BSP Newsletter

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BSP

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SUMMARY

MARKETS IN CRYPTO ASSETS (MICA) | ESMA Q&A AND FINAL REPORT ON RTS/ITS

Updates to ESMA Q&A

On 2 February 2024, ESMA has published updated questions and answers regarding Regulation (EU) 2023/1114 of 31 May 2023 on markets in crypto-assets ("**MiCA**").

With this update, ESMA confirmed that crypto-asset service providers ("**CASPs**") established between MiCA's entry into force (June 2022) and 30 December 2024 may to continue providing crypto-asset services (under national applicable law) until 1 July 2026 (assuming the applicable Member State allows the full duration of the grandfathering period). ESMA further confirmed that entities benefiting from grandfathering do not benefit from the EU passport (unless they were to acquire a MICA license and therefore cease to be a "grandfathered" entity. Entities benefiting from grandfathering will be forbidden from conducting cross-border activities in Member States where the grandfathering clause is not (or no longer) applicable.

ESMA clarified that the prohibition under Article 80(2) of MiCA to receive "remuneration, discount or non-monetary benefit in return for routing orders received from clients" applies to the crypto-asset services of receiving and transmitting orders on behalf of clients as well as the execution of orders on behalf of clients.

ESMA explained that a credit institution can provide any crypto-asset services of a notification under Article 60 of MiCA and also elaborated on certain conditions related to this. Article 60 notifications should be provided to the competent authority in charge of authorising CASPs under Article 62 of MiCA. The notification may in addition be provided to the authority that authorised the relevant CASP under the relevant other EU financial legislation.

ESMA Final Report on MiCA technical standards

On 25 March 2024, ESMA published a Final Report (the "**Final Report**") on the following regulatory technical standards (RTS) and implementing technical standards (ITS) specifying certain requirements of MiCA -the first package:-

- Draft RTS pursuant to Article 60(13) of MiCA
- Draft ITS pursuant to Article 60(14) of MiCA
- Draft RTS pursuant to Article 62(5) of MiCA
- Draft ITS pursuant to Article 62(6) of MiCA
- Draft RTS pursuant to Article 71(5) of MiCA
- Draft RTS pursuant to Article 84(4) of MiCA

ESMA has submitted the Final Report to the European Commission who shall decide whether to adopt the RTS and ITS within three months.

EU SECURITISATION REGULATION | NEW DELEGATED REGULATION

On 15 February 2024, Commission Delegated Regulation (EU) 2024/584 of 7 November 2023 (the "**New Delegated Regulation**") amending the regulatory technical standards laid down in Delegated Regulation (EU) 2019/1851 (the "**2019 Delegated Regulation**") as regards the homogeneity of the underlying exposures in simple, transparent and standardised (STS) securitisations, has been published in the Official Journal of the EU.

The 2019 Delegated Regulation lay down uniform criteria to determine the homogeneity of underlying exposures in STS securitisations.

The New Delegated Regulation amends the 2019 Delegated Regulation on the homogeneity of the underlying exposures in asset-backed commercial paper (ABCP) and non-ABCP securitisation to extend the scope to on-balance-sheet securitisations. To ensure clarity and accessibility to the applicable rules, the New Delegated Regulation combines the regulatory technical standards on homogeneity for non-ABCP, ABCP and on-balance-sheet STS securitisations in a single regulation.

Subject to transitional arrangements for outstanding STS securitisations, the New Delegated Regulation applies to securitisation transactions that are notified to ESMA as from 6 March 2024.

MIFID II AND MIFIR | VARIOUS DEVELOPMENTS

Updates to ESMA Q&A

On 2 February 2024, ESMA updated its questions and answers on MiFIR data reporting. With this update, ESMA updated the list of national client identifiers for natural persons to be used in transaction reports pursuant to the priority specified in Annex II of the Commission Delegated Regulation (EU) 2017/590.

ESMA Public Statement - deprioritisation of supervisory actions on RTS 28 reports

On 13 February 2024, the ESMA issued a Public Statement to provide clarity to market participants regarding their reporting requirements under RTS28, pending the full application of the new rules under MiFID II. ESMA expects National Competent Authorities ("**NCAs**") not to prioritize supervisory actions towards investment firms concerning the periodic RTS28 reporting obligation until the forthcoming transposition into national legislation in all Member States of the MiFID II review. Under the revised MiFID II/ MiFIR framework, investment firms are no longer obligated to annually report detailed information on trading venues and execution quality through RTS28 reports. This statement aims to promote coordinated action by NCAs under MiFID II.

