerned.

PREVIOUSLY PUBLISHED IN CORPORATE AND M&A

- Enterprises' duty of care with regard to sustainability

NEW PROVISIONS IN FAVOR OF HIGHLY QUALIFIED THIRD-COUNTRY WORKERS

On 30 August, the Luxembourg Parliament (“*Chambre des députés*”) tabled draft law No.8304 (the "**Draft Law"**) amending the law of 29 August 2008 on the free movement of persons and immigration (the "**Law"**).

The Draft Law aims at transposing into national law Directive (EU) 2021/1883 of 20 October 2021 on the conditions of entry and residence of third-country nationals for the purposes of highly qualified employment and repealing Council Directive 2009/50/EC (the "**Directive"**).

The main purpose of the Draft Law is to update the previous rules on the EU Blue Card as set out in Directive 2009/50/EC, now repealed by the Directive, and to provide the EU with a targeted legal migration system capable of addressing skills shortages and making it easier for highly qualified workers to join the workforce.

More specifically, the Draft Law provides, to the benefit of EU Blue Card holders:

- more flexible and inclusive admission criteria;
- more extensive rights;
- more favorable conditions for family reunification;
- facilitated intra-EU mobility.

More flexible and inclusive admission criteria

Currently, the Law requires applicants for an EU Blue Card to present a valid work contract for a highly qualified employment of at least one year. The Draft Law suggests to adapt this duration to **at least six months**.

The others admission criteria, i.e. proof of **higher professional qualifications** and **remuneration** at least equal to an amount to be set by Grand-Ducal regulation, remain unchanged. It should nonetheless be noted that:

- with regard to the requirement for higher professional qualifications, it will have to be attested by:
  - **higher education qualifications**, where the studies needed to acquire those qualifications last at least three years (*bachelor's degree*); or
  - **higher professional skills**, i.e. knowledge, skills and competences attested by at least five years of professional experience at a level comparable to higher education qualifications and which are relevant to the profession or sector concerned. For the occupations of manager and ICT specialist, this period is limited to three years in the seven years preceding the application for an EU Blue Card;
- with regard to remuneration levels, in order to harmonize admission criteria throughout the EU, the Directive suggests that each Member State should determine, after consulting the social partners, a salary threshold based on the average gross annual salary in the Member State concerned. This salary threshold, which may not be less than 1.0 times the average gross annual salary in the Member State concerned, nor exceed 1.6 times this salary, should determine the minimum salary that an EU Blue Card holder should receive.

This salary threshold may be lowered for specific professions, particularly where there is a shortage of available workers, or for third-country nationals who have recently obtained their qualifications. Currently, in Luxembourg, the salary threshold is set at 1.5 times the average gross annual salary, or 1.2 times this salary for professions for which the Government has identified a shortage of workers.

Finally, the Draft Law intends to formally enshrine the administrative practice whereby any residence permit issued by the Minister **entitles its beneficiary to obtain the required visa**, where applicable. Thus, once an application for an EU Blue Card has been approved, the Minister will also have to issue the necessary entry visa to the worker concerned.

Enhanced rights for EU Blue Card holders

- Enhanced rights during the renewal procedure: in principle, the EU Blue Card is **valid for four years**, renewable for the same period of time. In this respect, the Draft Law supplements Article 45-1 of the Law, specifying that if the EU Blue Card expires during the renewal procedure, the third-country national nevertheless remains authorized to reside

on Luxembourg territory as a highly qualified worker until the Minister has ruled on the renewal application.

- Extended access to the labour market: the Law currently provides that during the **first two years** of employment, EU Blue Card holders' access to the labour market is limited to the activity for which they have been admitted, with any employer. After the first two years, the Law grants EU Blue Card holders equal treatment with nationals, except for jobs related to the exercise of public authority, for which Luxembourg nationality is required.

The Draft Law aims to significantly extend access to the labour market of EU Blue Card holders: during the **first 12 months** of legal employment and unless the EU Blue Card holder benefits from the right to free movement, he/she will have to inform the Minister prior to any change in his/her professional situation (such as a change of employer, which would therefore in principle be possible). The Minister may object to the change within 30 days.
After the first 12 months, EU Blue Card holders will benefit from equal treatment with nationals, except for jobs linked to the exercise of public authority, for which the condition of Luxembourg nationality is required.

- Enhanced rights in the event of unemployment: during the initial 12-month period mentioned above, the Draft Law specifies that the EU Blue Card holder will also be authorized to seek and accept employment, provided that he/she complies with his/her obligation to inform the Minister, in particular of the beginning and, where applicable, the end of the period of unemployment, as well as of any new employment relationship.

The Draft Law also reinforces the conditions for withdrawing an EU Blue Card in the event of unemployment. The Law currently provides that the EU Blue Card is withdrawn if unemployment lasts for more than three consecutive months, or if it occurs more than once during the period of validity of the residence permit.
The Draft Law provides that as a matter of principle, the EU Blue Card will not be withdrawn and that renewal will not be refused in the event of unemployment, except in the event of i) unemployment over a period of more than **three months**, if the holder has held an EU Blue Card for less than two years, or ii) unemployment over a period of more than **six months** if the holder has held an EU Blue Card for at least two years.

- Enhanced rights to long-term resident status: in order to apply for **long-term resident status,** an EU Blue Card holder will be able to rely not only on the years of legal and uninterrupted residence spent in the territory of the EU as an EU Blue Card holder (as currently provided for by the Law), but also as the holder of a residence permit as a researcher, student or beneficiary of international protection.

Long-term residents of another Member State holding a long-term residence permit as "*Former holders of an EU Blue Card*" will also have the right to engage in an **employed or self-employed activity in Luxembourg** without having to fulfil the conditions laid down in Articles 42 (1) and 51 (1) of the Law relating to the issue of residence permits with a view to exercise an employed or self-employed activity.
Finally, the Draft Law intends to grant EU Blue Card holders:

- the right to exercise a **subsidiary self-employed activity** in parallel with the main activity exercised in a highly qualified job;
- the right to **education and vocational training** (excluding scholarships and student loans);
- the right to **recognition** of diplomas, certificates and other professional qualifications.

Greater mobility within the EU

The Law currently stipulates that for **stays of up to three months,** all third-country nationals must have a residence permit in order to carry out an employed or self-employed activity, except in the case of business trips (such as trips to visit business partners, develop business contacts, negotiate and conclude contracts, take part in trade fairs, attend board meetings, etc.).
The Draft Law aims to introduce another exemption for holders of a valid EU Blue Card issued by another Member State who wish to stay and work in Luxembourg for up to 90 days in any 180-day period.
On the basis of the Draft Law, EU Blue Card holders would be exempt from the requirement to have a visa, a work permit or an authorization other than the EU Blue Card, in order to carry out a "business activity" in Luxembourg. The Draft Law defines "business activity"

as a temporary activity directly related to the business interests of the employer and to the professional duties of the EU Blue Card holder, including attending internal or external business meetings, attending conferences or seminars, negotiating business deals, undertaking sales or marketing activities, exploring business opportunities, or attending and receiving training.

If the EU Blue Card was issued by a first Member State that does not fully apply the Schengen *acquis* (i.e. Romania, Bulgaria or Cyprus), the holder must, in order to work in Luxembourg for a maximum period of 90 days, carry their residence permit, a valid travel document and proof of the professional purpose of the stay (e.g. invitations, entry cards, documents describing the company's economic activities and the position held by the holder, etc.).

For **stays of more than three months**, the Law currently provides that after 18 months of residence in a first Member State, the holder of an EU Blue Card may move to another Member State for the purpose of highly qualified employment. No later than one month after entering Luxembourg territory, the third-country national must submit an application for an EU Blue Card to the Minister. Under the Law, the applicant is not authorized to work until the Minister has issued a new residence permit.

In this respect, the Draft Law aims to:

- reduce the period of residence in the first Member State for the purposes of mobility in a second Member State **from 18 months to 12 months**. This period is even reduced to **six months** of legal residence in the first Member State if the holder of the EU Blue Card makes use of his/her right to mobility for the second time;
- enable applicants to **start working immediately** after submitting their application for a residence permit in the second Member State, without having to wait for the Minister to issue a residence permit;
- introduce a **maximum period of 30 days for** the Minister to reach a decision. This initial period may be extended by 30 days in exceptional and duly justified circumstances linked to the complexity of the application.

Family reunification of family members of an EU Blue Card holder

The Law already provides for the possibility for certain family members of the holder of an EU Blue Card issued in a first Member State, and who have applied for mobility in Luxembourg, to accompany or join the latter.

To this end, family members must apply for a residence permit. Under the Law, this application can only be made if the family member concerned resides outside Luxembourg.

The Draft Law provides that the family members of an EU Blue Card holder may enter and reside in Luxembourg, **before** an application for a residence permit is submitted, if they hold a valid residence permit obtained in the first Member State as family members of an EU Blue Card holder.

With the aim of facilitating the swift entry of highly qualified workers, the Draft Law provides that residence permits to family members should be issued at the same time as the EU Blue Card where the relevant conditions are fulfilled and the applications were lodged simultaneously. Finally, if the family member joins the holder of an EU Blue Card after the EU Blue Card has been granted, the Draft Law provides for an **accelerated procedure**, and the residence permit will have to be granted no later than thirty days after the application is submitted.

Conclusion

The reform of the EU Blue Card aims at reducing the administrative burden on companies and better matching labour supply with demand by attracting skills. These provisions are more than welcome considering the labour and skills shortage faced by Luxembourg and the EU in key sectors of the economy.

