

Outsourcing: Luxembourg Overview

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A Q&A guide to outsourcing in Luxembourg.

This Q&A guide gives a high-level overview of legal and regulatory requirements on different types of outsourcing; commonly used legal structures; procurement processes; formalities required for transferring or leasing assets; data protection issues; supply chain compliance; specification, service levels and escalation; flexibility in volumes purchased; charging methods; customer remedies and protections; warranties and indemnities; term and notice period; termination and its consequences; liability, exclusions and caps; dispute resolution; and the tax issues arising on an outsourcing.

Regulation and Industry Requirements

National Regulations

1. To what extent does national law specifically regulate outsourcing transactions?

There are no specific laws regulating either single jurisdiction or cross-border outsourcing transactions in Luxembourg. As with any contract, outsourcing contracts are subject to the rules of the Civil Code. Outsourcing contracts fall under the general regime of service contracts (*louage d'ouvrage*), as defined by Article 1710 of the Civil Code. The fundamental principle in contract law is that of freedom of contract (Article 1134, Civil Code). The parties to the outsourcing contract are therefore free to agree on anything that is not contrary to mandatory laws, public policy or morality.

However, the Law of 23 July 1991 on the regulation of sub-contracting activities (Law of 23 July 1991) applies to public procurements and outsourcing agreements exceeding EUR55,000 in value, and imposes specific rules on them. Law of 23 July 1991 defines an outsourcing as:

"The operation whereby a contractor entrusts, by means of a sub-contract, and under its responsibility, to another person called the sub-contractor, all or a part of the execution of a service agreement or a procurement contract concluded with the client."

Sectoral Regulations

2. What additional regulations may be relevant for the following types of outsourcing?

Sector-specific Regulations

IT and cloud services. From 30 June 2022, new rules apply under CSSF Circular 22/806 of 22 April 2022 on outsourcing arrangements (CSSF Circular 22/806).

CSSF Circular 22/806 is applicable to entities subject to the supervision of the Commission de Surveillance du Secteur Financier (CSSF), the Luxembourg financial supervisory authority. These entities include:

- Credit institutions.
- Financial sector professionals (PSFs).
- Payment institutions and electronic payment institutions.
- Investment fund managers (IFMs).
- Undertakings for the Collective Investment in Transferable Securities (UCITS) funds.

CSSF Circular 22/806 sets out specific requirements regarding the outsourcing of IT and cloud services to:

- Licensed credit institutions and PSFs based in Luxembourg.
- Information and communication technology service provider contractors located outside of Luxembourg.
- An entity that is part of the outsourcing entity's company group.
- CSSF Circular 22/806 sets out additional requirements if the outsourcing arrangement relies on cloud computing infrastructure.
- See below, *Financial Services*.

Telecoms. Outsourcing of telecommunications is not specifically regulated under Luxembourg law.

Public sector. The Law of 23 July 1991 applies to public procurements and outsourcing agreements exceeding EUR55,000 in value. It imposes specific rules on these public procurements, which must abide by the public tender offer system.

Financial services. CSSF Circular 22/806 sets out requirements for CSSF-supervised entities in the context of outsourcing arrangements, including financial services. In particular, outsourcing arrangements must not impair the CSSF's supervision of PSFs.

Further specific requirements applicable to the delegation of activities by IFMs are included in the:

- Law of 17 December 2010 relating to undertakings for collective investment.
- Law of 12 July 2013 on alternative investment funds managers.
- CSSF Circular 18/698 on the authorisation and organisation of IFMs incorporated under Luxembourg law.

The delegation of an activity by an IFM does not affect its liability towards the funds managed.

Insurance. The Insurance Industry Act of 7 December 2015 transposed into Luxembourg law the provisions of Directive 2009/138/EC on the taking-up and pursuit of the business of insurance and reinsurance (Solvency II Directive) in regard to outsourcings. Under Article 32(1) 21 of the Insurance Industry Act, an outsourcing is:

"an agreement, in whatever form, between a natural or legal person in the insurance sector and a service provider, whether supervised or not, under which that service provider carries out, either directly or through a third party, a procedure, service or activity which would otherwise be carried out by the person himself".

Commission Delegated Regulation (EU) 2015/35 supplementing the Solvency II Directive sets out more detailed requirements on:

- How to choose a service provider.
- The written agreement to be entered into.
- The ongoing supervision that the insurance undertaking must exercise over a service provider.

On 24 April 2020, the European Insurance and Occupational Pensions Authority (EIOPA) issued a total of 16 guidelines on outsourcing to cloud service providers.

On 24 June 2020, the Commissariat Aux Assurances (CAA) issued a Circular Letter 20/13 on Outsourcing to cloud service providers, thereby adopting the EIOPA-BoS-20-002 Guidelines on this issued by EIOPA. Circular Letter 20/13 was supplemented by Circular Letter 21/15 of 5 August 2021, which is intended to incorporate all of the above guidance and some additional requirements of the CAA.