New Amending Directive and Regulation

On 8 March 2024, the following were published to improve access to market data and transparency:

1. Directive 2024/790 of 28 February 2024 ("**New Directive**") amending MiFID II
2. Regulation 2024/791 of 28 February 2024 ("**New Regulation**") amending Regulation (EU) No 600/2014 (MiFIR)

The New Regulation generally aims at enhancing data transparency, removing obstacles to the emergence of consolidated tapes, optimising the trading obligations and prohibiting receiving payment for order flow. The New Directive's target is to improve the transparency requirements on markets in financial instruments and the resilience for regulated markets. It strengthens the obligation to execute orders on the most favourable terms for clients and introduces new transparency obligations for operators of trading venues.

ESMA Public Statement - transition for the application of the MiFID II/MiFIR review

On 27 March 2024, ESMA published a Public Statement aimed at providing practical guidance on some key points to support the transition and consistent application of MiFID II and MiFIR in light of the changes introduced to them by the New Directive and New Regulation; the guidance focuses on various aspects such as equity transparency, systematic internalised regime, designated publishing entities, and reporting.

MARKET ABUSE | ESMA'S WARNING RE SOCIAL MEDIA

On 6 February 2024, ESMA published a warning for people posting investment recommendations on social media (the "**ESMA Warning**"). While aiming to raise awareness on the requirements established by Regulation (EU) 2023/2779 of 6 September 2023 (the "**Market Abuse Regulation**" or "**MAR**"), it also warns about the risks of market manipulation when posting on social media.

What is an Investment Recommendation?

ESMA starts this warning with a reminder of the definition of an investment recommendation pursuant to Article 3(1)(35) of MAR: "*information recommending or suggesting an investment strategy, explicitly or implicitly, concerning one or several financial instruments or the issuers, including any opinion as to the present or future value or price of such instruments, intended for distribution channels or for the public*" constitutes Investment Recommendation. ESMA emphasises how broad the definition is and therefore appeals to people to be careful when posting any opinion on the price or value of a financial instrument or any advice on buying or selling financial instrument, so as not to fall within the scope of this definition.

Who is this ESMA Warning directed at?

Everyone because anyone can produce investment recommendations. In doing so, such persons are subject to requirements set out by MAR and its implementing Commission Delegated Regulation (EU) 2016/958 ("**CDR 2016/958**", together with MAR, the "**MAR Framework**").

MAR Framework Requirements?

The MAR Framework identifies a general set of requirements applicable to *everyone* and some additional requirements applicable only to *professionals* and *experts* which are summarised in a non-exhaustive manner in the ESMA Warning.

The general requirements applicable to any person producing or disseminating Investment Recommendations are those set out in Article 2, 3 and 5 of CDR 2016/958 and the additional requirements applicable to "professionals" and "experts" are those set out in Article 4 and 6 of CDR 2016/958. ESMA helpfully elaborates on who falls within the scope of the terms "professionals" and "experts" in this context.

ESMA reminds people of the potential consequences of non-compliance and also provides some practical examples of social media postings which could qualify as in/direct investment recommendations and where the general / additional requirements would likely be deemed to not be met.

CREDIT SERVICERS DIRECTIVE | EBA GUIDELINES ON NATIONAL LISTS/REGISTERS OF CREDIT SERVICERS

Article 9 (1) subparagraph 1 of Directive 2021/2167 on credit servicers and credit purchasers (the "**Credit Servicers Directive**" or "**CSD**"), requires that Member States "*ensure that the competent authorities (CA) establish and maintain at least a list or, where considered more appropriate, a national register, of all credit servicers authorised to provide services within their territory, including credit servicers providing services under Article 13 of this Directive*.". Pursuant to the CSD, ESMA was mandated to develop guidelines for establishing and maintaining such lists or registers.

On 5 March 2024, the EBA issued its final "**Guidelines**" accordingly. Directed at Competent Authorities responsible for overseeing these lists or registers, the Guidelines delineate: i) the requisite content, ii) accessibility standards, and iii) update deadlines. Additionally, these lists or registers are expected to streamline borrowers' access to information regarding complaint handling procedures provided by competent authorities. For further information on the CSD (formerly referred to as the NPL Directive, we refer you to our previous newsletter on this topic.

Luxembourg has not yet transposed the CSD. A a draft law was submitted to the Luxembourg Parliament (*Chambre des Députés*) on 24 March 2023, and is going through the usual legislative process.

LISTING ACT | MULTIPLE VOTE SHARE STRUCTURES: PROVISIONAL AGREEMENT REACHED BY COUNCIL AND PARLIAMENT

On 14 February 2024, the Council and the European Parliament have reached a preliminary agreement on the directive on multiple-vote share structures in companies that seek the admission to trading of their shares on an SME growth market (the "Proposed Directive"). The Proposed Directive is part of the Listing Act package, a set of measures to make public capital markets more attractive to EU companies and to facilitate access to capital for small and medium-sized enterprises ("**SMEs**").