PREVIOUSLY PUBLISHED IN EMPLOYMENT, COMPENSATIONS & BENEFITS

- New Directive on transparency and equal pay for men and women
- Adoption of the Law introducing into the labour code a right to disconnect

CHANGES TO THE SUBSCRIPTION TAX INTRODUCED BY THE LAW AND GRAND-DUCAL REGULATION OF 21 JULY 2023

The law and RGD of 21 July 2023

The law of 21 July 2023 entered into force on 28 July 2023, and contained many changes amending all of the fund product laws, amongst which changes to the subscription taxes levied on certain funds. At the same time Grand-Ducal regulation was published the purpose of which was to repeal:

1. the Grand-Ducal regulation of 14 April 2003 determining the conditions and criteria for the application of the subscription tax referred to in Article 129 of the law of 20 December 2002 on undertakings for collective investment (repealed by the law of 17 December 2010, relating to undertakings for collective investment (the "**UCI Law**")), and
2. the Grand-Ducal regulation of 27 February 2007 determining the conditions and criteria for the exemption from the subscription tax referred to in Article 68 of the law of 13 February 2007 relating to specialised investment funds ("**SIFs**"), as amended (the "**SIF Law**")

both of which had become obsolete, as a result of the amendments brought about by the law of 21 July 2023.

Key changes to the subscription tax

- **SIF**

In order to encourage investment into European Long-Term Investment Funds ("**ELTIFs**"), the SIF Law now provides that SIFs (or sub-funds thereof) authorized as ELTIFs are exempt from subscription tax.

In addition, SIFs authorized as money market funds ("**MMFs**") are exempt from subscription tax if they (i) qualify as short-term money market funds and (ii) have received the highest possible rating from a recognized rating agency.

In order to benefit from these exemptions, specialized investment funds must disclose the value of their eligible net assets in their periodic filings with the Luxembourg Registration Duties, Estates and VAT Authority (*Administration de l'enregistrement, des domaines et de la TVA*) ("**AED**").

- **RAIF**

RAIFs authorised as MMFs are exempt from subscription tax if they (i) qualify as short-term MMFs and (ii) have obtained the highest possible rating from a recognised rating agency.

Finally, in order to encourage investment into ELTIFs, the RAIF Law now provides that RAIFs (or sub-funds thereof) authorised as ELTIFs are exempt from subscription tax.

- **UCITS & PART II UCI**

In order to align with EU terminology, it is clarified that UCITS & Part II UCIs (or sub-funds thereof) that qualify as MMF's benefit from the reduced subscription tax of 0.01%. The requirements for MMFs to qualify for the subscription tax exemption have been slightly amended to align with EU terminology. UCITS and Part II UCIs (or sub-funds thereof) wishing to benefit from this exemption must (i) qualify as short-term MMF's, (ii) be available only to institutional investors and (iii) have obtained the highest possible rating from a recognized rating agency. In addition, and to support the development of pan-European personal pension products ("**PEPPs**") as requested by the European Commission, UCITS & Part II UCIs reserved for PEPP investors are exempt from subscription tax. Finally, to encourage investment into ELTIFs the new law now provides that Part II UCIs (including sub-funds thereof) authorised as ELTIFs are also exempt from subscription tax.

ESMA OPINION ON UNDUE COSTS REQUIREMENTS FOR AIFS AND UCITS

Background

On 17 May 2023, ESMA issued its opinion on undue costs of UCITS and AIFs (the **"Opinion"**). The Opinion follows ESMAs Common Supervisory Action (**"CSA"**) with National Competent Authorities (**"NCAs"**) launched in January 2021. The aim of the CSA was to assess compliance with the cost-related provisions of the UCITS framework and the requirement that investors not to be charged undue costs.

The CSSF started the CSA in March 2021 and published on 20 October 2022 a "feedback report" to inform the industry about the main observations that the CSSF made in the context of its CSA supervisory work as well as the related recommendations for improvements to the IFMs by the end of March 2023 (see our article published in our newsletter dated 18 January 2023).

In this context, the Opinion contains suggested amendments to (i) Directive 2011/61/EU of 8 June 2011 on Alternative Investment Fund Managers (the **"AIFMD"**); and (ii) Directive 2009/65/EC of 13 July 2009 on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS) (recasts) (the "**UCITS Directive**"), which would require AIFMs and UCITs management companies:

- To act to prevent undue costs being charged to a fund and its investors; and
- To develop a pricing process.

ESMA deems that a lack of supervisory convergence leaves room for regulatory arbitrage and risks hampering competition in the EU market. Moreover, it might lead to different levels of investor protection depending on where a fund or fund manager is domiciled.

Key points covered in the Opinion

A. Clarification on the Notion of Undue Costs in the UCITS Directive and AIFMD

In its Opinion, ESMA considers the following:

1. A further specification of the notion of undue costs in both the UCITS Directive and AIFMD frameworks would provide NCAs with a clearer legal basis to take supervisory and enforcement actions;
2. the European Commission should clarify the eligibility of costs considering the broad "List of costs" (the **"PRIIPs List"**) set out in Commission Delegated Regulation (EU) 2017/653 of 8 March 2017 on key information documents for packaged retail and insurance-based investment products (the **"PRIIPs Regulation"**);
3. European authorities should propose draft regulatory technical standards to specify the circumstances where the costs included in the PRIIPs List should be considered eligible, considering funds' investment policies and to specify the conditions NCAs may authorise on a case-by-case basis additional cost categories not included in the PRIIPs List; and
4. The assessment of costs eligibility (**"Eligibility Test"**) should, according to ESMA, also take account of the relevant fund type as some costs borne by some kinds of alternative investment funds and their investors are not borne by UCITS and their investors. To comply with the Eligibility Test, ESMA considers it important for fund managers to assess the appropriateness of costs on a case-by-case basis, taking account of the fund type and its investment policy.

The proposed legislative amendments to Article 14 of the UCITS Directive and Article 12 of the AIFMD, reflecting the above, are set out in full in the Opinion.

B. Development of a Pricing Process and a Framework for Redress and Sanctions

The Opinion with respect to this matter states the following:

1. Assessment regarding undue costs should also cover as a part of the pricing process a consideration of the quantum of the cost (and not just whether it is undue) ESMA proposes that transactions shall take place at prices or at conditions equal to or better than market standards;
2. ESMA considers that specific attention should be

given to the compliance function of the fund manager to ensure internal controls and appropriate reporting to NCAs and investors of detected shortcomings and the actions to address them;
3. ESMA believes that a legislative proposal should ensure that managers reimburse or indemnify investors without undue delay where undue costs have been charged including where such costs have been incorrectly calculated to investors' detriment; and
4. ESMA believes that NCAs should be empowered to impose sanctions of a minimum given percentage which should be proportionate to unduly charged fees where a manager has intentionally or negligently committed an infringement.

ESMA proposes changes to both the UCITS Directive and AIFMD introducing obligations for managers to develop a pricing process in line with the above.

Conclusions

The Opinion continues the trend towards improving the participation of retail investors in the capital markets by enhancing the fair treatment and protection of every investor whether retail or institutional.

After the issuance of the Opinion, the arguments exposed regarding undue costs were taken into consideration and reflected to a great extent (even if not textually) for the legislative proposal on the Retail Investment Strategy, which was published by the European Commission the past 24 May 2023 amending Directives (EU) 2009/65/EC, 2009/138/EC, 2011/61/EU, 2014/65/EU and (EU) 2016/97 as regards the EU retail investor protection rules and which aims is to empower retail investors, enhance confidence and trust and increase their participation in the EU capital markets.

UPDATE ON CSSF CIRCULAR 21/789 IMPACTING INVESTMENT FUND MANAGERS

In a recent development, the CSSF has issued Circular 23/839, amending circular CSSF 21/789 concerning, inter alia, the self-assessment questionnaire to be submitted annually by investment fund managers and rules concerning the management letter (as amended the "**Circular**"). The Circular specifically addresses investment fund managers ("**IFMs**") governed by Luxembourg laws and parties involved in the operation and control of these entities.

Scope and objective of the revised circular

The Circular defines practical rules regarding the annual preparation and submission of specific documents by IFMs and their approved statutory auditors (*réviseurs d'entreprises agréés* – "**REA**"). Notably, the Circular:

- sets out an obligation for IFMs to submit a self-assessment questionnaire annually and the practical rules associated with it; and
- sets out rules on the engagement of the REA, the statutory audit of IFMs, the management letter and the separate report to be completed by the REA.

Changes in the spontaneous information transmission by IFMs to the CSSF

Initially, the Circular detailed information to be spontaneously provided by IFMs to the CSSF if the REA issued a modified audit opinion during the statutory audit of an IFM's annual report. The section detailing spontaneous information transmission by IFMs to the CSSF in the event of a modified audit opinion by the REA has been deleted.

Key revisions

The circular CSSF 21/789 previously stated that its provisions did not apply to management companies under Article 125-1 of Chapter 16 of the UCI Law. It is now clarified that Points 4.1 and 4.2 of the Circular concerning the statutory audit of an IFM and the management letter, do apply to these management companies.

It is also expressly clarified that the Circular repeals circulars CSSF 18/698 and 19/708 concerning the procedures for transmitting the management letter.

MODIFICATION TO THE FAQ | SUBMISSION OF CLOSING DOCUMENTS AND FINANCIAL INFORMATION BY MANAGERS

On 28 July 2023, the CSSF published In changes to the frequently asked questions regarding the submission of closing documents and financial information by managers (the "**FAQ**"). This article provides a succinct summary of the key changes, tailored for a quick review.