Other Legal or Regulatory Requirements

Subject to certain conditions, the Labour Code provides for joint and several liability (*donneur d'ordre*) for the principal for any remuneration, allowances and charges due to a sub-contractor's employees (Article L. 281-1, Labour Code). In the case of a posting of employees, the principal has an obligation of control since it must require any (direct or indirect) sub-contractor to provide a copy of the posting declaration. If a foreign sub-contractor does not prove that it has made the posting declaration, the principal must communicate certain information relating to the posting, as well as a copy of the service provision contract to the Labour and Mines Inspectorate, within eight days (Article L. 142-2, Labour Code).

3. What industry sectors require (formally or informally) regulatory notification or approval for outsourcing transactions?

Financial Services

Critical or important outsourcing arrangements by entities covered by the CSSF Circular 22/806 must be notified to the CSSF before becoming effective. Guidelines on how to assess whether the outsourcing is critical or important are provided in the Circular. The notification must be made at least three months before the planned outsourcing comes into effect, which may be reduced in certain cases. Notifications not made within the applicable timeframe are considered to be not notified.

IFMs subject to the CSSF Circular 18/698 must also give prior notification to the CSSF before proceeding with an outsourcing.

Insurance

The written notification requirements referred to in Article 81(3) of the amended Law of 7 December 2015 on the insurance sector and specified by EIOPA's guidance on the governance system are applicable to any outsourcing of significant or critical operational activities or functions to cloud service providers. If an outsourced activity or operational function that was previously classified as non-material or non-critical becomes material or critical, the company must inform the CAA.

Structuring the Transaction

4. What transaction models are commonly used in an outsourcing in your jurisdiction? What are their respective advantages and disadvantages?

Direct Outsourcing

Direct outsourcing is commonly used in Luxembourg. In this type of structure, the contract is signed directly between the customer and the supplier. The supplier has its own organisation, infrastructure and employees.

The advantages of this structure are:

- Flexibility.
- Cost and time reduction.
- Facilitation of a focus on core business.

The disadvantages are:

- Risk as to the quality of the service provided.
- Risk of fraud or disclosure of personal data, and privacy issues.
- Risk of loss of autonomy.

Multi-sourcing

Multi-sourcing is commonly used in Luxembourg. The customer outsources a number of separate activities to different suppliers.

The advantages are:

- Flexibility.
- Maximising the company's competitive advantage.

The disadvantages are:

- Risk of loss of control and in-house know-how.
- Risk of deterioration in the quality of service.
- Risk in relation to management.
- Risk of loss of coherence and cohesion.

Indirect Outsourcing

Not applicable.

Joint Venture or Partnership

The customer creates a new entity through a joint venture signed with a supplier for the outsourced activity.

The advantages are:

- Facilitated penetration of local markets.
- Spreading of financial risks and costs between partners.

The disadvantages are:

- Reduced profits, since they are shared.
- Risk of disagreement over the distribution of dividends.

Captive Entity

Not applicable.

Build Operate Transfer (BOT)

The supplier builds or optimises a service and starts operating it before transferring it to the customer.

The advantages are:

- Flexibility.
- Risk reduction and cost control.

The main disadvantages are:

- Complexity.
- Operating and financial risks.
- The requirement for strong corporate governance.

Procuring the Supplier/Service Provider

5. What procurement processes are used to select a service provider or supplier of outsourced services?

Market Testing

A customer may evaluate the competitive provision of goods and services through market testing, to lower costs through competitive tender processes, or to raise internal efficiency through benchmarking against potential external providers. Different procedures can be used (see below) and the duration and number of advisors will depend on the type of procedure chosen.

Request for Information (RFI)

A customer may use an RFI to request information about a service from suppliers. This way, the customer can:

- Get an idea of the possibilities offered by each service provider.
- Compare different service providers.
- Gather information on a market in a structured way.

RFIs are especially useful for companies that choose to or must research many potential partners. This procedure can be quick and does not necessarily require the involvement of advisers.

Invitation to Tender (ITT)

In an ITT (also called a "call for tenders"), service providers are invited to submit their offers to conclude a service agreement. This procedure is common, although it is not mandatory for the conclusion of an outsourcing contract. ITTs are often used by public sector organisations, which are legally obliged to offer contracts for service requirements through this process. In an open ITT, any service provider can tender an offer. In a closed ITT, service providers may be pre-selected, screened or qualified by an expression of interest to generate a shortlist of eligible candidates. This procedure may take longer, depending on the envisaged outsourcing, and may require the involvement of advisers.

