

# Transfer Pricing Country Summary

## Luxemburg

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## 1. Introduction

In Luxembourg, the transfer pricing principles are laid down in:

- Article 56 and new Article 56bis of the Luxembourg Income Tax Law;
- Circular LIR No 56/1-56bis/1.

These rules respect the OECD Transfer Pricing Guidelines. The Luxembourg tax authorities can apply an adjustment if transactions between connected firms (international or domestic) do not meet the arm's length norm.

Specific provisions apply to Luxembourg companies performing intra-group financing transactions, which must also:

- Have genuine substance;
- Bear economic risks;
- Report an arm's length remuneration on their financing activities.

The arm's length character of the remuneration must be supported by a transfer pricing analysis.<sup>1</sup>

There is no contemporaneous transfer pricing documentation required in Luxembourg. However, per article 171 of the LIR, a Luxembourg taxpayer with intra-group transactions is required to maintain transfer pricing documentation.

The taxpayer does not have to file the documentation with for example its corporate income tax return, but has to provide documentation upon request to the tax authorities. There is no specific timing in terms of providing the information. A reasonable timing will be provided by the tax authorities.

## 2. Laws & Regulations

### a) References to OECD/EU/Local Rules

The Luxembourg law on transfer pricing is concisely expressed in article 56 of the Luxembourg Income Tax Code and in the general tax law.

As of the Law of 19 December 2014, a more detailed framework for transfer pricing was added. This brought changes to the article 56 of the Luxembourg Income Tax Code (ITL), which now states: "When an enterprise participates, directly or indirectly, in the management, control or capital of another enterprise, or where the same individuals participate, directly or indirectly, in the management, control or capital of two enterprises and where, in either instance, the two enterprises are, within their commercial or financial relations subject to conditions made or imposed which differ from those

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<sup>1</sup> [Transfer pricing in Luxembourg | Practical Law \(thomsonreuters.com\)](#)

which would be made between independent enterprises, the profits of these enterprises are to be determined under conditions prevailing between independent enterprises and taxed in consequence.”

The law of 19 December 2014 introduces a new sub-article in paragraph 171 of the general tax law, which clarifies that entities will find it mandatory to provide documentation when the tax authorities are seeking the verification of transfer prices. Further on, there is no clear specification of the documentation required.

This law applies as of 1 January 2015 and defines the arm's length principle according to Article 9 of the OECD Tax Model Convention. Furthermore, this implies that the arm's length principle applies to transactions between a local entity and a foreign entity, as well as two entities located and taxed in Luxembourg.

Moreover, the Income Tax Code embraces 2 circulars, Circular ITL no 164/1 dated 9 June 1993, and Circular ITL no. 164/1 dated 23 March 1998, which refer to shareholders accounts and define transactions that can be seen as hidden distribution of profits and hidden contribution. Article 164 specifies that the hidden distribution and hidden contribution of profits shall be included in the taxable basis.

“A hidden distribution of profits is considered when a shareholder or an interested person receives directly or indirectly advantages which he normally would not have received if this relationship had not existed.”

The following transactions may, inter alia, be treated as hidden distribution profits:

- Increased buying prices or reduced selling prices;
- Loans made to shareholders either free of interest or at an unreasonably low rate of interest, or loans given without the intention of repayment;
- Loans from shareholders at an unreasonably high interest rate.

The advantage granted is included in the taxable basis and the funds not received are considered to have been distributed to the shareholders as a dividend subject to the standard withholding tax rate unless a reduction or exemption applies. This distribution is not automatically deemed to be net of withholding tax. To tax using this basis, the Luxembourg tax authorities would have to show that the payer was willing to pay the withholding tax.

A hidden contribution is deemed to take place if a parent company grants an advantage to a subsidiary because of their group relationship.

The following transactions may, inter alia, be treated as hidden contribution:

- Reduced buying prices or increased selling prices;
- Loans from shareholders either free of interest or at an unreasonably low rate of interest;
- Loans to shareholders at an unreasonably high interest rate.

If the parent is a Luxembourgish company and the subsidiary a foreign company in line with arm's length principles sufficient interest should be calculated on the receivable in the hands of the Luxembourgish parent company. In the situation where a foreign parent grants an interest-free loan to a Luxembourg subsidiary, the interest-free character of the loan is perfectly possible from a Luxembourg tax point of view.

Circulars 164/2 of January 28, 2011 and 164/2 bis LITL of April 8, 2011 replaced by Circular nr 56/1-56bis/1 of December 27, 2016, specifically focusing on intra-group financing activities (the "2017 Circular").

## b) Definition of Related Party

Article 56 and 56bis LITL follow the definition of related party included in Article 9 of the OECD model tax treaty: "two enterprises are deemed associated when one enterprise participates, directly or indirectly, in the management, control or capital of the other, or if the same persons participate, directly or indirectly, in the management or share capital of both enterprises."