Context

The FAQ provide certain clarifications relating to CSSF Circular 19/708 on the electronic transmission of specific documents to the CSSF using an accepted secure infrastructure.

Recent additions

The changes made reflect certain changes to practice since publication of Circular 19/708. The FAQ reminds managers that for those with an accounting close as of 31 December 2021 and subsequent, the transmission modalities for the recommendation letter are as per CSSF circular 21/789. This circular also outlines the transmission modalities for the self-assessment questionnaire and the separate auditor's report.

The CSSF also clarifies that the organizational chart of the group to be submitted in the approval of the Manager is the one referred to in Point 10 of the CSSF Circular 18/698.

Clarification of the documents to be provided

The CSSF also highlighted that the below cited three documents, while only listed in the Annex of the CSSF circular 19/708 and not in Point 3 of Annex 2 of the CSSF circular 18/698, are also to be submitted annually by authorised AIFMS and management companies. These are:

- Minutes of the governing body's meetings;
- Minutes of the management committee's meetings during the year where AML/CFT topics were discussed; and
- Proof that all conducting officers/managers/directors underwent AML/CFT training.

Transmission procedures

Depending on the document type, two distinct procedures must be followed:

- For the annual report: Submission Financial Reports (*Remise Rapports financiers* 5007 or 5004 or 10033);
- For all other closing documents: Submission Closing Documents (*Remise Documents de clôture* 5556).

For clarity on the practical modalities of preparing and transmitting the self-assessment questionnaire, separate auditor report, and the recommendation/non-recommendation letter required pursuant to circular 21/789 as well as submission deadlines for same, managers and their approved statutory auditors can refer to the eDesk portal under the "Funds and Vehicles" Section.

Date consistency

The CSSF has stressed that documents submitted via the same procedure must have consistent dates in their nomenclature.

Financial information updates

In the "financial information" to be provided by Managers, the CSSF provided examples in the B-2 "Interest and Paid Commissions" post, including retroceded commissions. In the C3-10 line "Equity of the Management Company" post, the CSSF has reminded that "capital equity" should not be considered liquid assets for capital requirements.

CIRCULAR LBR 16/02 | LBR REGISTRATION OF RAIFS

On 23 August 2023, the Luxembourg Business Register (hereinafter "**LBR**") issued circular 16/02 (the "**Circular**") aiming to provide certain clarifications regarding the steps to be taken with the LBR, following the entry into force of the law of 23 July 2016 on reserved alternative investment funds (the “**RAIF Law**”). The Circular has been updated further to the entry into force of the law of 21 July 2023 modernizing the toolbox for Luxembourg funds, which updated, *inter alia*, the RAIF Law (the "**Modernisation Law**"). The Circular cancels and replaces the circular of 3 August 2016.

The Circular in a nutshell

- **Registration of reserved alternative investment funds:** The Circular specifies the information to be provided so that reserved alternative investment funds ("**RAIF**") can be registered in the Trade and Companies Register (“**RCS**”) in the legal form adopted at the time of their incorporation, and in the relevant section.
- **Publication of the notice of incorporation of the RAIF:** It is worth to remind that the Modernisation Law abolishes the need to draw up a *constat de constitution* with a notary for RAIFs established by notarial deed (which is always the case for public limited liability companies (*sociétés anonymes*), private limited liability companies (*sociétés à responsabilité limité*) and partnerships limited by shares (*sociétés en commandite par actions*). Such *constat de constitution* remains necessary only for RAIFs established under private seal.
- **Registration of RAIFs with the LBR:** The Circular specifies that all RAIFs, whatever their legal form, shall request their registration on a list maintained by the LBR in accordance with paragraph (3) of Article 34 of the RAIF Law.

Pursuant to Article 11*bis* of the amended Grand-Ducal regulation of 23 January 2003 implementing the law of 19 December 2002 on the RCS, registration is to be made on paper, by sending a registered letter to LBR. This letter must contain the following information:

- the name and address of the RAIF;
- the name of the management company of the RAIF;
- the date of incorporation of the RAIF (in the case of incorporation by notarial deed) or the date of notarization of its incorporation (in the case of incorporation by private deed).

Any change to the information on the above list shall be notified to the LBR by registered letter.

PREVIOUSLY PUBLISHED IN INVESTMENT MANAGEMENT

- UCIs and virtual assets | CSSF FAQ
- SFDR data collection for Luxembourg investment funds | update
- ESMA updated Q&A on the application of the AIFMD
- Revitalizing EU capital markets: new rules for retail investors
- Navigating the path to ESG transparency: joint consultation paper on review of SFDR delegated regulation
- CSSF SFDR FAQ | Addressing fund name considerations and efficient portfolio management techniques

EC PROPOSAL FOR A TRANSFER PRICING DIRECTIVE

Harmonized TP framework for the EU

On 12 September 2023, the European Commission ("**EC**") introduced a proposal for a Directive on transfer pricing (the "**TP Directive**").

This proposal follows the EC communication "Business Taxation for the 21st Century" on 18 May 2021 and has been issued together with the EC proposal for Directive on Business in Europe: Framework for Income Taxation.

As per the Explanatory Memorandum, the proposal stems from the fact that the arm's length principle, the internationally recognized standard for the pricing of cross border transactions between related parties as enshrined in article 9 of the OECD Model Convention and detailed in the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations ("**OECD TPG**"), is not uniformly applied and interpreted in the EU.

As a result, taxpayers face greater uncertainty (potential double taxation, over-taxation, and high compliance costs) and tax authorities face increased risk of profit shifting and tax avoidance.

The TP Directive puts forward certain remedies notably by incorporating the arm's length principle and key transfer pricing rules, clarifying the role and status of the OECD TPG and easing the process for cross-border TP adjustments.

Harmonized framework

The TP Directive would introduce in EU Member States' domestic legislations:

- The obligation to apply the arm's length principle to cross-border intragroup transactions, restate arm's length conditions if not applied and tax profits accordingly.
- The application of the TP Directive rules consistently with the 2022 version of OECD TPG. The TP Directive shall be amended upon update of the OECD TPG which "should be the new binding reference framework".
- A common definition of associated enterprises which would include:
  - a person participating in the management of another person by being in a position to exercise a significant influence over the other person;
  - a person participating in the control of another person through a holding that exceeds 25 % of the voting rights;
  - a person participating in the capital of another person through a right of ownership that, directly or indirectly, exceeds 25 % of the capital;
  - a person entitled to 25 % or more of the profits of another person;
  - a permanent establishment ("**PE**") would be treated as an associated enterprise. PE is defined by reference to applicable double tax treaty or absent such treaty, by reference to domestic legislation. As a result, transactions between a head office and its PE would be subject to the arm's length principle.

The proposal also allows the Council to issue binding rules through implementing acts notably with respect to certain transactions and safe harbours.

Dealing with cross-border TP adjustments

Where tax authorities of one EU jurisdiction increase the taxable basis of a taxpayer in restating arm's length conditions (i.e., a primary adjustment), the tax authorities where the counterparty is located should proceed to a corresponding adjustment to eliminate potential double taxation. EU Member States shall grant a corresponding adjustment where (i) they agree that the primary adjustment is in line with the arm's length principle, (ii) the primary adjustment resulted in the taxation of profits in another jurisdiction in which the EU located associated enterprise has already been subject to tax and (iii) in case a non-EU jurisdiction is involved, there is a double tax treaty with such jurisdiction.

The TP Directive provides for a so-called "fast track" procedure. Within 30 days EU Member States shall notify the taxpayer of the request's receivability or missing information and, if the primary adjustment took place within the EU, the procedure must be concluded and motivated within 180 days. Mutual agreement

procedures remain applicable in the context of the Arbitration Convention, Directive on tax dispute resolution or joint audits.

Absent any primary adjustment, a Member States may still perform a downward adjustment to the extent (i) it is consistent with the arm's length principle, (ii) an equivalent amount is included in the profits of both associated enterprises triggering a double taxation and (iii) the Member State granting the downward adjustment informs the tax authorities of the other jurisdiction involved.

An adjustment performed by a taxpayer for tax purposes to reflect an arm's length price (i.e., a compensating adjustment), shall be accepted by the relevant EU Member State where (i) the taxpayer initially made reasonable efforts to achieve an arm's length outcome, (ii) a symmetrical adjustment is made in the accounts of all EU parties involved, (iii) the same approach is consistently applied over time, (iv) the adjustment takes place before filing of the tax returns and (v) the taxpayer can explain the difference between the forecast and the result.

Choice of the TP method and arm's length range

The TP Directive relies on the methods provided by the OECD TPG and the taxpayer must chose the most appropriate method under the selection process provided by the TP Directive. Other methods are allowed where it can be demonstrated that the OECD methods are not appropriate or workable and the alternative valuation method or technique results in a more reliable arm's length result.

With the stated objective to reduce dispute and ensure a common approach, where the TP methods produce a range of results, the arm's length result is determined using the interquartile range and, in such case, taxpayer should not be subject to adjustments (unless a different positioning in the range is justified by specific facts and circumstances). Tax authorities can adjust the results to the median of all results where the results of a controlled transaction fall outside of the arm's length range (unless specific circumstances justify other positioning in the range).

Documentation

Taxpayers must maintain appropriate information and analysis proving that transactions with associated enterprises are at arm's length and at least (i) identifying the commercial or financial relations, (ii) determination of the most appropriate method, (iii) comparability analysis and (iv) determination of the arm's length range.