The Proposed Directive is specifically aimed at encouraging company owners, particularly those of SMEs, to initiate the listing of their company's shares on an SME growth market as well as other multilateral trading facilities ("**MTFs**") by utilising multiple vote share structures, thereby enabling them to maintain adequate control of their company post-listing.

Scope of Proposed Directive

The Proposed Directive lays down rules on multiple-vote share structures in companies that seek the admission to trading of their shares on MTFs (which include SME growth markets); the Proposed Directive excludes from its scope companies that have shares already admitted to trading on a regulated market or (except for Article 6(2) of the Proposed Directive) an MTF. Pursuant to the Proposed Directive Member States must ensure that a company that does not have shares admitted to trading on a regulated market or MTF has the right to adopt a multiple-vote share structure for the admission of its shares on an MTF.

Covered by the definition of "**multiple vote shares**" are those shares belonging to a distinct class that carry more votes per share than another class of shares with voting rights on matters to be decided at a general meeting.

Safeguards

The Proposed Directive requires Members States to ensure that companies that have a multiple-vote share structure (as envisaged by the Proposed Directive), have appropriate safeguards to protect the shareholders holding shares with lower voting rights. In that regard, Member States:

- shall require that a company's decision to modify a multiple-vote share structure in a way that affects the voting rights of shares is taken by the general meeting by at least a qualified majority (and such majority shall apply to each class in case of multiple classes of shares);
- limit the impact of the multiple-vote shares on the decision-making process at the general meeting by introducing at least one of the following
  - a maximum ratio of the number of votes attached to multiple-vote shares to the votes attached to shares with the least voting rights.
  - a restriction for decisions by the general meeting subject to qualified majority of the votes cast, excluding appointment and dismissal of members of the administrative, management and supervisory bodies of the company as well as operational decisions to be taken by such bodies and that are submitted to the general meeting for approval, by requiring that the majority is calculated on the basis of the total number of votes cast and on either the share capital represented at the general meeting or the number of shares represented at the general meeting, or on the basis of the total number of votes cast and on votes cast in each class of shares affected by the decision.

The Proposed Directive allows Member States to provide for further safeguards within their national legislation to ensure adequate protection of the interest of shareholders who do not hold multiple-vote shares.

Next Steps

The provisional agreement on the Proposed Directive needs to be endorsed and formally adopted by the Council and the European Parliament.

LUXEMBOURG LAW OF 7 AUGUST 2023 ON BUSINESS CONTINUATION AND MODERNISATION OF BANKRUPTCY LAW | RECENT CASE LAW DEVELOPMENTS

Following the entry into force of the Luxembourg law of 7 August 2023 on business continuation and modernisation of bankruptcy law (the "**Law**") on 1 November 2023, the Luxembourg courts have handed down several decisions clarifying the scope of application of judicial reorganisation proceedings, the new debtor-in-possession restructuring proceedings introduced by the Law.

Opening of judicial reorganisation proceedings

Judicial reorganisation proceedings are a new debtor-in-possession tool aiming to preserve continuity of businesses under control of a court. Judicial reorganisation proceedings can be initiated when the continuity of the business is threatened in the short term or in the long term. The courts have already assessed this condition on several occasions and have found the relevant applications to be admissible notwithstanding the fact that the relevant debtor might not be acting in good faith. In most cases, the debtors stress their future prospects to justify why bankruptcy proceedings should be avoided, even though the fact that a company meets the substantive criteria for bankruptcy *per se* does not prevent the opening of judicial reorganisation proceedings under the Law.

The courts have accepted an application for the opening of judicial reorganisation proceedings from a company that was non-compliant with the legal requirements for publishing its annual accounts with the Luxembourg Register of Commerce and Companies within the legally prescribed period.

Transfer by court order of all or part of debtor's business

Under the Law, the opening of judicial reorganisation proceedings can have more than one objective: to reach a mutual agreement with creditors, to agree on a restructuring plan or to transfer all or part of the company or its activities. The parliamentary discussions which led to the adoption of the Law, emphasize that transferring a company or its activities (i.e. production lines, clientele, or personnel) often serves as the most effective method to ensure its continuation.

Since the Law does not explicitly define what "activities" can be transferred, this remains open to court interpretation. Indeed, in a recent judgment the court ruled that the ownership of shares by a non-operational, purely holding company does not constitute a transferable economic activity within the meaning of the Law and rejected the relevant application for putting a holding company into judicial reorganisation proceedings by ordering the transfer of its assets. In doing so, the court made reference to other activities that would fall under the scope of the Law by way of example (e.g. producing goods, providing services, or generally engaging in activities that fall under the VAT regime). Furthermore, the court stated that the Law only refers to the activity of the debtor and not the activity of its subsidiaries; consequently, it is not possible for a holding company to request the transfer of all or part of its subsidiaries' assets (in case these are operational companies).