The following situations can be considered as evidence to determine this relation

- direct or indirect majority (more than 50%) shareholding (voting rights);
- common direct or indirect majority shareholder;
- one is able to appoint or dismiss the majority of the key management or the supervisory board of the other enterprise;
- foreign entrepreneur with domestic branch;
- domestic entrepreneur with foreign branch;
- same management.

## c) Nature of Transfer Pricing Documentation

Luxembourg, as an Organisation for Economic Co-operation and Development (OECD) member, has approved both the OECD Transfer Pricing Guidelines and the OECD Model Double Taxation Convention on Income and on Capital 2014, seen as a model to sign more than 77 double tax treaties (DTTs) currently entered by Luxembourg.

## d) Tax Havens & Blacklists

The bill prohibiting (under certain conditions) the tax deductibility of interest and royalties due to associated enterprises located in a country listed on the EU list of non-cooperative jurisdictions, usually referred to as the "EU Blacklist," was enacted by the Parliament on January 28, 2021. Such law follows guidance of the Council of the European Union ("EU Council"), that released recommendations

in 2019 promoting EU Member States to implement national defense actions in relation to jurisdictions on the EU Blacklist.<sup>2</sup>

### e) Advance Pricing Agreement (APA)

The Law of 19 December 2014 introduces new regulated APAs procedures, aiming to provide legal certainty to the taxpayers and increase transparency of the transfer pricing system. By this matter, the APA practice applies also to other intra-group services, as an extent to the Circular letter of 2011, which imposes APAs only for intra-group financing transactions. It is also understood that tax rulings and APA's may be subject to exchange of information, in particular with the relevant authorities of other EU Member States.

In order to obtain a tax ruling, the taxpayer needs to formulate a sufficiently reasoned written request, mentioning the following details:

- full information of the applicant (name, residence and file number, if any), the parties and other concerned third parties, as well as a description of their respective activities;
- a detailed description of the intended transactions;
- a detailed analysis of the legal issues, as well as a duly motivated assessment of the legal situation of the applicant; and
- the confirmation that all information which is submitted is complete and correct.

The law also specifically mentions the administrative fees that apply, between €3,000 and €10,000, according to the level of complexity of the case. The fees are due in one month following the confirmation of the tax authorities and are not reimbursable.

The tax inspector may issue an advance decision relating to the application of Luxembourg tax law to one or more transactions envisaged by a taxpayer. The validity of the advanced decision is five years from the date of the agreement and it is binding only in the following situations:

- the situations are incorrect or have errors;
- the resulting situation is different from the one described in the request;
- the advanced decision is not compliant, or no longer compliant, with the law.

As of the Law of 19 December 2014, a tax ruling commission is created, namely the Advance Decision Commission, and it is in charge of providing advice for advanced tax confirmations, assuring an equal treatment between taxpayers. A summary of these advance decisions is going to be anonymously published.

Rulings are subject to mandatory exchange. To this effect a form 777 E must be filed electronically, and this form contains a summary of the ATA / APA.

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<sup>2</sup> [Luxembourg Tax Alert 2021-04 - Newsletter - KPMG Luxembourg \(home.kpmg\)](#)

Companies wishing to seek for a confirmation have to introduce a formal request, through a process defined in the Circular of 19/12/2014, and for content related information, refer to section 5 of the 2017 Circular. Filing fees are applicable and range between EUR 3K to EUR 10K depending on the complexity of the file. As from January 1, 2017, all administrative decisions that were based on rules applicable before the entry into force of article 56bis LITL, are no longer binding the tax authorities.

#### f) Audit Practice

As part of the 2017 tax returns, the tax authorities established disclosure requirements on transfer pricing, allowing them to determine whether Luxembourg taxpayers are involved in intercompany transactions. To examine conformity with the arm's length principle, transfer pricing documentation may be requested for a desktop assessment or in preparation for a tax audit.<sup>3</sup>

### 3. Transfer Pricing Documentation

#### a) Level of Documentation

The Master File discloses general information relating to the Group (Group TP policy, allocation of activity between the group entities etc.).

The main focus is, nevertheless on the Local File, which needs to be organized as follows:

##### Industry analysis

- a) Activity of the Group and main competitors;
- b) Description of the Company activity;
- c) Intercompany transactions overview;
- d) Functions.

##### Economic analysis

- a) Selecting the method to be applied;
- b) Application of the Transfer Pricing Method;
- c) Benchmark description;
- d) Results;
- e) Adjustments;
- f) Determination of the "arm's length" remuneration.

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<sup>3</sup> [Document - Luxembourg - Transfer Pricing - 13. Documentation Requirements - Tax Research Platform - IBFD](#), para. 13.6.1.

## b) Industry Analysis

By identifying value drivers for the relevant industry, a first indication of the level of profitability common in the industry is being given.

## c) Company Analysis

A description of the management structure of the local entity, a local organisation chart, and a description of the individuals to whom local management reports and the country(ies) in which such individuals maintain their principal offices.

A detailed description of the business and business strategy pursued by the local entity including an indication whether the local entity has been involved in or affected by business restructurings or intangibles transfers in the present or immediately past year and an explanation of those aspects of such transactions affecting the local entity.