The Commission will further issue a standard template, rules on content and linguistic arrangements, timeframes and taxpayers in scope considering chapter V of the OECD TPG and the Code of conduct on transfer pricing documentation for associated enterprises in the European Union.

Conclusion

Based on the current proposal, EU Member States shall transpose these rules by 31 December 2025 and apply them as from 1 January 2026.

The TP Directive constitutes a first step in the harmonization of the TP rules in the EU, as further binding rules should be issued with respect to specific transactions and the interpretation of the arm's length principle would be shifted from domestic to EU courts.

DIRECTIVE PROPOSAL ESTABLISHING A HEAD OFFICE TAX SYSTEM FOR SMES IN EUROPE

One-stop shop for EU SMEs with EU permanent establishment(s)

On 12 September 2023, the European Commission ("**EC**") proposed a Directive establishing a Head Office Tax system for micro, small and medium sized enterprises and amending Directive 2011/16/EU.

The contemplated Head Office Tax ("**HOT**") system intends to simplify tax obligations of standalone SMEs with one or more permanent establishments ("**PEs**") in other EU Member States.

SMEs with PEs located in the EU can opt to compute the taxable basis of their PEs under the rules applicable to the head office, file a single tax return and pay of the tax liability to the head office Member State, thus interacting only with a single tax authority. The latter would apply the tax rate of the PEs' relevant Member State, exchange the filed return and share tax revenue with relevant Member States. The proposal does not affect allocation of taxing rights applicable under relevant double tax treaties.

Scope of application

The Directive would apply to stand alone SMEs operating in other Member States only through PEs:

- **SME definition:** micro, small and medium-sized is defined by reference to Directive 2013/34/EU on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings.
- **Legal form and taxation:** the SME must be formed under the laws of an EU Member State, have a legal form listed in the appendix to the Directive (which includes corporate entities and certain partnerships) and be subject directly or at the level of its owners to a tax listed by the Directive (the list includes corporate taxes and personal income taxes).
- **Tax residency:** the SME must be resident for tax purposes in a Member State (under domestic legislation and relevant bilateral conventions for the avoidance of double taxation).
- **Stand-alone status:** the SME is not part of a consolidated group for financial accounting purposes and is an autonomous enterprise without being either (i) an associated enterprise as defined under Directive 2013/34/EU or (ii) a linked enterprise as defined under Commission Recommendation 2003/361/EC.

The above-mentioned SMEs are eligible where during the last two fiscal years (i) the joint turnover of its PEs did not exceed the double of the head office's turnover, (ii) it has been tax resident in the head office Member State and (iii) it has qualified as a micro, small and medium-sized under Directive 2013/34/EU.

The option for the HOT system would apply to all EU PEs in existence at the time of the request and those created during the application of the regime.

Head offices deriving shipping income subject to a tonnage tax are excluded from the mechanism.

Mechanics of the HOT system

- **Opting in:** the head office shall notify its domestic tax authorities (i.e., filing authority). If the requirements are met, the latter inform the tax authorities of the PE's Member State (the host Member State) which in turn provides the applicable tax rate.
- **Tax return filing:** the head office files one tax return with its domestic tax authorities computing its own tax liability as well as the tax liability of its PEs using the host Member State tax rules and rates.
- **Tax assessments:** the filing authority issues a tax assessment to the Head Office and draft tax assessments to the PEs. The latter documents, together with the tax return, documentation mandatorily filed under the laws of the head office Member State and relevant information for taxation under the host Member State are provided through automatic exchange of information to the host Member States.
- **Review by host Member States:** the latter can accept or reject the draft tax assessment. If the assessment is rejected, the host Member State must revise this draft tax assessment in connection with the attribution of profits rules under the relevant double tax treaty.
- **Possible appeal by the head office:** the head

office might appeal against the PE's tax assessment accepted by the host Member State before the filing authority and under its domestic rules. Appeal against the PE's assessment revised by host Member State might take place before the Courts of the head office jurisdiction. Disputes on the attribution of profits to the PEs shall be settled under the relevant double tax treaty or the Directive on tax dispute resolution mechanisms in the EU.

- **Collection of tax due:** the head office settles with its domestic tax authorities its own income tax and the tax liability of its PEs. In turn, the filing authority transfers the relevant amounts initially collected with the host Member States.
- **Tax audits:** domestic rules governing tax audits, legal remedies and proceedings remain applicable. Host Member States can also request a joint audit on the computation of the taxable result of the permanent establishment in accordance with the head office taxation rules, the attribution of profits to the permanent establishment and/or the applicable tax rate.

Duration, renewal, and termination of the option

The HOT system applies for a five-year period and its renewal is subject to prior notification.

The mechanism ceases to apply within the five years period when (i) the head office transfers its tax residency outside the Member State or (ii) for at least two fiscal years the joint turnover of the PEs exceeded three times the head office's turnover (the system no longer applies as from the fiscal year that follows the one in which the event takes place).

Transposal and application

Based on the current proposal, Member States must implement the Directive by 31 December 2025 and apply its provisions as from 1 January 2026.

MODERNIZATION OF LUXEMBOURG ACCOUNTING LEGISLATION

Luxembourg government introduced to the Luxembourg Parliament (*Chambre des Députés*) on 31 July 2023 a draft law to modernize the Luxembourg accounting legislation (the "**Draft Law**"). The Draft Law intends to clarify and consolidate general accounting legislation, currently spread in several legislations, into a single accounting law and foresees the introduction of new accounting obligations. If adopted, the provisions of the Draft Law should be applicable as of 1st January 2025.

Consolidation of general Luxembourg accounting rules into a single accounting law

The Luxembourg accounting rules to be consolidated into a single law are the following:

- Bookkeeping and annual inventories as set forth in the Commercial Code;
- Annual accounts and related reports of the amended Law of 19 December 2002 on the register of commerce and companies and the accounting and annual accounts of undertakings;
- Consolidated accounts and related reports of the Law of 10 August 1915 on commercial companies;
- Mandatory report on income tax information from Directive (EU) 2021/2101 of 24 November 2021 currently being transposed in Luxembourg (see our previous newsflash);

The Draft Law proposes to integrate several doctrinal positions issued by the Luxembourg *Commission des Normes Comptables* or "**CNC**" (i.e., the Luxembourg accounting standards committee).

Accounting rules contained in special law are not integrated in the Draft Law but are referred to where relevant:

- Law of 17 June 1992 pertaining to accounting rules applicable to the Banking sector;
- Law of 8 December 1994 pertaining to accounting rules applicable to the Insurance and Reinsurance sectors;
- Law of 11 January 2008 on transparency requirements in relation to information about issuers whose securities are admitted to trading on a regulated market;
- Law of 13 February 2007 on specialised investment funds;
- Law of 15 June 2004 relating to the investment company in risk capital ("**SICAR**");
- Law of 17 December 2010 relating to undertakings for collective investment; and
- The criminal provisions relating to offences and misdemeanours in accounting are maintained in the amended Law of 10 August 1915 on commercial companies.

Moving from a top-down approach to a bottom-up approach and easing the determination of the scope of the different accounting obligations

As per the Draft Law, the regime for small companies should constitute the standard regime for all undertakings (save for micro-undertakings) to be complemented by additional requirements applicable to medium, large and public interest undertakings.

For this purpose, the scope of accounting and filing obligations should be based on an exhaustive listing of undertakings subject to each obligation with the aim to facilitating the determination of the accounting obligations of the different type of undertaking.

Holding undertakings category and audit requirement for large holding undertakings

The Draft Law introduces the notion of holding undertakings defined companies whose principal activity is the holding, financing or management of financial holdings or similar securities held on a long-term basis or with a view to their subsequent sale. Commentary on the Draft Law acknowledges that these holding enterprises are generally subject to the small undertakings' regime, currently excluded from the audit requirement.

The Draft Law also introduces the notion of large holding undertakings defined as holding enterprises subject to the small undertakings' regime but whose total balance sheet exceeds EUR 500 million at the accounting closing date. These large holding undertakings should be subject to the audit requirement.

In addition, the Draft Law explicitly provides that holding undertakings must provide details on the participations held.

Introduction of the micro-undertakings regime and increase of the threshold for small undertakings

Micro-undertakings' regime

The Draft Law foresees the introduction of an option for micro-undertakings, provided for by Directive (EU) 2013/34, that do not exceed the limits of at least two of the three following criteria for two consecutive financial years:

- Balance sheet total: EUR 350.000
- Net turnover: EUR 700.000
- Average number of employees: 10

Application of the micro-undertakings' regime will notably have the following effects:

- Preparation of abridged balance sheet and abridged profit and loss accounts;
- Limited disclosures in the annual accounts (no obligation to prepare detailed appendices to the financial statements provided that certain information is disclosed as footnotes to the balance sheet);
- Exemptions to (i) prepare a management report, be audited by a *réviseur d'entreprises agréé*, (ii) publish the profit and loss accounts.

The micro-undertakings regime should not apply to undertakings qualifying as holding undertakings, credit institutions, undertakings under CSSF supervision, undertakings of the insurance sector, securitization undertakings, reserved alternative investment funds.

Threshold increase for the small undertakings' regime

The thresholds to be met for the application of the small undertakings' regime will be increased as follows:

- Balance sheet total: from EUR 4.4 million to EUR 6 million;
- Net turnover: from EUR 8.8 million to EUR 12 million;
- Average number of employees: 50 (unchanged).

As a result, certain entities subject to the medium undertakings' regime would fall within the scope of the small undertakings' regime and would, notably, be exempt from the preparation of a management report as well as audit by a *réviseur d'entreprises agréé* and have the possibility to prepare an abridged balance sheet and not publish their profit and loss accounts.