The judgement was subsequently appealed, one of the arguments presented to the court of second instance being a recent Belgian jurisprudence that would allow for the judicial reorganization of holding companies. However, the Luxembourg court maintained the decision from the lower court that the judicial reorganisation procedure by transfer of the debtor's activity applies primarily to operational companies the preservation of which should be ensured, while the holding of shares does in general not constitute such an activity.

ECJ'S YELLOW CARD TO FIFA AND UEFA

On 21 December 2023, the Court of Justice of the European Union (the "**ECJ**") adopted a ruling, in case C-333/21 European Superleague Company, on the interpretation of Articles 101 and 102 of the Treaty on the Functioning of the European Union (**TFEU**). In the ruling, the ECJ held that the *Fédération Internationale De Football Associations* (**FIFA**) and the Union of European Football Associations (**UEFA**) would breach the European Union (**EU**) rules on competition law by abusing their dominant position on the market for the organisation of European inter-club football competitions and the related commercial rights.

Background to the dispute

In April 2021, twelve (12) of the main European clubs announced the creation of a new league, the European Super League ("**Super League**"), and a company to manage it (the "**ESL**"). Following the announcement, the clubs, as well as their players, faced fierce opposition from FIFA and UEFA, who threatened to exclude them from all competitions, including competitions for nations such as the World Cup.

Aiming at avoiding sanctions, ESL sued FIFA and UEFA for damages before the Spanish courts competent for commercial disputes, claiming that the football associations would breach the EU rules on competition by relying on the provisions of their respective statutes which, respectively, (i) require their prior approval for the establishment of international football competitions for professional clubs as well as the participation thereto of clubs and their players, and establish mechanisms of supervision and sanctioning, and (ii) govern the exploitation of commercial rights related to competitions approved by both FIFA and UEFA.

Subsequently, the Spanish courts referred to the ECJ certain question on the interpretation of Articles 101 and 102 TFEU.

The issues at stake

FIFA and UEFA's immediate and vehement reaction to the proposal of organising an alternative European championship is proof of the importance of the bold move of the promoters of the Super League. The primacy of these football associations actually had never been challenged before, partly due to a well-run system, developed throughout time in order to respond appropriately to and meet the changing tastes of viewers, partly to an effective management of the rules on the access to market by FIFA and UEFA.

Interestingly, the ECJ's ruling was preceded by a (non-binding) opinion of Advocate-General (AG) Rantos (adopted on 15 December 2022) finding that FIFA and UEFA's approval and supervision rules are not intrinsically incompatible with the EU rules on competition, as *inter alia* they respond to legitimate objectives inherent in sport and would be required for the proper functioning of competitions. Thus, the mood of the EU judiciary appeared (temporarily) favourable to the incumbent football associations, adding to the general public's massive demonstrations of loyalty toward the organisers of the beloved UEFA Champions League.

The findings of the ECJ

In the ruling, the ECJ once more recognised the specificity of sport, whose economic activities present certain characteristics, such as the creation of associations to which regulatory and supervisory powers, including the power to impose sanctions, are generally attributed.

Nevertheless, the organisation of European football matches and the exploitation of the media rights are economic activities subject to EU competition rules and respect the freedoms of movement, in particular the free movement of workers. As it could be expected, the ECJ also recognised that FIFA and UEFA hold a dominant position on the market for the organisation and commercial exploitation of international matches among European football clubs.

The ECJ also found that the rules of FIFA and UEFA on the prior approval of international football competitions among clubs, such as the European Super League, constitute an abuse of dominance and, as such, are contrary to European competition law. In the ECJ 's view, the fact that a dominant enterprise – such as FIFA and UEFA – organises football events while, at the same time, enjoying the power to determine the conditions under which competing enterprises may enter the market of the organisation of competitions highlights a conflict of interests.

Given this, the powers of approval, supervision and sanction should be designed to ensure that their exercise be transparent, objective, fair and proportionate. However, the ECJ found that the powers of FIFA and UEFA are not subject to any such criteria, ultimately leading to the conclusion that the football associations abused their dominant position.

The ECJ reached similar conclusions regarding the exploitation of the commercial rights relating to football competitions, where it (obviously) observed that FIFA and UEFA's rules can be detrimental to all market players, i.e. European football clubs, media companies as well as consumers and viewers, as these would be prevented from enjoying new and potentially innovative or interesting events. The assessment of the applicability of the exceptions under Article 101, para. 3, TFEU was left to the referring Spanish courts, with the ECJ's indicating that, under these circumstances, the grounds for the application of such exception would be difficult to demonstrate.