Request for Quotation (RFQ)

An RFQ (also known as an "invitation for bid") is a process in which a customer solicits select suppliers to submit price quotes and to bid for the chance to fulfil certain tasks or projects. The RFQ process is commonly used by customers that need a consistent supply of a specific number of standard products. Companies may send RFQs alone or before a request for proposal (see below).

Request for Proposal (RFP)

An RFP is a business document that announces a project, describes it, and solicits bids from qualified service providers to complete it. Larger companies often use the RFP process for big-ticket projects. This procedure can be relatively quick, depending on the envisaged outsourcing and the number of service providers or suppliers involved.

Shortlisting

This method can also be used but has no consequences under Luxembourg law (except for in relation to public procurement).

Due Diligence

Due diligence is the process of investigating the reliability of a service provider, and will include assessing the risks associated with outsourcing the functions of the customer's business.

In an outsourcing, due diligence is often a two-way process, unlike other arrangements where only the buyer administers the process. While the customer assesses the expertise and qualifications of the service provider, the service provider will also verify the outsourcing project and the legitimacy of the customer's company. This process can be relatively lengthy and usually requires the involvement of advisers.

Negotiation and Further Due Diligence

The aim of the negotiations is to conclude a final comprehensive agreement. A more formal or less formal negotiation process may be used, depending on the case. The length of the negotiations is dependent on the scope and complexity of the outsourcing project, and can vary from several weeks to several months for complex cross-border transactions. This is usually followed by a verification phase, which may lead to final adjustments before the parties sign and execute the final contract.

Transferring or Leasing Assets

Formalities for Transfer

6. What formalities are required to transfer assets on an outsourcing transaction?

Immovable Property

All real estate transfers must be established by a notary. A taxpayer who sells or exchanges real estate must declare it to the Luxembourg Inland Revenue (*Administration des contributions directes*) (ACD). There are no controls on foreign ownership of real estate in Luxembourg.

IP Rights and Licences

For evidentiary reasons, the law requires that the assignment and transmission of economic rights be in writing. The formalities depend on the type of rights assigned. For a trade mark transfer, registration with the Benelux Office for Intellectual Property or the World Intellectual Property Organisation (WIPO) (for international transfers) may be required.

Movable Property

There is no specific legislation regulating the transfer of movable property.

When a vehicle registered in Luxembourg is transferred, sold, sold for export or temporarily or permanently put out of use, the transferor must inform the Société Nationale de Circulation Automobile (SNCA) within five working days.

Key Contracts

Any transfer of a contract requires the approval of the other contracting party. Consent may be included in the contract before the outsourcing or obtained through specific negotiation.

Data and Information

The transfer of data must comply with the General Data Protection Regulation ((EU) 2016/679) (GDPR) and the relevant national regulations in Luxembourg (see [Question 9](#)).

Formalities for Leasing or Licensing

7. What formalities are required to lease or license assets on an outsourcing?

Immovable Property

Specific legislation governs the leasing of real estate. Parties may contractually derogate from these provisions. Leases of real estate must be registered with the competent land office.

IP Rights and Licences

The transfer of IP rights and licences usually requires a written agreement between the parties. In some cases (such as a transfer of rights in software), additional formalities may apply. Before any assignment of IP rights, the assigning company must ensure that it is authorised to do so. In the case of the transfer of registered IP rights, registration of the transfer in the relevant registers may be required (for example, with the Benelux Office for Intellectual Property or WIPO (for international leases)).

Movable Property

No specific formalities are required to lease or license movable property. For evidential reasons, it is recommended that the parties conclude a contract in writing.

Key Contracts

A contract cannot be leased or licensed. Instead, depending on the choice of the contracting parties, a contract can be sub-contracted or transferred.

Transferring Employees on an Outsourcing

8. Are employees transferred by operation of law?

For information on transferring employees in an outsourcing transaction in Luxembourg, including structuring employee arrangements (including any notice, information and consultation obligations) and calculating redundancy pay, see [Country Q&A: Transferring Employees on an Outsourcing in Luxembourg: Overview](#).

Data Protection and Secrecy

9. What legal or regulatory requirements and issues may arise on an outsourcing concerning data protection?

For all EU member states, the GDPR applies to the processing of personal data wholly or partly by automated means, or other than by automated means, if the data forms part, or is intended to form part, of a filing system (Article 2(1)). The GDPR defines personal data as "any information relating to a data subject" (Article 4(1)). For more details on the GDPR, see [Practice Note, Overview of EU General Data Protection Regulation](#).

Data Protection and Data Security

Use of processors and sub-processors. Under Article 28 of the GDPR, if any data processing activities are carried out on the instruction of a controller, the data processor must implement appropriate organisational and technical measures to meet the guidelines set out by the GDPR.