Extension of the obligation to prepare financial statements

Entities concerned by such extension are the followings, unless specific legislation provides for derogatory accounting rules:

- Civil companies;
- Agricultural associations;
- Mutual insurance associations;
- Pension savings associations (assep);
- Mutual funds (FCP);
- Temporary trading companies and commercial joint ventures.

Additional filing for special limited partnerships ("SLPs")

SLPs are currently not subject to the (non-public) filing of their financial statements (mainly regulated SLPs). SLPs should be required to file their balance of accounts following the Luxembourg Standard Chart of Accounts on the Luxembourg Trade and Companies Register ("**LTCR**") (these filings being non-public).

This obligation shall not apply to SLPs required to prepare financial statements according to the Draft Law (meaning SLPs of insurance sector, credit institutions, SLPs subject to CSSF supervision, SLPs preparing financial statements under IFRS, SLPs under the securitization regime which are not supervised by the CSSF and SLPs under the RAIF regime).

Clarification of accounting obligations of companies dissolved and put into liquidation

The Draft Law aims at filling certain gaps of current legislation, so that:

- The general accounting principles should continue to apply to companies dissolved and in liquidation but to reflect that the company no longer operates on a going concern basis, accounts should be prepared on a liquidation basis as per CNC Q&A 21/022;
- Companies in liquidation should be required to prepare and file interim annual liquidation financial statements within the 6 months as of the end of the financial year or of the anniversary of the liquidation's opening;
- Financial statements of a company in liquidation

should only be presented to shareholders' general meeting and filed with the LTCR; and

- Upon closing of the liquidation, the last financial statements should be subject to a filing obligation with the LTCR and may have to be published depending on the company's legal form.

Removal of the "commissaire aux comptes" function

The Draft Law proposes to suppress the function of "*commissaire aux comptes*" (statutory auditor) that currently has a supervisory/internal control function for public companies subject to the small-undertakings accounting regime.

Other notable points introduced in the Draft Law

- Interpretation of the **repetition criteria** applied for the determination of the accounting regime (as per CNC Q&A 19/019)
- **Euro Currency** of the financial statements should apply by default and conditions for an alternative currency are included (integrating CNC Q&A 22/026)
- **Duration of the financial year** is defined with the possibility for floating financial years (integrating CNC Q&A 14/003)
- Option to apply the **substance over form principle** as already mentioned in CNC Q&A 14/003
- Accounting for the effects in a **change in accounting methods** shall take place during the financial year such change is decided (integrating CNC Q&A 21/024R)
- Applicable rules to deal with **accounting errors** (integrating CNC Q&A 21/025)
- **Intangible assets with indefinite useful life** might be amortized subject to an annual impairment test based on IAS 36 or alternatively on the accounting standards of another Member State
- Introduction of **key definitions** not foreseen by Directive (EU) 2013/34 for the terms "control" (key notion to determine consolidation requirements), "notable influence" and "joint control"

LUXEMBOURG STARTS TRANSPOSITION OF THE PILLAR TWO DIRECTIVE

On 4 August 2023, the Luxembourg government introduced to the parliament the Draft Law (the "**Pillar Two Draft Law**" or the "**Draft Law**") to transpose Council Directive (EU) 2022/2523 of 14 December 2022 on ensuring a global minimum level of taxation for multinational enterprise groups and large-scale domestic groups in the Union (the "**Pillar Two Directive**" or the "**Directive**").

Background

The Pillar Two Directive implements at EU level the OECD GLoBE Rules on Pillar Two, which were released on 20 December 2021. The Directive provides for adjustments compared to the OECD Model Rules to ensure compatibility with EU law, notably in that it also applies to purely national groups.

Under the Pillar Two Directive, multinational and national groups with an annual revenue of at least EUR 750 million, per the consolidated financial statements of the ultimate parent company, should effectively be liable to a 15% tax in each jurisdiction on the net profits realized by the constituent entities established in that jurisdiction. The level of taxation is assessed on a harmonized taxable basis (i.e., "**Net Qualifying Income**" in the Directive and "**Net GloBE Income**" in the OECD Model Rules) which is to be compared to the taxes effectively paid ("**Adjusted Covered Taxes**" in both frameworks). If the effective tax rate for a jurisdiction is below such agreed minimum rate, an additional amount of tax would be payable ("**top-up tax**") to reach the minimum agreed level of taxation. Parent entities (the Ultimate Parent Entities or UPE, an Intermediate Parent Entity or a Partially Owned Parent Entity as defined in the Pillar Two Directive) should levy the top-up tax through an Income Inclusion rule ("**IIR**"). Where such rule cannot be enforced, the Undertaxed Profits Rule ("**UTPR**" and together with the IIR, the "**GLoBE Rules**") would apply at the level of the constituent entities (i.e., any entity part of a multinational or domestic group) entitling the latter to levy the top-up tax. Jurisdictions considered as low tax jurisdictions are entitled to levy the top-up tax before application of the IIR and UTPR if they implement a Qualified Domestic Top-Up Tax ("**QDMTT**").

Another component of Pillar Two, as agreed by the OECD / BEPS Inclusive Framework, is the Subject to Tax Rule ("**STTR**") allowing source countries to levy additional taxes on certain payments regardless of the allocation of taxing rights under an applicable double tax treaty. The STTR will be implemented separately through a multilateral agreement and will apply in priority to the GLoBE Rules.

The Pillar Two Draft Law closely follows the Pillar Two Directive and provides certain additions derived from the administrative guidelines published by the OECD.

Key characteristics of the Pillar Two Draft Law

- The Pillar Two Directive will be transposed through a separate law and will not be included into the Luxembourg income tax law.
- **Three new taxes have been introduced**: an IIR Tax (*impôt relatif à la règle d'inclusion des revenus*), a UTPR Tax (*impôt relatif à la règle des bénéfices insuffisamment imposés*) and a QDMTT (*impôt national complémentaire*). These taxes are neither creditable nor deductible against other taxes.
- As per the introductory comments to the Draft Law, the Pillar Two Draft Law also takes into consideration the OECD Model Rules, the OECD Commentary on the Model Rules and the OECD administrative guidance issued on 2 February 2023. Items from the latter guidance transposed in the Pillar Two Draft Law notably includes clarifications on entities that are excluded from the scope of application of the rules ("**Excluded Entities**") and exclusion of certain debt releases from the GloBE Income. It remains to be clarified whether and how other elements of the February 2023 OECD administrative guidance as well as the administrative guidance issued in July 2023 will be taken into account during the legislative process.
- The Pillar Two Draft Law also includes the **transitional CbCR Safe Harbour rules** agreed by the OECD Inclusive Framework on BEPS on 15 December 2022. These rules are intended as temporary simplification measures applicable to fiscal years beginning on or before 31 December

2026 but not including the fiscal year that ends after 30 June 2028. The CbCR safe Harbour provides for three alternative tests (a *de minimis* revenue and income test, a simplified ETR test and a route profits test) based on the data available in the Country-by-Country Reports ("**CbCR**") filed by multinational groups. Where one of the tests is met for a jurisdiction, the top-up tax would be deemed as equal to zero for such jurisdiction.

- **Entry into force of the new taxes**: the IIR Tax and the QDMTT will be applicable to fiscal years starting on or after 31 December 2023. The UTPR will be applicable to fiscal years starting on or after 31 December 2024 unless the UPE of the group in located in an EU Member State having opted for a delayed application of the IIR and UTPR under Article 50 of the Directive, in such case the UTPR would apply as from fiscal years starting on or after 31 December 2023.

Transposal options

- The Draft Law does not provide for the option allowed under Article 50 of the Pillar Two Directive for a delayed application of the IIR and UTPR.
- Luxembourg will introduce a QDMTT allowing Luxembourg constituent entities to levy any top-up tax due, should Luxembourg be considered as a low tax jurisdiction for the purpose of Pillar Two, with respect to a given group.
- The UTPR will be introduced as an additional top-up tax rather than as a denial of deduction against taxable income.

Luxembourg specific commentaries on Covered Taxes

Commentaries to the Draft Law provide that for the purposes of computing the effective tax rate of Luxembourg constituent entities, Covered Taxes would notably include corporate income tax, municipal business tax and net wealth tax.

Per the Directive and the Draft Law, the amount of Covered Taxes is reduced by "any amount of current tax expense that is not expected to be paid within three years after the end of the fiscal year." Commentaries of the Draft Law provide that the application of the Luxembourg self-assessment procedure (i.e., issuance of a tax assessment based on the filed tax returns subject to a review by the tax authorities within the statute of limitation) would not imply that the taxes are not to be paid within three years. In addition, the commentaries to the Draft Law provide that the filing of a tax return by a taxpayer, except for specific circumstances, is considered as triggering an expectation that the relevant taxes are to be paid within three years.