The way forward

The ruling brought the ECJ to again consider the intersections among sports rules, the exploitation of the rights relating thereto and the economic rules of the EU Treaties. The most famous (but not the only) precedent is certainly the judgment in case C-415/93 URBSFA v Jean-Marc Bosman, having acknowledged the right of EU football players to sign for another club at contractual expiration without a need to pay any transfer fee.

Like the Bosman case, the ruling on the Super League has the potential to dramatically reshape the entire market of the organisation of football events and competitions. These may actually no longer respond to the dominance of traditional football powerful incumbents, FIFA and UEFA, but to the initiative of bold and, most of all, well-funded competitors supported by the main European football teams in the continent.

It should be stressed that the finding of abuse of dominance of FIFA and UEFA does not amount to an approval of the Super League's proposed competitions. For the time being, the ECJ served a (heavy) yellow card to the existing football associations: the ball is now in the field of the latter, whose next moves will determine whether they will remain (or fail to remain), the main reference in the organisation of European football events.

EUROPEAN COMMISSION PROPOSES ELTIF RTS AMENDMENTS

Background

Regulation (EU) 2023/606 of 15 March 2023 (the "ELTIF 2.0") entered into force on 10 January 2024. These awaited amendments to the ELTIF Regulation (EU) 2015/760 (the "ELTIF Regulation") were expected to combine the best of different investment fund types-professional and retail, open and closed-ended - into one 'fit for all purpose' vehicle. ELTIF 2.0 aimed at striking a fine liquidity balance, in order to reconcile the presence of retail investors with a wider array of eligible illiquid assets. However, ever since the adoption of the final text, market players have expressed particular concerns in relation to its impact on open-ended ELTIFs. Liquidity requirements, liquidity management tools (LMTs), notice periods and cost disclosures have been in the spotlight since the European Securities and Markets Authority (ESMA) submitted the first draft Regulatory Technical Standards (RTS) to the ELTIF Regulation in December 2023.

Key Changes Proposed by the Commission

Removal of ex post notification of material changes to redemption policy

The draft RTS provided for three business days from the date of the material change in the redemption policy to notify the ELTIF national competent authority of such changes. The Commission does not believe that ELTIIF managers can make such changes without prior authorization from the national competent authority.

Minimum notice periods for redemptions

The draft RTS provided for a notice period for redemptions of at least 12 months for all ELTIFs, unless they meet a minimum asset liquidity threshold. The Commission considered this approach arbitrary and not considerate enough of the specific characteristics of each of the relevant ELTIF portfolios. The Commission therefore recommended that the minimum notice period of 12 months be removed as a condition for all ELTIFs.

Liquidity requirements related to standardised notice periods

One of the proposals of the draft RTS was the calibration of the redemption notice period for the ELTIF based on the liquid basket of assets of the fund and taking into account the maximum amount of redeemable assets as set out in the proposed table in article 5(6) of the RTS. The Commission considered that requiring the simultaneous application of both of these requirements (minimum percentage of liquid assets and maximum percentage that can be redeemed) fails to consider the individual situation of each ELTIF.

The Commission gave the following illustration of the application of the proposed article 5(6): "*an ELTIF with a quarterly redemption frequency and a 2% gate would limit the redemptions up to 8% each year. However, the draft RTS proposed by ESMA would force such an ELTIF to maintain at least 40% of the ELTIF's portfolio in liquid assets*". This would clearly hamper ELTIFs pursuing certain investment strategies, such as real estate, infrastructure, and private equity.

The Commission also noted the problem of cash drag brought on by the proposed liquidity requirements and more general concerns about their capacity to finance long-term initiatives. It has recommended that ESMA review these clauses and make reasonable adjustments that consider the unique characteristics of each ELTIF.

Liquidity management tools (LMTs)

The draft RTS used a more constrained approach to LMTs than was envisaged under ELTIF 2.0 by mistakenly emphasizing swing pricing, redemption fees, and anti-dilution charges as the necessary LMTs. Once more, this strategy was rigid, did not take into consideration the unique characteristics of various ELTIFs, and was inconsistent with the strategy used for other alternative investment funds (AIFs).

Redemption Gates

The draft RTS obliges ELTIFs to link redemption gates to the notice period or the size of liquid assets and to establish redemption gates in certain special situations. According to the Commission, this is not compatible with the possibility of allowing redemption within the minimum limits of liquid assets during the operational period of the ELTIF. It sets additional requirements in addition to those set out in the ELTIF Regulations.