A processor may choose to sub-contract all or part of the data processing to a third party called a "sub-processor". In this case, the processor must obtain prior written authorisation when the data controller intends to transfer the processing of personal data to a sub-processor. Once the processor has obtained the formal authorisation of the data controller, the processor remains fully responsible to the data controller for the performance of the sub-processor. The processor must put in place a contract with the sub-processor. The terms of the contract that relate to Article 28(3) must offer an equivalent level of protection for the personal data as those that exist in the contract between the controller and the processor.

Liability for breaches of personal data processing requirements (for both customer and service provider). As it will be a controller that determines the purposes and means of the processing of personal data, a customer involved in a processing of personal data is liable for any damage caused by any processing of personal data that violates the GDPR (Article 82(2), GDPR).

As it will be a processor (the service provider) that processes personal data on behalf of the data controller (the customer), the service provider would be liable for damage caused by the processing if it fails to comply with obligations of processors under the GDPR or it has acted outside or contrary to the lawful instructions of the data controller (Article 82(2), GDPR).

If any data breaches are found, a data protection officer will impose a fine according to the degree of responsibility of the processor and the controller, taking into account all of the technical and organisational measures implemented by the controllers and processors (Article 83, GDPR).

Transfer of personal data to third countries. A transfer of personal data to a third country or an international organisation can only take place if the European Commission has decided that the third country, a territory or one or more specified sectors within that third country, or the international organisation in question, ensures an adequate level of protection (Article 45, GDPR). In the absence of a decision of adequacy, a controller or processor can only transfer personal data to a third country or an international organisation if the controller or processor has provided appropriate safeguards (for example standard contractual clauses or binding corporate rules) and on condition that enforceable data subject rights and effective legal remedies for data subjects are available (Articles 46 and 47, GDPR). However, there is derogation where data subjects have given their explicit consent to such processing (Article 49, GDPR).

Security requirements. Both the data controller and any processors must implement appropriate technical and organisational measures to ensure a level of security appropriate to the risks. These security measures must take into account the:

- State of the art.
- Costs of implementation.
- Nature, scope, context and purposes of processing.
- Likelihood and severity of risks to the rights and freedoms of natural persons.

(Article 32, GDPR.)

Mechanisms to ensure compliance. When a contract between a processor and a sub-processor is drawn up, it must contain the same data protection obligations originally set out in the contract between the data processor and the data controller. This is commonly referred to as a "back-to-back contract".

Under Article 28(3) of the GDPR, the contract between the processor and its sub-processor must contain the following information:

- The subject-matter of the personal data and the duration for which it will be processed.
- The exact purpose and nature of the data processing.
- The data processor's obligation to keep the data secure and alert the data controller if there are any data breaches.

Sanctions for non-compliance. The National Commission for Data Protection (CNPD) can impose penalties for non-compliance. The penalties for the most serious infringements can be fines of up to EUR20 million or 4% of the entity's total annual worldwide turnover for the previous financial year.

Banking Secrecy

General requirements. Banks have a professional duty of secrecy (Article 41, Law of 5 April 1993 on the financial sector). To protect banking secrecy, banks must implement appropriate measures to ensure a level of security appropriate to the data. Banks must obtain clients' prior consent to disclose any of the clients' personal data.

Security requirements. There are no specific security requirements to ensure the preservation of banking secrecy.

Mechanisms to ensure compliance. There are no specific mechanisms to ensure compliance concerning banking secrecy.

International standards. There are no international standards regarding banking secrecy.

Sanctions for non-compliance. In case of violation of any professional secrecy, the offender is liable to imprisonment for a maximum of six months and a fine of EUR5,000 (Article 458, Penal Code).

Confidentiality of Customer Data

General requirements. Customer data is personal data and must therefore be processed in accordance with the rules of the GDPR.

Security requirements. The processor must:

- Ensure that it has appropriate measures to protect personal data.
- Prevent unauthorised access to personal data and the equipment used to for the processing.
- Ensure that all persons authorised to process the personal data have committed themselves to confidentiality or have the appropriate statutory obligations of confidentiality.
- Ensure that non-personal customer data is also adequately secure.

Mechanisms to ensure compliance. See above, *Data Protection and Data Security: Transfer of personal data to third countries and Security requirements*.

Sanctions for non-compliance. The CNPD can impose penalties for non-compliance. The penalties for the most serious infringements can be fines of up to EUR20 million or 4% of the entity's total annual worldwide turnover for the previous financial year.

International Standards

The ISO 27001 standard is the most commonly used international standards in terms of data security. Compliance with these standards is recommended.