Key obligations and deadlines

- **Registration:** Each Luxembourg constituent entity must register with the Luxembourg tax authorities ("**LTA**") within 15 months after the end of the relevant fiscal year (18 months for the transition year which is the first year the multinational group or the domestic group falls within the rules). Any change in status must be notified with 15 months after the end of the relevant fiscal year. A EUR 5,000 fine might apply in case the obligations (registration, notification, deregistration) are not met.
- **GloBE information return:** Each Luxembourg constituent entity must file a GloBE information return. One Luxembourg constituent entity can be designated as the reporting entity. Such obligation would not apply in case the UPE or the designated entity located in another jurisdiction has filed such return in another jurisdiction with which Luxembourg has entered into an eligible agreement allowing for the automatic exchange of such information. The LTA must be notified in such case. The information return must be filed within 15 months after the end of the relevant fiscal year (18 months for the transition year). A fine of up to EUR 250,000 might apply in case of non-filing, incomplete or incorrect filing of the information return and a EUR 5,000 fine applies in cases where the notification obligation is not fulfilled.
- **Top-Up Tax return:** Luxembourg parent entities liable to IIR Tax and constituent entities liable to the UTPR Tax or QDMTT (for the latter taxes a designated constituent entity can be in charge of the obligations) must file a specific return within 15 months after the end of the relevant fiscal year (18 months for the transition year) and the relevant tax must be paid within one month after the filing of the return (interest for late payment might apply and a draft Grand Ducal Decree has been issued to include these taxes within the scope of interests for late payment applicable to the currently applicable Luxembourg taxes). Luxembourg constituent entities are jointly and severally liable for the payment of the

top-up taxes. In case of non-declaration, incomplete or incorrect declaration, the LTA can assess the taxes due under the IIR, UTPR or QDMTT and issue a tax assessment in that respect.
- A draft Grand-Ducal Decree has been issued to clarify that the above-mentioned registration, deregistration, notification and filing **processes should take place electronically**.

Next steps

The legislative process will now continue, notably, by seeking comments from the State Council and other interested parties which could result in amendments to the initial Draft Law.

Per the Pillar Two Directive, the transposition should take place by 31 December 2023.

DOUBLE TAX TREATY LUXEMBOURG | CAPE VERDE

Entry into force

The income and capital double tax treaty between Cape Verde and Luxembourg was signed on 13 January 2022 ("**DTT**"). On 21 June 2023, the Luxembourg Government Council approved the ratification of the DTT.

The DTT will enter into force as from 1 January of the year following the exchange of notification between the contracting states. In Luxembourg, the ratification of the new DTT requires a law, the draft of which (No. 8282) was submitted to the Luxembourg Parliament (*Chambre des Députés*) on 20 July 2023. The entry into force of said law is expected in the course of the year, so that the DTT would likely enter into force as of 1 January 2024, provided the formalities are completed in time in Cape Verde as well.

Tax residency

While the DTT foresees the standard wording with regards to residents, the protocol to the DTT states that undertaking for collective investments that are treated as companies for the purposes of taxation in the contracting state in which they are established are considered as resident of that contracting state and as the beneficial owner of the income they receive, for the purposes of the DTT.

Dividend withholding tax

Withholding tax on dividends paid to beneficial owners resident in the other contracting state cannot exceed 10%. A reduced withholding tax rate of 0% will however be available to distributions made to beneficial owners that is a company holding directly or indirectly at least 10% of the capital of the distributing company for an uninterrupted period of at least 12 months (preceding the dividend payment).

Interest withholding tax

Withholding tax on interest payments made to beneficial owners in the other contracting state cannot exceed 10%. The DTT foresees a withholding tax exemption for interest payments however in very limited situations.

Royalties withholding tax

Withholding tax on royalty payments made to beneficial owners in the other contracting state cannot exceed 10% withholding tax.

Capital gains

While the DTT largely follows the OECD model on the allocation of taxing rights on capital gains to the contracting state where the alienator is a resident, it does not foresee a real estate rich clause. As a result, solely capital gains from the alienation of immovable property situated in the other State; and from the alienation of movable property forming part of the business property of a permanent establishment may be taxed by the other State.

Gains Professional services

Last but not least, the DTT, contrary to the latest developments in the OECD model, includes an article 14 on the taxation of professional services and other activities of an independent character and foresees in addition to the standard criteria of a fixed base (the equivalent of a permanent establishment for professional services) an alternative criterion solely based on a remuneration exceeding EUR 25,000 per year without the need for a fixed base. Meeting one of the alternative thresholds would lead to a taxation right in the source state.

DIRECTIVE PROPOSAL ON BUSINESS IN EUROPE | FRAMEWORK FOR INCOME TAXATION (BEFIT)

A harmonized taxable basis for the EU

On 12 September 2023, the European Commission ("**EC**") proposed a Directive on Business in Europe: Framework for Income Taxation ("**BEFIT**" or the "**Proposal**"). The Proposal replaces to a certain extent the Common Corporate Tax Based and Consolidated Corporate Tax Base proposals and essentially leverages recent developments with respect to (i) Pillar 2 which also starts from a common tax base, (ii) Pillar 1 which proposes formulary apportionment to reallocate certain profits and (iii) the increased administrative capacity of tax authorities across the EU. The EU Member States envision an implementation of BEFIT by 1 January 2028 with an application as from 1 July 2028.

This Proposal follows the EC communication "Business Taxation for the 21st Century" on 18 May 2021 and has been issued together with the EC proposal for Directive on Transfer Pricing.

In addition to a set of common rules to determine the taxable basis of group of companies that have annual combined revenues exceeding EUR 750 million, the Proposal provides for a simplified risk assessment procedure for low-risk distributors and contract manufacturers.

BEFIT clearly provides that an entity in scope "shall cease to be subject to the national corporate tax law in all Member States where it is established in respect of all matters regulated by this Directive" while Member States retain the possibility to determine adjustments applicable to their allocated share of taxable profits.

BEFIT scope

BEFIT should apply to EU tax resident companies and EU permanent establishments belonging to a domestic or multinational ("**MNE**") group that prepares consolidated financial statements and have combined annual revenues of EUR 750 million or more in at least two of the last four fiscal years.

Where the ultimate parent entity ("**UPE**") of the group (i.e., the entity consolidating line by line the assets, the liabilities, income, expenses and cash flow of other entities), is not located in the EU, the combined revenue of the group in the EU must exceed either (i) 5% of the total revenues for the group based on its consolidated financial statements or (ii) the amount of EUR 50 million in at least two of the last four fiscal years.

Where the combined revenue threshold is not met, the domestic or MNE group may opt-in subject to the preparation of consolidated financial statements. The option is binding for a five-year period and should be renewed at the end of the period.

The BEFIT rules are limited to situations where the UPE holds, directly or indirectly, at least 75% of the ownership rights or profit rights in an EU entity during the fiscal year and their EU permanent establishment(s). Sectors such as shipping, international transport and extractive industries are not per se benefiting from a scope exclusion, but their specifics are considered for the purposed of the computation and/or allocation of the tax base.

Preliminary tax result computation for each group member

The computation of the individual tax base of group members starts from the financial accounting net income or loss determined using the same acceptable accounting standard (standard applied by the EU UPE or EU filing entity for groups with a non-EU based UPE).

A set of specific adjustments is then to be applied, notably the exclusion of (i) 95% of dividends and distributions, and capital gains and losses when the BEFIT group member held for more than one year an ownership interest carrying a right to more than 10% of the profits, capital, reserves or voting rights, (ii) ownership interests gains/losses resulting from fair value adjustments, or (iii) the profit or loss of permanent establishments. Interest deduction limitation rules (ATAD regulations), should be restricted to transactions carried out with non-BEFIT group members. Furthermore, specific rules regarding depreciations, stocks, provisions, bad debts, result from long term contracts and hedging instruments are considered.

Change in the BEFIT group size (entities entering or

leaving the group) and business reorganizations are also apprehended through special rules.

Aggregation into a single tax base, allocation, and domestic adjustments

Preliminary tax results of the BEFIT group entities should subsequently be aggregated to form the BEFIT tax base. EC puts forward that such aggregation benefits are threefold: (i) offsetting losses across jurisdictions, (ii) simplified transfer pricing rules for intra-BEFIT group transactions and (iii) withholding tax relief on interest and royalties paid within the BEFIT group if the beneficial owner is part of such group (to be assessed at national level).

BEFIT tax base should then be allocated to each group member by application of an allocation key corresponding to the average of the three prior taxable bases of a group member over the sum of the individual average. During the first year of application, the taxable basis considered should be the domestic tax base to be progressively replaced by the preliminary tax result as computed under BEFIT.

As intra-BEFIT group transactions of the members might affect the allocation key, the proposal includes a simplified transfer pricing assessment based on the variation of income or expenses from these transactions for a given fiscal year compared to their average amount in the previous three fiscal years. A variation of less than 10% will be deemed low risk and at arm's length. Where the 10% threshold is reached or exceeded, pricing will be presumed not at arm's length leading to denial of the portion exceeding 10% for the allocation key purposes (reversal of proof lies with the taxpayer).

This allocation key should be applicable until 30 June 2035. Afterwards, the EC should determine a permanent allocation rule that could be based on formulary apportionment taking into consideration the experience from the first years of BEFIT application and the potential impact of Pillar 2 Directive.

Allocated portion of the tax base should be subject to a common set of adjustments (technical adjustments and commonly accepted tax adjustments within the provisions of domestic legislation). The Proposal foresees possibilities for Member States to set further adjustments (increasing or decreasing the allocated portion) for BEFIT group members resident in their jurisdictions. The Explanatory Memorandum provides that domestic adjustments must respect the rules set by Pillar 2.

BEFIT filings and local assessment

BEFIT will in practice require two levels of filings: (i) one information return for the BEFIT group to be filed by the EU UPE or a designated entity when the UPE is non-EU based and (ii) one local BEFIT return to be filed locally by each individual member of the BEFIT group.

BEFIT teams composed of representatives of the tax authorities from relevant EU jurisdictions should be responsible for the review of the information return and referred to where domestic adjustments might affect such information return.