Common definitions, calculation methodologies and presentation formats of costs

The Commission identified a number of deficiencies in the approach to costs disclosures proposed by ESMA, essentially requiring better alignment of the rules with the PRIIPs Regulation, MiFID and the AIFMD.

Conclusions

From a market practice perspective, ESMA's draft RTS were lacking what the industry was expecting.

The Commission's intervention is welcomed, but there are other challenges ahead for ELTIF 2.0 such us to create an efficient investment product that can boost European long-term investments in the real economy with fewer mandatory regulations and to alleviate barriers for retail investors to invest in such EU based alternative investment fund.

EU UCITS DEEMED "EQUIVALENT" FOR UK'S OVERSEAS INVESTMENT FUNDS REGIME

The UK Government confirmed that investment funds regulated under Directive 2009/65/EC of the European Parliament and of the Council of 13 July 2009 on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities ("**UCITS Directive**") (recast), are equivalent under the UK overseas funds regime (**OFR**). On 30 January 2024, the UK Government published the statement (the "**Statement**") in respect of EU undertakings for collective investment in transferable securities (the "**EU UCITS**") and the OFR, confirming that in order to create a more streamlined process for overseas investment funds to be sold to UK investors and other relevant arguments expressed in the Statement, it has found the EEA states, including the EU member states, equivalent under the OFR.

Other Key points covered in the Statement

The Statement also cover the following matters:

- the Government does not intend to require the funds assessed to comply with any additional UK requirements as part of this equivalence determination at this time;
- the equivalence assessment does **not** include UCITS which are also money market funds (**MMFs**);
- to allow for a smooth transition for EU UCITS currently marketing in the UK under temporary arrangements, the Government is planning to extend the existing UK's temporary permissions regime until 2026 (currently to be closed at the end of 2025);
- the UK's sustainable disclosure regime (**SDR**) is currently in development - the Government will consult on whether to broaden the scope of SDR to include funds recognised under the OFR. Industry will, though, be given adequate time to adapt to any further requirements in this area.

Conclusions

We regard this as a welcome result for the managers of EU UCITS who market their funds to UK retail clients as the positive equivalence decision will remove a significant concern of disruption to these fund ranges. While it was sated that there is no intention to require EU UCITS to comply with any additional UK requirements at this time, the Statement also notes that secondary legislation will be required in due course to enact the equivalence decision.

NEW COMMUNICATION MEANS FOR AIFM REPORTING AS OF 31 JANUARY 2024

In a press release dated 31 January 2024, the Commission de Surveillance du Secteur Financier (the "CSSF") announced that a new channel is available for alternative investment fund managers to submit their AIFM reports via Application Programming Interface ("API") the eDesk platform.

Key changes

- This new communication mean enriches the Application Programming Interface ("API") solution available since 02 November 2023 allowing professionals to exchange directly with the CSSF, without using the external transmission channels.
- EDesk Report submission is only available for entities that are sender for at least one AIFM.
- EDesk allows the submission of reports and the consultation of feedback via a dashboard.

The CSSF has published a dedicated user guide which will provide technical details is available at the following link https://www.cssf.lu/en/Document/aifm-reporting-technical-guidance/.
There are therefore three channels currently for submission of the AIFM Reporting, the API solution, Via EDesk and via traditional channels. It is however expected that reporting via traditional channels will be phased out in the course of 2024.

EMIR REFIT | UPDATE OF REPORTING OBLIGATIONS

In 2012, the European EMIR regulation came into force to improve the transparency of over-the-counter (OTC) and exchange-traded (ETD) derivatives markets and reduce credit and operational risks. Twelve years later, a regime update reinforcing the requirements applicable to derivatives processing is about to come into force.

This new regime will be applied to all EU entities currently subject to EMIR reporting, i.e. financial and non-financial counterparties involved in derivatives transactions, including banks, investment funds, insurance companies and management companies/AIFMs. The requirements apply regardless of whether these entities report directly or delegate their obligations to a third party.

The Commission Delegated Regulation (EU) 2022/1855 of 10 June 2022 supplementing Regulation (EU) No 648/2012 of the European Parliament and of the Council with regard to regulatory technical standards and Commission Implementing Regulation (EU) No 2022/1860 of 10 June 2022 laying down implementing technical standard on European Market Infrastructure Regulation reporting ("**EMIR Refit**") were adopted on 10 June 2022. The European Stability Mechanism (ESMA) is taking a prominent role in providing guidance to market participants on how to comply with the new EMIR Refit reporting requirements. The Guidelines of ESMA on reporting under EMIR, published on 23 October 2023 ("**ESMA Guidelines**") provides comprehensive information on the new reporting landscape. With its Circular CSSF 23/846, the CSSF has integrated the ESMA Guidelines into its administrative practice and regulatory approach.

