LUXEMBOURG

Overview

ATOZ Tax Advisers, Taxand Luxembourg

With over 70 tax practitioners, ATOZ is a high-end, independent advisory firm offering a comprehensive and integrated range of tax and transfer pricing services. Our collective industry expertise encompasses local and global companies in a wide variety of industry sectors, including – but not limited to – investment funds (real estate, private equity, infrastructure, venture capital, debt funds), aviation, banking, capital markets, communications, financial services and insurance.

In the field of transfer pricing, we assist our clients with the development of transfer pricing strategies, the preparation of transfer pricing documentation, regular risk reviews and disputes (local and cross-border).

Our transfer pricing expertise covers a broad spectrum of areas, such as financing activities, mere intermediary services, interest rate assessments on a wide range of debt instruments, fund management services, operational services, debt/borrowing capacity analyses, valuation of tangible and intangible assets, attribution of profits between a permanent establishment and its head office.

General: Transfer Pricing Framework

Luxembourg tax law does not provide for integrated transfer pricing legislation. Transfer pricing adjustments with the objective to restate arm's length conditions can be made on the basis of different tax provisions and concepts applicable under Luxembourg domestic tax law. The arm's length principle is explicitly stated in Article 56 of the Luxembourg Income Tax Law (hereafter: "LITL"). Article 56 of the LITL is complemented by Article 56bis of the LITL which provides more guidance on the application of the arm's length principle under Luxembourg tax law. More precisely, Article 56bis of the LITL formalises the authoritative nature of the OECD Transfer Pricing Guidelines and replicates some of the key concepts provided in Chapter I (Arm's length principle) of the OECD Transfer Pricing Guidelines.

The law might be amended to introduce new rules specifically for multinational groups (Bill of Law No. 8186, 28 March 2023).

In addition, a transfer pricing decree on intra-group financing activities contains additional guidance and requirements in this specific context.

Accepted Transfer Pricing Methodologies

The OECD Guidelines are not incorporated in Luxembourg legislation but are an explicit point of reference and guidance.

Therefore, the general hierarchy of transfer pricing methodologies is commonly accepted and no method is *per se* rejected, if its use is justified in the individual case at hand (noting that certain market practices have developed over time for a number of transactions).

The taxpayer is, however, free to choose another method if he can substantiate the appropriateness for the use of such method in light of an arm's length result.

The most commonly used method is the comparable uncontrolled price method, mainly for a wide range of financial transactions and license fees. However, other methods such as the cost-plus method (for low value-adding services) as well as the profit split (e.g. for highly integrated fund management activities) are regularly relevant in practice as well.

Transfer Pricing Documentation Requirements

Taxpayers are not explicitly required to prepare annual documentation (although this may be effectively required depending on the case at hand) and are not required to file transfer pricing documentation with the local tax authority (but to be provided upon request). Transfer pricing documentation should be prepared at the time the transaction is entered into (or even before) in order to reduce the risk of challenge.

While there are no legal de minimis thresholds, in practice all material related-party transactions are covered by an appropriate transfer pricing documentation and pragmatic approaches may be chosen for small transactions with immaterial tax risks.

Luxembourg taxpayers may indirectly be obliged to prepare a master or local file, if this is imposed by another jurisdiction (i.e., the jurisdiction of a subsidiary or parent company).

With effect as from tax year 2024, new documentation requirements might also be introduced for Luxembourg group companies of multinational groups that fall within the scope of country-by-country reporting (i.e. with a consolidated turnover of at least EUR 750 million).

Luxembourg companies forming part of such multinational groups would have to prepare a local file and a master file, under certain circumstances.

The master and local file requirements broadly correspond to BEPS Action 13, with some exceptions, deviations and additional local requirements.

Local Jurisdiction Benchmarks

Given the absence of Luxembourg-specific benchmarking data, the Luxembourg tax authorities generally accept pan-European benchmarks, provided that they meet OECD-compliant search strategy standards. Multiple-year data are not commonly used. The use of interquartile ranges in terms of benchmarking is generally feasible with a preference for measures of central tendency. A yearly update is not explicitly required and in practice, most taxpayers do not update their benchmark searches on an annual basis. In cases where a business activity does not undergo significant changes, a search can be updated every 3 years.

LUXEMBOURG

Advance Pricing Agreement "APA"/Bilateral Advance Pricing Agreement "BAPA" Overview

Despite the legal possibility to do so, the number of APA in Luxembourg is extremely limited in practice.