Local tax authorities should remain responsible for the issuance of individual tax assessments. Tax rate and enforcement rules should continue to rely on domestic legislation. BEFIT group member should be entitled to an administrative and judicial appeal against the individual tax assessments which would be governed by the laws of the BEFIT group member's jurisdiction.

Simplified transfer pricing compliance for low-risk distributors and contract manufacturing

Distribution activities taking place through low-risk distributors and manufacturing activities through contract manufacturer (as defined in the BEFIT proposal) within a BEFIT group or with associated enterprises outside of such BEFIT group should be subject to simplified TP reviews. Entities engaged in additional activities might still benefit from such simplification to the extent that other activities can be segregated or are ancillary and immaterial.

With respect to these activities, the EC intends to publish public benchmarks on which the harmonized risk assessment will be based. Depending on the positioning of the taxpayer within the public benchmark, it will be classified as low risk (above 60th percentile), medium risk (below 60th but above 40th percentile) or high risk (below 40th percentile).

Finally, the Proposal includes a harmonized set of incremental actions local tax authorities may take depending on the risk exposure:

- Low risk: no allocation of resources is needed but adjustment for profits outside the low-risk zone is possible.
- Medium risk: monitoring of the results and seeking information from the taxpayer before initiating risk assessment and audits.

- High risk: recommendation to the taxpayer to review its TP policy and initiating a review or audit.

ECJ ADMITS DIRECT CLAIM FILED FOR REIMBURSEMENT OF OVERPAID INPUT VAT PAID TO SUPPLIERS

Key takeaways

On 7 September 2023, the European Court of Justice ("**ECJ**") issued its ruling in case **C-453/22** where **a VAT taxable person** has been considered **entitled to recover overpaid VAT from VAT authorities** directly when the latter is not in **a position to recover such overpaid VAT** from its suppliers due to civil law limitation periods.

Facts of the case

The plaintiff is a Germany-based farmer and forester and operates a commercial trade in firewood. In the years 2011 to 2013, the plaintiff purchased timber from his suppliers and settled the respective invoices which applied the 19% standard VAT rate. The plaintiff subsequently sold and delivered the wood to his customers as firewood applying the reduced rate of 7%. The upstream suppliers each declared the turnover and paid the 19% input VAT to the tax authorities. The plaintiff declared output sales at 7% and for his part deducted the input tax in respect of its purchases in the amount of 19%.

A subsequent **tax audit** revealed that the reduced VAT rate of 7% should also have been applied on the acquisitions of timber, rather than the standard 19% VAT. **The plaintiff asked his suppliers for corrected invoices and a refund of the excess VAT paid.** However, the latter raised **the objection of the civil law statute of limitation** and refused to correct the invoices and refund the excess VAT.

The plaintiff then turned to the tax office to assert **a direct claim for reimbursement of the overpaid input VAT**. He also claimed **interest on the VAT amount**. He brought an action against the tax office's refusal before the Finance Court of Münster (*Finanzgericht Münster*). In those circumstances, the Finance Court of Münster decided to stay the proceedings and to refer the following question to the ECJ for a preliminary ruling:

In the circumstances of the main proceedings, do the provisions of the VAT Directive – in particular the **principle of fiscal neutrality and the principle of effectiveness** – require that the applicant has **a right to claim reimbursement of the VAT overpaid by the latter to his or her upstream suppliers, including interest, directly from the VAT authorities**?

Outcome

According to the ECJ's decision, **the principle of VAT neutrality and the principle of effectiveness** must be interpreted as requiring that **a receiver of supplies of goods has a direct right to claim from the VAT authorities the reimbursement of improperly invoiced VAT paid to his or her suppliers and paid by those suppliers to the public purse**, together with related interest, in circumstances where :

- first, that **receiver cannot be criticized for fraud, abuse or negligence** but **cannot claim that reimbursement** from those upstream suppliers **due to the limitation period provided for by national law** and,
- second, there **is a procedural possibility of those suppliers subsequently claiming reimbursement of the overpaid VAT from the VAT authorities after having adjusted the invoices** that were issued initially to the receiver of those supplies.

Failing reimbursement of the VAT improperly charged by the VAT authorities within a reasonable time, the damage suffered on account of the unavailability of the amount equivalent to that **improperly charged VAT must be compensated by the payment of default interest**.

SECONDARY RESIDENCE | INTRODUCTION OF TAX BENEFITS

On 18 July 2023, a draft law introducing the concept of secondary residence into Luxembourg tax law and suggesting that certain tax benefits applicable to principal residences be extended to secondary residences (the "**Draft Law**") has been submitted to the Luxembourg Parliament (*Chambre des Députés*).

According to the Draft Law, a secondary residence should be defined as a building which, alongside a natural person's principal residence, is used for residential purposes, without being occupied on a continuous basis.

The Draft Law foresees an extension of the property tax (*impôt foncier*) and non-occupancy tax benefits applicable to principal residences to secondary residences.

The Draft Law is part of a wider reform of Luxembourg property tax and the introduction of a non-occupancy tax (draft law No. 8082 submitted on 10 October 2022). As it stands, the planned reform provides for a EUR 2,000 allowance for property tax purposes and a complete exemption from non-occupancy tax for the principal residence. The Draft Law proposes to extend these benefits to secondary residences.

It should however be noted that the Draft Law explicitly states that, as far as direct taxation is concerned, the exemption for principal residences will not apply to secondary residences.

AMENDMENTS TO THE LUXEMBOURG - GERMANY DOUBLE TAX TREATY SIGNED ON 6 JULY 2023

On 20 September 2023, the Luxembourg government submitted to the Luxembourg Parliament (*Chambre des Députés*) draft law No. 8311, aiming to ratify the amending protocol to the double tax treaty between Luxembourg and Germany (the "**DTT**"), as agreed and signed on 6 July 2023 in Berlin (the "**Draft Law**").

The notable changes introduced by the amending protocol concern both the DTT itself as well as the former protocol from 2012 and are as follows:

Preamble

In line with the BEPS actions, the preamble has been adapted to clarify that the purpose of the DTT is to eliminate double taxation, without however creating the possibility of non-taxation or reduced taxation through tax avoidance or fraud. The protocol also adds the principal purpose test into the DTT, such that benefit will be denied if it is reasonable to conclude that obtaining that tax benefit was one of the principal purposes of any arrangement or transaction (subjective test). However, DTT benefits will still be granted if it can be demonstrated that granting such benefits, in the circumstances at hand, would remain in accordance with the object and purpose of the relevant provisions of the DTT (objective test).

Persons covered

Article 1, relating to covered persons has been enhanced by a new paragraph, which provides *inter alia* that the benefit of the DTT shall not be granted to tax transparent entities.

Interests

Article 11 of the DTT on interests is now worded in accordance with the OECD Model Tax Convention, in that the recipient of the interest payment needs to be the beneficial owner of such interest payment for Article 11 to apply.

Dividends

The DTT now contains a specific provision regarding the treatment of dividends paid by real estate investment trusts (so called "**REITs**") or paid to undertakings for collective investments ("**UCIs**"), which are now subject to a 15% withholding tax.

The amended DTT foresees in its protocol that the term UCIs shall mean – as far as Luxembourg is concerned – UCIs subject to the law of 17 December 2010, specialised investment funds within the meaning of the law of 13 February 2007 and the reserved alternative investment funds within the meaning of the law of 23 July 2016, to the extent such UCIs do not take the form of a partnership. For Germany, this term covers any investment fund in the sense of the Investment Tax Act. The door has also been left open for other undertakings which may be widely held, hold directly or indirectly a diversified portfolio of securities or with the main purpose of investing directly or indirectly in immovable property with the aim of realising rental income, provided that they are subject to investor protection regulations in the contracting state of their establishment and have been set up in one of the contracting states, to be included, pursuant to an agreement between the competent authorities of the contracting states,

Remote working

The new version of the DTT provides for an increased tolerance threshold from 19 to 34 days of remote workdays for cross-border workers. By application of this increase of the tolerance threshold, cross-border workers, tax resident in Germany within the meaning of the DTT, employed in Luxembourg and exercising their salaried activity for up to 34 days outside of the Luxembourg territory, shall remain subject to tax in Luxembourg on such employment income.

The benefit of this 34-days tolerance has also been expanded to persons covered by Article 18 of the DTT, relating to public functions.

Finally, among the main clarifications made in the protocols on the taxation of employees, the following two are to be noted:

- an activity as an employee is only considered to be carried out during a working day in a contracting State when that activity is carried out for at least 30 minutes. This means for example that a cross-border German tax resident employee who reconnects from home in the evening to send emails for more than 30 minutes would be considered to have worked from

Germany during that day, reducing the number of remaining tolerance days;
- in respect of remunerated on-call services, the right to tax on-call allowances belongs to the State where the person is physically present, even when the employee has not been called for service.

Abolition of arbitration procedure

Finally, the amending protocol specifies that the arbitration procedure provided for in paragraph 5 of Article 24 of the DTT will no longer apply to cases submitted on or after 1 January of the calendar year immediately following the year in which the amended protocol enters into force.

LUXEMBOURG LOWER TRIBUNAL RULES ON TAX TREATMENT OF REDEMPTION OF CLASSES OF SHARES

On 14 June 2023, the Luxembourg Lower Tribunal handed down a judgment regarding the tax treatment of the repurchase of a class of shares and the application of the general prohibition of abuse in tax law.