The EMIR Refit has not altered the fundamental objectives of EMIR, but rather seeks to improve and refine specific provisions in order to increase regulatory efficiency, reduce administrative burdens and tailor requirements for different market participants.

The EMIR Refit reporting technical standards as well as ESMA Guidelines will come into effect on 29 April 2024.

All the reports submitted by the counterparties to the trade repositories after the start of reporting under the EMIR Refit will have to comply with the amended requirements. This applies to the reports of derivatives concluded after the reporting start date and to any modifications or terminations reported after that date, irrespective of when the derivative that is modified or terminated was concluded.

New obligations

The number of fields to be declared for each transaction has increased from 129 to 203, with 77 new, 67 modified and only 3 fields deleted. The new fields include data categories relating to guarantees, product prices and specifications, and complex financial instruments.

To ensure consistency in reporting standards, the ISO-20022-XML format will now be used for transmitting data to a central repository. This aligns with the data transmission format used in MiFIR and SFTR regulations.

EMIR Refit emphasises the responsibility of the reporting entity, requiring error notifications to be sent to the regulator. There is also a stronger emphasis on data quality, starting with the Legal Entity Identifier (LEI) needing to be kept up to date.

Evolutions

The CSSF has announced a stricter position on EMIR. It has made it clear that any failure to report by 29 April 2024 will be considered a breach of EMIR reporting obligations.

With EMIR Refit on the horizon, discussions are already underway about a possible EMIR 3.0, which could bring further changes to reporting requirements.

2024 CSSF FAQ VIRTUAL ASSETS UCI UPDATES: A DOOR OPENS FOR WELL-INFORMED INVESTORS

Embracing change in the virtual asset space

The *Commission de Surveillance du Secteur Financier* ("**CSSF**") has recently revised its frequently asked questions ("**FAQ**") on virtual assets for undertakings for collective investment ("**UCI**"), marking another significant regulatory adjustment following a previous update two months ago. This change comes in response to the evolving nature of virtual assets and the growing interest from well-informed investors.

Key amendments for alternative investment funds ("AIFs")

The CSSF's latest update has significant implications for AIFs and undertakings for collective investment in transferable securities ("**UCITS**"). The CSSF now accepts that both AIFs and UCITS can invest directly and indirectly in virtual assets, provided their units are marketed exclusively to well-informed investors (previously the CSSF would not accept that such funds be marketed to any non-professional investors).

Future implications: What this means for the market

The amendments of the CSSF reflect a growing recognition of virtual assets' potential while maintaining rigorous investor protection standards. As the market for virtual assets continues to evolve, this regulatory adaptation could lead to:

- Increased participation: Enhanced access for well-informed investors could inject new capital and momentum into the virtual asset sector.
- Heightened scrutiny: With greater involvement comes increased regulatory oversight, ensuring a balanced approach between innovation and investor protection.

Conclusion: Navigating New Territories

The CSSF's updated FAQ represents a significant step forward in integrating virtual assets into Luxembourg's financial sector. By allowing AIFs to engage with these assets under stringent conditions, Luxembourg is positioning itself as a forward-thinking hub for financial innovation.

NEW AML/CTF SUMMARY REPORT TEMPLATE FOR COLLECTIVE INVESTMENT SECTOR - CSSF CIRCULAR 24/854, FAQ AND TECHNICAL GUIDE

On 29 February 2024, the CSSF published a new Circular 24/854 setting out guidelines for the submission of the SRRC (as defined below) by investment fund managers and investment funds supervised by the CSSF (the "**Circular**"). The Circular is supported with a FAQ (list of questions and answers) on the SRRC for compliance with AML/CFT obligations (the "**FAQ**") and a practical and technical guide about the SRRC (the "**SRRC Guide**").

In accordance with Article 42 (7) of CSSF Regulation No. 12-02 of 14 December 2012 on the fight against money laundering and terrorist financing, as amended, the compliance officer (*responsable du controle du respect des obligations professionnelles* (the "**RC**")) of supervised entities, including **(i)** Luxembourg investment fund managers (both authorised and registered alternative investment fund managers), **(ii)** Luxembourg branches of foreign investment fund managers; or **(iii)** Luxembourg investment funds supervised by the CSSF for AML/CFT purposes, has an obligation to prepare a summary report dedicated to AML/CFT (the "**SRRC**"). Such SRRC has to be submitted by the person responsible for compliance with the AML/CFT professional obligations at the level of the authorised management (*responsable du respect du des obligations professionnelles* (the "**RR**")) to the Luxembourg regulator, the CSSF, within five months after the closing of the annual accounts of such entities.