Supply Chain Compliance

10. What (if any) compliance provisions should an outsourcing customer include in the contract?

A customer may include compliance-related provisions in the outsourcing agreement to ensure compliance throughout the entire supply chain. To ensure compliance of suppliers (and their sub-contractors) with any requirement the customer may be subject to (such as anti-money laundering and anti-bribery obligations, Foreign Account Tax Compliance Act obligations, data protection compliance, and so on), customers usually include in the outsourcing contract an obligation to comply with any applicable law and with their own code of conduct, if any (which may be attached as an appendix to the contract). The customers may also seek a warranty that the suppliers will ensure that their own sub-contractors (if any) comply with these obligations. It is possible to insert a penalty clause in the contract providing that in the event of non-compliance by the supplier (or sub-contractor), the supplier will pay a substantial sum, which serves as a deterrent.

Services: Specification, Service Levels and Escalation

11. How is the service specification typically drawn up and by whom?

The service specification, which describes the outsourced services that are to be provided, is usually drafted by the party initiating the outsourcing (either the customer or the supplier). The clauses to be included in the contract should reflect the needs of the outsourcing party. The contract should also indicate the means put in place to ensure continuity of service, and data protection measures.

12. How are the service levels and the service credits scheme typically dealt with in the contract?

The parties usually enter into detailed service level agreements (SLAs) that allow the supplier's performance to be measured. SLAs should contain:

- Clearly defined service levels.
- Expected results.
- How these results are communicated to the customer.
- Consequences if the service level is not achieved.

In the absence of an SLA, it is usual to include service levels in an annex to the outsourcing contract. Service levels are often designed and defined by the customer's business teams.

If the agreed service level is not achieved, the parties may provide for a system of service credits resulting in price reduction mechanisms on the next month's invoice. Service credits should be clearly defined so that they are not considered to be illegal private penalties. Operational level agreements between different suppliers are often used in a multi-sourcing context.

13. Are there any service escalation mechanisms that are usually included in the contract? How often are these exercised and how effective are they in restoring the services to the required levels?

There are no standard contractual clauses on escalation mechanisms. Parties are free to negotiate and include such mechanisms in the contract. For example, they may provide for:

- A right to monitor when the supplier repeatedly fails.
- Step-in rights when the supplier's performance continues to be poor.

The customer could take over the service provision using its own staff or a third party. Although the inclusion of this type of clause is relatively common, in practice, customers often do not exercise their step-in rights because they do not have the capacity to intervene. If these mechanisms do not work, the customers usually decide to terminate the contract.

Transaction Management

Organisational Structures and Change Management

14. What types of organisational structures are commonly used to govern outsourcing transactions?

Depending on the complexity of the outsourcing, the organisation of the customer company and the type of services, the parties may decide to contractually designate an audit committee to measure the actual services rendered during the execution of the outsourcing contract. The reasons for and scope of the intervention of this committee must be provided for in the contract.

Similarly, it is usual to insert:

- Remedy clauses to cover default by one of the parties (see [Question 25](#)).
- Dispute resolution clauses to mitigate any deadlock between the parties (see [Question 31](#)).

15. What change management models are commonly used to govern outsourcing transactions?

Depending on the type of service provided, outsourcing contracts may provide for different procedures to change work orders. Usually, the parties can annex to their contract a work order that the customer can send back to the service provider, completed and signed, setting out precisely the new services requested and the conditions under which they are to be provided.

Flexibility in Volumes Purchased

16. What mechanisms are commonly used to manage adjustments in the volume of services?

There is no specific legislation governing the issue of customers adjusting service volumes. The parties may allow for changing volumes in their outsourcing contract. The level of flexibility to adjust service volumes by the customer generally depends on the type of services provided and the billing method. If service volumes are fixed for a certain period of time (such as monthly), the customer can, in principle, vary the volume at the end of the fixed period, although it is usual to provide for a minimum volume of services and a clause whereby the parties agree to review the contract according to the needs of the customer at the end of a certain period. The parties may also agree on thresholds whereby a reduction in the volume of services constitutes a termination event or triggers an obligation on the part of the customer to pay additional charges or termination fees.

Charging Methods and Key Terms

17. What charging methods are commonly used on an outsourcing?

The parties are free to negotiate the charging methods. Most often, a fixed price is agreed, which is based on the contractually described services. A variable price may also be considered by the parties, based on defined deliverables, with pricing based on the unit or service when the volume is not predictable. For ongoing services, a pay-per-use fee may be agreed.

18. What other key terms are used in relation to costs, including auditing and benchmarking mechanisms?

In outsourcing contracts, the parties are free to negotiate any clauses they wish and to include clauses on, for example:

- Indexation.
- Rate variation mechanisms.
- Benchmarking provisions.
- Payment terms and interest on late payments.
- Dispute resolution.
- Service credits.
- Auditing mechanisms.

Customer Remedies and Protections

19. If the service provider fails to perform its obligations, what remedies and relief are available to the customer under general law?

There are no specific statutory remedies or reliefs available to the customer if the supplier fails to perform its obligations. Under the general provisions of contract law, the customer can:

- Claim damages that are directly or indirectly caused by a breach of contract by the supplier.
- Withhold payments for services that are not delivered.
- Ask for a price reduction.
- Terminate the agreement because of the supplier's breach.