In the case at hand, the tax administration challenged the tax treatment of the repurchase of two classes of shares, held by non-resident shareholders, immediately followed by the cancellation of the said shares, on the grounds that the transaction was abusive within the meaning of § 6 of the *Steueranpassungsgesetz* ("**StAnpG**"). The tax administration argued that the repurchase price paid to these non-resident shareholders should be deemed a dividend distribution subject to 15% withholding tax.

The Luxembourg Lower Tribunal first held that the repurchase price paid by a company for the buy-back of its own shares should *a priori* be treated as capital gain income in the hands of the non-resident shareholders in so far as the shares were cancelled and the company's capital reduced. This principle was however subject to several limitations, notably the general prohibition of abuse in tax law.

The Lower Tribunal recalled that in the event the price actually paid by the company to its shareholders in connection with the repurchase of its shareholding exceeds the fair market value of that shareholding and the price can only be explained by the existence of the shareholder relationship, the excess price may be qualified as a hidden distribution subject to 15% withholding tax.

In addition, the Lower Tribunal considered whether the repurchase should be found abusive, within the meaning of § 6 StAnpG. The Lower Tribunal highlighted the following features:

- The classes of shares were not created *ab initio*, but during the life of the company and following receipt of two dividend distributions;
- The classes of shares did not have different economic rights;
- The redemption and cancellation of a class of shares entitled each shareholder, on a pro rata basis, to an identical amount regardless of the shareholder or the concerned class of shares;
- The company had received dividend distributions shortly prior to the redemption of shares.

In light of these above features, the Lower Tribunal held that in the case at hand, the repurchase should be deemed abusive and considered, from an economic perspective, as a dividend distribution. The Lower Tribunal found that the repurchase had enabled the company to circumvent the withholding tax on dividends which should have applied. The company failed to present any non-tax motives which would have justified the transaction.

This judgment is a welcome addition to the recent line of case-law from the Luxembourg administrative courts confirming and refining the treatment of a repurchase of classes of shares under Luxembourg law.

A SUSPENSION OF THE TAX LIMITATION PERIOD COMPLIES WITH PRINCIPLES OF LEGAL CERTAINTY AND EFFECTIVENESS OF EU LAW

On 13 July 2023, in its judgement rendered in case C-615/21, the European Court of Justice (the "**ECJ**") ruled that the interruption of the statutory limitation period in respect of the right of the tax authorities to assess VAT is in line with the principles of legal certainty and of effectiveness of the EU.

Facts of the case

In the case at hand, following a tax inspection, the Hungarian tax authorities (the "**HTA**") considered that certain VAT transactions realised by a Hungarian company (the "**Company**") were unrelated to an economic operation and considered as a tax fraud. As a result, the HTA assessed VAT, imposed a fine and a late-payment penalty to the Company.

A long administrative and judicial procedure with multiple iterations followed. The administrative decision taken by the HTA was first set aside by the Budapest Administrative and Labour Court, as being vitiated by contradictory reasoning, and a new procedure was initiated. A second administrative decision, adopted by the HTA, suffered the same fate, since the court considered that it substantially reproduced an identical reasoning. When an appeal against a subsequent, third administrative decision, which was still unfavourable for the taxpayer, was brought before the Hungarian courts, the applicant argued that the repeated adoption of decisions is contrary to the principle of legal certainty which the limitation period is supposed to protect.

The referring court noted in that respect that no limit on the number of times a tax procedure may be repeated by the HTA was foreseen under Hungarian law and that, pursuant to domestic case law, the statutory limitation period is suspended throughout the entire duration of the judicial review of a decision taken by that authority. Accordingly, there is no limit on how long the suspension of the limitation period in cases of judicial review can last, with the result that the tax authority's right to assess VAT amounts to be repaid could be extended by a number of years or even, in extreme cases, by decades. For that reason, the referring court had doubts as to the compatibility of the Hungarian legislation and administrative practice with the principles of legal certainty and effectiveness.

Key features of the ECJ's reasoning

The ECJ first noted that, as EU law currently stands, it does not lay down a period within which the right of the tax authorities to assess VAT is time-barred, and it also does not, *a fortiori*, specify the circumstances in which such a period ought to be suspended. It is therefore for the Member States to establish and apply rules on limitation periods in relation to the right of the tax authorities to assess VAT including the procedures for suspension and/or interruption of that limitation period. When doing so, the Member States must ensure consistency with EU law, which requires reasonable time limits to be laid down which protect both the taxable person and the tax authority.

The ECJ further recalled that the principle of legal certainty is aimed at ensuring foreseeability of situations and requires, *inter alia*, that the tax position of a taxable person having regard to his or her rights and obligations *vis-à-vis* the tax or customs authorities should not be open to challenge indefinitely. This principle however is not absolute and must be weighed against other requirements resulting from EU law, such as those to ensure the fulfilment of the obligations arising from acts adopted by the EU institutions, such as the EU VAT directive. Accordingly, the national rules laying down the rules for the suspension of the limitation period in respect of the right of the tax authority to assess the VAT due must be devised in such a way as to find a balance between, on the one hand, the requirements inherent in applying the principle of legal certainty and, on the other hand, those enabling the EU VAT Directive to be implemented effectively and efficiently.

The ECJ found that, although the Hungarian legislation at issue is capable of causing the duration of the limitation period to be extended, it is however not capable, in principle, of causing the situation of the taxable persons concerned to be under challenge

indefinitely. By contrast, according to the ECJ, the suspension of the limitation period foreseen under Hungarian law makes it possible to ensure the effective and efficient implementation of the EU VAT Directive.

Conclusion

The ECJ concluded that the principles of legal certainty and effectiveness do not preclude national legislation and administrative practice which provides that the limitation period in respect of the right of the tax authorities to assess VAT is to be suspended for the whole duration of judicial review, regardless of the number of times the administrative tax procedure concerned has had to be repeated following those reviews and with no ceiling on the cumulative duration of the suspensions of that period.

REFERENCE FOR PRELIMINARY RULING TO THE ECJ REGARDING LEGAL PROFESSIONAL PRIVILEGE AND EXCHANGE OF INFORMATION

In a judgment dated 11 July 2023 (*docket No. 48677Ca and 48684Ca*), the Luxembourg Higher Administrative Court (*Cour administrative*) (the "**Court**") referred several questions to the European Court of Justice (the "**ECJ**") for a preliminary ruling. The questions focus on the application of legal professional privilege in the context of the exchange of information upon request in tax matters introduced by the Directive 2011/16/EU of 15 February 2011 on administrative cooperation in the field of taxation (the "**Directive**").

In the case at hand, following a request by the Spanish tax authorities, the Director of the Luxembourg Direct Tax Administration (*Administration des Contributions Directes*) (the "**DTA**") ordered a Luxembourg law firm to disclose a set of documents relating to a transaction it had advised on. The Luxembourg law firm refused to provide the documents on the grounds of the latter being protected by legal professional privilege.

In the context of the case pending before the Court, the question arose as to whether the Directive complied with the Charter of Fundamental Rights of the EU (the "**Charter**") and, in particular, with Articles 7 (respect for private and family life) and 52(1) (scope of guaranteed rights) of the Charter.

In particular, by reference to the conclusions drawn by the ECJ in existing case law at the EU level, namely the ruling of 8 December 2022 in *Orde van Vlaamse Balies*, (*case C-694/20*), concerning notification obligations for lawyers under the Directive 2018/822 of 25 May 2018 on mandatory automatic exchange of information in the field of taxation in relation to reportable cross-border arrangements, the Court recalled that the rights enshrined in Article 7 of the Charter are not absolute rights but must be considered in relation to their function in society. Additionally, the provision in Article 52(1) of the Charter allows for limitations to be placed on the exercise of those rights, provided that those limitations are provided for by law, that they respect the essence of those rights and that, in compliance with the principle of proportionality, they are necessary and they genuinely meet objectives of general interest recognised by the EU, or the need to protect the rights and freedoms of others.

However, insofar as the Directive does not specifically regulate the actual scope of the limitation on the exercise of the right to privacy in its specific emanation relating to correspondence between a lawyer and his client, the Court raises the question of its conformity with the Charter. Indeed, the Directive simply gives Member States the possibility (but not the obligation) to refuse the exchange of information in cases where it *"would lead to the disclosure of a commercial, industrial or professional secret or of a commercial process, or of information whose disclosure would be contrary to public policy"* (Article 17(4) of the Directive). However, it does not provide for a framework for the exchange of information covered by professional secrecy (in particular that of a lawyer), in the event that a Member State chooses not to systematically refuse to transmit such information.

If the ECJ were to consider that the Directive complies with Articles 7 and 52(1) of the Charter, the Court also raises the question as to whether the scope of the duty of cooperation of lawyers (or of a law firm), in their capacity as third parties holding information in the context of the application of the mechanism for the exchange of information upon request, in particular, specific limitations to take into account the effect of their legal professional privilege can be governed by the provisions of domestic law of each Member State.

Finally, if the ECJ arrives at the conclusion that the scope of the duty of lawyers to cooperate may indeed be governed by the provisions of each Member State's domestic law, the question arises, whether, in order to comply with Article 7 of the Charter, a national legal provision must include specific conditions which ensures respect of the essence of the confidential nature of communications between lawyers and their clients and reduces the lawyer's obligation to cooperate, to that which is appropriate and necessary for the achievement of the objective of the Directive.

The ECJ is expected to render a final decision in the coming months.

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- Opinion of the Advocate General of the European Court of Justice in the Engie Fiscal State Aid Case
- Draft law No. 8207: new reporting obligations for payment service providers to prevent VAT fraud
- Implementation of DAC 7 into Luxembourg Law

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