## d) Functional Analysis

In conducting a functional analysis, an assessment is made of the significant activities and responsibilities that are performed by the related parties relevant to the Intercompany Transactions under review, the tangible and intangible assets that are employed and the risks that are borne in undertaking the business activities. Such an assessment is consistent with the recommendations that have been made in the OECD Guidelines at paragraph 1.51.

## e) Choice of Transfer Pricing Method

The Luxembourg legislation follows the recommendation of the OECD TP Guidelines. The following methods are accepted:

- Comparable Uncontrolled Price Method
- Resale Price Method
- Cost Plus Method
- Transactional Net Margin Method
- Profit Split Method

If none of them is applicable, the taxpayer has the opportunity to define and use another approach if adequately justified.

### f) Economic Analysis – Benchmark Study

Local comparable are preferred. However, if the reliability of these comparable is not sufficient, other comparable data with similar economic conditions from different geographical regions are acceptable as well.

### g) Inter-company (IC) Legal Agreement

Although an Inter-company legal agreement formalizes the business and financial relationship between group entities, the legal agreements have a lower ranking since the OECD 2017 Guidelines made the “conduct of parties” the prevailing concept.

### h) Financial Statements

Each (ultimate parent) entity of an MNE group tax resident in Luxembourg that is required to prepare consolidated financial statements and has a consolidated annual group turnover exceeding EUR 750 million during the fiscal year immediately preceding that for which the report is being made falls within the scope of the CbC reporting. In cases where the MNE group is not required to prepare consolidated financial statements, to determine whether the threshold is met, taxpayers should analyse whether they would have consolidated if its equity interest would be publicly traded.<sup>4</sup>

### i) Production Process for TP Relevant Returns, Documents, Forms and Financials

In the chart below, the existence of the filing requirements with the details of which format is used, the latest filing date, notification requirement and its deadline, thresholds to be applied in case it exists, and the required languages are demonstrated. This information can be seen respectively for CIT, master file, local file, CbCR, local forms, annual accounts and segmented P&L documentations.

	Prepare or File?	Format	Deadline	Notification Deadline*	Threshold* (Yes/No)	Local Language (Yes/No)*(If “No”, it can be filed in English)
<b>Corporate Income Tax</b>	File	Electronic	By 31 <sup>st</sup> of May of each year following	No	N.A.	No

<sup>4</sup> [Document - Luxembourg - Transfer Pricing - 13. Documentation Requirements - Tax Research Platform - IBFD](#) para. 13.2.2.

			the calendar year during which the income was earned.			
<b>Master File</b>	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.
<b>Local File</b>	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.
<b>CbCR</b>	<a href="#">File</a>	Electronic Form	Reporting fiscal years beginning on or after 1 January 2016	The notification (at year-end) and the CbC report (1 year after notification) can both be filed in electronic format	Yes	No
<b>Local form</b>	File	Form 500	By 31 <sup>st</sup> of May	No	No	No
<b>Annual Accounts</b>	Prepare	Local GAAP	No later than 7 months after the end of the financial year	No	Yes	No

<b>Segmented P&amp;L</b>	Prepare	Excel/Other	Ready upon filing CIT/TP documentation	No	No	No
* Luxembourg has signed the MCAA agreement for the filing of CBCR						
* Luxembourg does not request as much and detailed information from smaller and less complex enterprises (SME's included) than it does from large and complex enterprises.						

### j) Mandatory Language

The Luxembourg tax authorities accept any transfer pricing documentation drafted in Luxembourg's official languages: Luxembourgish, French and German. Nevertheless, English language is also accepted.

### k) Notification Requirement

A Luxembourg group entity must notify the tax authorities before the end of the financial year whether it will file the CbC report as the ultimate parent entity or as a surrogate parent entity. If it is not a Luxembourg entity, the identity of the UPE or surrogate parent entity must be disclosed to the tax authorities (including the identification of its tax residency).

The notification must be submitted to the tax authorities electronically. For tax years ending on December 31, 2015, the first notification was required on December 31, 2016. The notification should be filed on the final day of the reporting fiscal year for any fiscal years ending after December 31, 2015. If the fiscal year ended on April 30, 2016, for example, the notification must be filed by April 30, 2016.

In the case of incomplete or inaccurate notification, or failure to file the notification, a penalty may be imposed of up to EUR 250,000.<sup>5</sup>

### l) Record Keeping

Luxembourg income tax legislation does not include any specific rules relative to keeping transfer pricing records or documentation, so the general income tax rules relative to keeping records and documentation apply. Accordingly, all documentation useful to determine the taxable profit should be kept for a period of ten years.

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<sup>5</sup> [Document - Luxembourg - Transfer Pricing - 13. Documentation Requirements - Tax Research Platform - IBFD](#), para. 13.2.4.

### m) Penalties and Interest Charges

Penalties applied on transfer pricing assessments can reach up to four times the amount of the tax evaded, in case of tax evasion or ten times the tax evaded, in the case of fraud.

In the absence of sufficient documentation, the burden of proof shifts from the tax authorities to the taxpayer.