20. What customer protections are typically included in the contract to supplement relief available under general law?

Customer protection clauses usually included in the contract include the following:

- A right to audit the supplier's performance.
- The possibility for the customer to sub-contract the service to another supplier.
- An insurance plan.
- A parent company guarantee.
- A clause allowing termination for cause.
- Financial penalties for the supplier (such as service level penalties).

Warranties and Indemnities

21. What express warranties and/or indemnities are typically included in the contract documentation?

Contracts usually include clauses providing that:

- The parties have the authority to enter into the agreement and acknowledge that the information given is complete and accurate.
- The parties will comply with all applicable laws, including data protection, anti-bribery and anti-money laundering legislation.
- The parties are licensing IP rights and indemnify the other party against third-party claims of IP infringement.
- The supplier will provide the services with reasonable skill and care and in accordance with industry best practice.
- The parent company of the supplier guarantees the compliance of its subsidiary with its contractual obligations.

The customer will generally claim unlimited indemnities in respect of:

- Confidentiality.
- Data protection matters.
- Compliance with anti-bribery and anti-money laundering legislation.

22. What requirements are imposed by national or local law on fitness for purpose and quality of service, or similar implied warranties?

Luxembourg law does not impose warranties in relation to fitness for purpose and quality of service. However, these warranties may be negotiated between the parties and included in the contract. Where the outsourcing also involves the supply of certain products (for example, hardware), the Civil Code rules governing sale-purchase contracts implies warranties of absence of latent defects and fitness for purpose.

23. What types of insurance are available in your jurisdiction concerning outsourcing? Are there any types of insurance required by law?

Insurance policies can cover many types of risks, such as:

- Business liability.
- Professional liability (professional errors and omissions).
- Third-party liability.
- Data protection liability.
- Property damage.
- Cyber-risk liability.
- Employee liability.

Termination and Termination Consequences

Events Justifying Termination

24. What events justify termination of an outsourcing without giving rise to a claim in damages against the terminating party?

Material Breach

For termination to be valid, the material breach must be serious and justify the impossibility of the terminating party remaining bound by the contract. The parties are free to define in the contract what constitutes a material breach (such as a failure to provide the required quality of service for a defined period of time, or a failure of the customer to pay). Termination for material breach may also be declared by a court on request of the other contracting party.

Force Majeure Events

Article 1148 of the Luxembourg Civil Code provides that:

"There shall be no damages and interest when, as a result of *force majeure* or a fortuitous event, the debtor has been prevented from giving or doing what he was obliged to do, or has done what he was forbidden to do."

An event of *force majeure* must be:

- External (not related to any of the contracting parties).
- Irresistible (in the sense that the impact of the event could not be mitigated by appropriate measures).
- Unforeseeable (that is, the event could not be foreseen at the time of the conclusion of the agreement and there was no reason to believe that it would occur).

However, as is the case for a material breach, the parties are free to define in the contract what constitutes a *force majeure* event (such as a war, pandemic and so on). When such an event occurs, the execution of the contract is suspended, unless the resulting delay justifies the termination of the contract. If the impediment is definitive, the contract is automatically terminated, and the parties are released from their obligations.

Insolvency Events

It is common practice in Luxembourg for the parties to agree that the contract can be unilaterally terminated if one of the parties becomes bankrupt or is subject to insolvency proceedings.

Termination for Convenience

Under general contract law, any contract for an indefinite period must be terminable without cause by either party at any time, provided that a period of notice is given. However, it is in principle not possible to terminate a fixed-term contract before the end of its term without having to pay damages. It is common practice in Luxembourg to provide in outsourcing contracts that if one of the parties terminates the contract for convenience, it must:

- Do so in writing (by registered letter with acknowledgement of receipt or by email).
- Respect a certain contractually agreed period of notice.
- Pay a termination fee, where applicable, the calculation of which is provided for in the contract.

This compensation usually covers the costs that the supplier incurred to fulfil its obligations under the contract, as well as possibly the loss of certain profits. In principle, the termination fee decreases with the remaining duration of the contract.

25. What remedies are available to the contracting parties?

The parties are entirely free to agree on remedies. The range of remedies can be very wide, and may include, for example:

- Contractual damages.
- Early or partial termination.
- A right to demand remedial action from the supplier.
- A right to withhold payment, where justified by the defaulting party's contractual non-performance.
- A right of the customer to require the supplier to provide the relevant services again to the appropriate service standard.
- A right of intervention, allowing the customer to take over the services itself or through a third-party step-in.