Transfer Pricing Audits

Within the statute of limitation, the Luxembourg tax authorities can perform audits at their discretion. Matters of interest seem to be focused on financial transactions. The Luxembourg tax authorities do not conduct audits in great numbers compared to the number of taxpayers. However, since a couple of years, tax inspectors are highly likely to review transfer pricing aspects in more detail and request detailed documentation.

The Burden of Proof in Transfer Pricing: Theory versus Practice

Under Luxembourg tax law, the burden of proof is generally shared between the taxpayer and the Luxembourg tax authorities. The burden of proof for facts and circumstances that result in an increase in the taxpayer's taxable income rests with the Luxembourg tax authorities, while the burden of proof for facts and circumstances that result in a decrease in the taxpayer's taxable income rests with the taxpayer (Article 59 of the Law of 21 June 1999; BFH, Decision of 24.6.1976, IV R 101/75, BStBl II 1976, p. 562; BFH, Decision of 11.4.1984, I R 175/79, BStBl II 1984, p. 535). Thus, a distinction must be made between upward and downward adjustments with respect to the burden of proof for transfer pricing adjustments.

Burden of proof in case of upward adjustments

The burden of proof that transactions are not at arm's length generally rests with the Luxembourg tax authorities. It is up to the administration to verify whether the transfer prices for goods and services transferred between group companies are in line with the arm's length principle.

In practice, although the burden of proof is on the tax authorities, they can still reasonably require a Luxembourg company to provide consistent arguments regarding its transfer pricing (RFH, Decision of 21.12.1938, RStBl 1939, p. 307; BFH, Decision of 7.4.1959, I 2/58 S, BStBl III 1959, p. 233). In this regard, the company must consider that the voluntary production of documents can significantly improve the persuasiveness of the company's transfer pricing approach to the tax authorities.

Burden of proof in case of downward adjustments

In the case of hidden capital contributions and "downward adjustments" under Article 56 LITL, the fair market value of the advantage shifted to a Luxembourg company is deducted from the company's taxable income. It follows that the facts and circumstances underlying the advantage shifted to a Luxembourg company must be proven by the taxpayer.

In practice, in these situations, the Luxembourg tax authorities may reasonably require that the value of a hidden capital contribution or the advantage that would result in a downward adjustment under Article 56 LITL be substantiated in a transfer pricing study.

Transfer Pricing Penalties

There is no specific penalty for the non-preparation of transfer pricing documentation, but the non-availability of such documentation upon request of the tax authorities significantly increases the risk of adjustments.

Local Hot Topics and Recent Updates

Although it has been outstanding since 2023, the potential introduction of master and local file requirements for certain multinational groups as from the fiscal year 2024 marks a milestone in the development of Luxembourg transfer pricing rules.

In line with long-standing views from practitioners, recent court cases have shown that the delayed preparation of transfer pricing documentation long after the transaction date (e.g. only upon request by the tax authorities some years later during a tax audit or review of the tax returns) significantly increases the risk that the result of such belated transfer pricing studies will be rejected/challenged as a matter of principle (and due to a lack of credibility of such delayed documentation when the benchmark analysis happens to confirm the transfer price that has been charged in a given undocumeted transaction).

MNEs with significant ESG initiatives may face new considerations when pricing their intra-group transactions, especially if these initiatives are tied to sustainability-linked financing or green IP structures.

Finally, the implementation of BEPS 2.0 (Pillar One & Two) reflects the evolving regulatory environment and the increasing complexity of managing intra-group transactions.

LUXEMBOURG

Documentation threshold

Master file	Not Applicable (draft Law)
Local file	Not Applicable (draft Law)
CbCR	EUR 750m consolidated group turnover

Submission deadline

Master file	Not yet specified in the draft law
Local file	Not yet specified in the draft law
CbCR	12 months after the final day of the reporting fiscal year of the MNE group

Penalty Provisions

Documentation – late filing provision	Not Applicable
Tax return disclosure – late/incomplete/no filing	Up to 10 percent of the tax due and a fine up to EUR 25,000
CbCR – late/incomplete/no filing	Up to EUR 250,000

CONTACT

Oliver R Hoor
ATOZ Tax Advisers
Oliver.Hoor@atoz.lu
+352 26 940 646

Fanny Addouda
ATOZ Tax Advisers
Fanny.Addouda@atoz-services.lu
+352 26 9467 714