Exit Arrangements

26. What mechanisms are commonly used to address exit and post-termination transition issues?

To address any exit and transition problems that may arise after the termination of the activity, specific clauses or a reversibility plan (either reintegration of the service into the company or a transfer to a third-party service provider) should be included in the outsourcing contract negotiations. This plan should set out:

- Precise terms describing the procedures for transferring skills, equipment and documentation.
- Matters relating to equipment ownership, IP, contracts (licence, maintenance, insurance), personal data transfers, and employee transfers.
- A timetable for the execution of the reversibility procedures.

It may also be useful to include a clause stating that the parties must respect the obligations of good faith and collaboration. This is a delicate phase where the service provider could be tempted to simply stop its services once the contract has been terminated by the customer.

27. To what extent can the customer (or if applicable, its new service provider) gain access to the service provider's know-how post-termination and what use can it make of it?

In principle, the customer (or its new service provider) has no right to access the service provider's know-how after termination, unless otherwise stipulated in the outsourcing contract. If the customer wishes to continue to use the service provider's know-how, the parties must negotiate a separate licence agreement.

Liability, Exclusions and Caps

28. What liability can be excluded?

Luxembourg law and court practice have accepted, in principle, the validity of clauses that aim to reduce or eliminate the liability of the service provider in the event of non-performance or poor performance of its obligations. Therefore, except in the case of fraudulent non-performance, compensation in contractual matters covers only the damage normally foreseeable at the time of conclusion of the contract (Article 1150, Civil Code).

There are certain limits to this principle:

- A clause limiting or excluding contractual liability is ineffective in the case of fraud or gross negligence by the service provider.
- The Court of Cassation has rejected such clauses when they empty the contract of its substance (*Lux. 21 March 2003, no. 77/2003 III*) or when they exclude a mandatory legal obligation. A clause can restrict or diminish the substance of the obligation, provided that it retains a sufficient, efficient cause, in which case the clause is valid (Article 1135, Civil Code). The application of this rule will involve a concrete analysis of the balance of the contract and the will of the parties.
- The use of such arrangements is prohibited or restricted in certain areas, such as consumer law.

29. Are the parties free to agree a cap on liability and, if desirable, a cap on indemnities? If so, how is this usually fixed?

The parties can freely agree on a liability cap, provided the cap is reasonable (limitation and exclusion of liability clauses cannot completely erode the meaning of the agreement (see [Question 28](#))). If the liability cap in the contract is too low, the limitation of liability clause may be considered by a judge as null and void.

It is common in outsourcing contracts to provide for a total and aggregate liability cap that is a function of the total value of the contract and/or an annual liability cap that is a function of the annual value of the contract, with exceptions, such as for intentional breach, fraud, or material breach. It is also common to provide for specific higher or capped liability limits for certain issues (such as in relation to IP).

30. What other provisions may be included in the contract to protect the customer or service provider regarding any liabilities and obligations arising in connection with outsourcing?

As an outsourcing project is likely to have a direct impact on the employees assigned to the service to be outsourced, it is recommended to insert clauses relating to the status of the employees (providing in particular that they are to be taken over by the service provider) and setting out the respective obligations of the customer and the service provider towards these employees.

Dispute Resolution

31. What are the main methods of dispute resolution used?

Although not legally required, it is strongly recommended that a dispute resolution procedure be included in the outsourcing contract. This way, the parties agree the method for dispute resolution at the time of signing the contract and not when a dispute actually arises, when negotiations between the parties are often more delicate.

Depending on the complexity of the outsourcing contract, the nature of the dispute may be diverse and may concern, for example, the fulfilment of an obligation by one party, or the transfer or termination of the contract.

An amicable method of termination, such as negotiation or mediation, may be provided for in an outsourcing contract. The parties may also choose to use arbitration to resolve their dispute. Where arbitration is preferred, the case is often submitted to arbitration under the arbitration rules of the Chamber of Commerce of the Grand Duchy of Luxembourg. The parties may also have recourse to a third-party expert to resolve their dispute. These alternative dispute resolution mechanisms are frequently chosen because they are:

- Confidential (whereas court proceedings are in principle public).
- Faster than ordinary proceedings (the arbitrator(s) usually render(s) their award within six months).
- Contained in a single proceeding (which is an advantage in an international dispute, for example, where there is a risk multiple lengthy and costly court proceedings).
- Potentially less expensive (the costs of often complex court proceedings can be high).

However, more often than not, the parties resort to legal proceedings before the courts. Disputes relating to the exit from services and the transition from one provider to another are not very common in Luxembourg.

Tax

32. What are the main tax issues that arise on an outsourcing?

Transfers of Assets to the Service Provider

Any transfer of assets to a service provider giving rise to a gain (where the fair market value exceeds the accounting value) is subject to corporate income tax and municipal business tax in Luxembourg at the current aggregate rate of 24.94% (for a corporate customer located in Luxembourg-City in 2022).

Transfers of Employees to the Service Provider

A temporary transfer of employee to the supplier may be considered as a service subject to VAT. However, if the employee is transferred in the framework of a transfer of business as "a going concern", the transaction should be VAT-exempt (under Article 19 and Article 29 of Directive 2006/112/EC on the common system of value added tax (VAT Directive), as transposed into Luxembourg law by Article 9 (supply of goods) and Article 15 (supply of services) of the Luxembourg VAT Law).

On a transfer of employees to a Luxembourg-based service provider, the service provider will be subject to administrative obligations such as the:

- Registration of each transferred employee with the Luxembourg social security centre (*centre commun de sécurité sociale*).
- Declaration of the employees to the Luxembourg tax administration.
- Withholding of tax on the employees' salaries.

VAT or Sales Tax

VAT is levied on the supply of goods and services that are deemed to take place in Luxembourg, at the standard rate of 17%. Under the Luxembourg VAT Law, the transfer of business as a going concern is not subject to VAT provided certain conditions are met (Article 19, VAT Directive; Article 9, Luxembourg VAT Law).

Service Taxes

Luxembourg does not impose any service taxes.

Stamp Duty

The transfer of goods (including real estate assets) may be subject to registration duty, at a flat or *ad valorem* rate, depending on the nature of the asset transferred. As a general rule, if such a transfer is subject to VAT in Luxembourg, only a flat tax is due (currently EUR12), except for real estate assets.

A registration fee applies to a transfer of immovable property at a rate of 6%, increased by a 1% transcription tax. For real estate assets located in Luxembourg City, an additional charge amounting to 50% of the transfer tax is imposed (unless exemptions apply under certain conditions).

Corporation Tax

The taxable base is determined by reference to the annual commercial result as per the stand-alone accounts adjusted under the specific provisions of the tax code (including deductions of tax-exempt income under the Luxembourg participation exemption regime, Luxembourg double-tax treaty provisions or the reintegration of non-tax-deductible expenses).

A corporate income tax rate of 17% applies to a company whose taxable income exceeds EUR200,000. The rate is 15% if the annual taxable income is below EUR175,000.

Municipal business tax ranges between 6.75% and 10.5%, depending on where the undertaking is located. The effective corporate income tax rate of an undertaking located in Luxembourg city is 24.94%, including the unemployment fund contribution and the municipal business tax.

In addition, a Luxembourg company is subject to net wealth tax (NWT) at the annual rate of 0.5% on a taxable base up to EUR500 million (a rate of 0.05% applies on the taxable base exceeding EUR500 million). This tax is assessed on the company's worldwide net wealth as of 1 January each year (based on the assets held on 31 December of the preceding year). A minimum NWT of EUR4,815 is payable by corporate entities located in Luxembourg where the sum of fixed financial assets, transferable securities and "cash at bank" of the entity both:

- Represents more than 90% of its balance sheet total.
- Exceeds EUR350,000.

Otherwise, a Luxembourg company is liable to an NWT ranging between EUR535 and EUR32,100, depending on its total balance sheet.

Other Tax Issues

All cross-border and domestic transactions taking place between related entities must comply with the arm's length principle.

Under domestic law, the arm's length principle is set out under Article 56 of the Luxembourg Income Tax Law, which allows for profit adjustments if transfer prices differ from the prices that would have been agreed on between independent enterprises for comparable transactions taking place in an open market under comparable circumstances.

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Publications

- *Les nouveaux enjeux en droit du travail luxembourgeois.*
- *Comparative Guide Labour and Employment.*
- *L'impact du Brexit en pratique sur le détachement de personnel du Royaume-Uni vers le Luxembourg.*
- *Chambers Employment Global Practice Guide.*
- *Privacy in Luxembourg: overview.*

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Publications

- *CSSF Circular 22/810 | Notification and De-Notification procedures for marketing and pre-marketing on eDesk.*
- *ESMA supervisory briefing on sustainability risks and disclosures in the area of investment management.*
- *Infographic | Direct and indirect tax deadlines for funds.*
- *Regulation of State and Supplementary Pension Schemes in Luxembourg: overview.*
- *National Risk Assessment of ML/TF for the Year 2020.*

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Publications

- *Report of the Committee on Economic and Monetary Affairs on the European Commission's proposed ATAD 3 Directive.*
- *Higher Administrative Court | Clarifications on the calculation of time limits applicable to administrative remedies.*
- *EU Commission: draft Directive on tax incentive to reduce debt-equity bias.*
- *Luxembourg tax administration publishes guidance on the application of administrative and criminal fines for tax fraud.*
- *Infographic | Direct and indirect tax deadlines for funds.*

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Professional associations/memberships. Employment Law Specialists Association, Luxembourg (ELSA); European Employment Lawyers Association (EELA); International Bar Association (IBA).

Publications

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