Purpose of the Circular and clarifications of the FAQ/SRRC Guide

The Circular has the following two main purposes:

1. To introduce the new SRRC template to the collective investment sector; and
2. To clarify the means of reporting to the CSSF.

The SRRC Guide explains the submission procedure with technical steps available for the new SRRC template.

The FAQ state that the SRRC must be exclusively submitted via the CSSF's eDesk and is under the responsibility of the RR. The RR can delegate the technical submission of the SRRC to another person, however, the RR shall remain ultimately responsible for the submission. The Circular confirms that in the case of Luxembourg investment funds which have designated a Luxembourg management company in charge of submitting the SRRC, they do not have to submit such report and consequently are out of the scope of the Circular.

Conclusions

The Circular has to be complied with for the financial years ending on or after 31 December 2023 but for financial years ending on 31 December 2023, an extension of two extra months is granted for the submission i.e. up to the end of July 2024.

LUXEMBOURG HIGHER ADMINISTRATIVE COURT RULES ON PARTICIPATION EXEMPTION AND STOCK LENDING

Key Takeaways

On 6 February 2024, the Luxembourg Higher Administrative Court **denied the benefits of the Luxembourg participation exemption** to participations which had been lent by a Luxembourg-resident capital company to third-parties as "*créances-titres*".

Facts at hand

In the case at hand, a resident parent company (the "**Company**") lent participations held into subsidiaries' capital, and which initially qualified for the purposes of the application of the local participation exemption, (the "**Participations**") to several third-parties (the "**Borrowers**") as "*contrats de prêt de titres*" (the "**Debt Securities**"). Part of the Participations were listed on stock exchanges.

By virtue of its status of lender of the Debt Securities, the Company **was remunerated** by way of interests, commissions or retrocessions of dividends derived by the Borrowers from the Participations. However, the Luxembourg tax authorities (the "**LTA**") considered, according to the facts of the case, that the Debt Securities should **not qualify for the purposes of the application of the Luxembourg participation exemption at the level of the lender, i.e. the Company**, which resulted into the qualification of (i) **the remuneration received by the Company** from the Debt Securities **as fully taxable income** from a corporate income tax/municipal business tax, and (ii) the receivable depicting the lent Debt Securities **as non-exempt assets for net wealth tax** ("**NWT**") purposes. At first instance, the Lower Administrative Tribunal agreed with the LTA that the Debt Securities should not qualify for the benefits of the Luxembourg participation exemption considering that the Company **was no longer entitled to both the legal and economic ownerships** of the Participations by virtue of the terms of the "*contrats de prêt de titres*".

Higher Administrative Court's findings

Legal ownership of the Participations

The Higher Administrative Court concluded, in light of the terms of the Debt Securities' agreements, that some of the Debt Securities had the features (i.e., fungibility of the securities to be returned or retroceded, remuneration to be paid to the Company by the Borrowers, etc.) **of "consumer credits" and not "loans for use" from a Luxembourg civil law point of view**, having the effects **of transferring to the respective Borrowers**, for the entire duration of the Debt Securities, the **legal ownership of the underlying assets**, i.e., the Participations.

Economic ownership of the Participations

The Higher Administrative Court also assessed whether the Company **could still invoke the benefits of the Luxembourg participation exemption in the light of the economic ownership approach** as provided by §11 of the *Steueranpassungsgesetz* (meaning whether the Company is treated as still being entitled to the economic rights related to the Participations from a strict tax perspective regardless of any legal ownership transfer carried-out by reasons of the "*contrats de prêt de titres*").

In the case in point, the Debt Securities' agreements entered into by the Company provided for the **payment of compensation by the Borrowers in relation to the dividends generated by the Debt Securities**, as well as, in certain circumstances, the termination of the "*contrats de prêt de titres*" leading to an earlier date for the return of the Debt Securities. In addition, the Company asserted that these Debt Securities' agreements had not been entered into with a view to obtaining a tax advantage (but for the purpose of generating additional income). In addition, some of the Debt Securities' agreements enabled the Borrowers **to benefit from market fluctuations in the share price of some of the listed Participations**. Finally, Borrowers benefited from staggered loan durations, and could freely dispose of the Debt Securities until the loans matured.

In view of the foregoing, the Higher Administrative Court concluded that the the Lower Administrative Tribunal judges **were right to find that the Borrowers also benefited from the economic ownership** (on top of the legal ownership) of the Debt Securities. Consequently, the Company was not entitled to the benefits of the Luxembourg participation exemption with respect to said assets.

Valuation of the Debt Securities into the hands of the Company for NWT

The Higher Administrative Court recalled the principle of evaluating debts at **their estimated realization value** within the meaning of §10 (1) of *Bewertungsgesetz* (“**BewG**”). In addition, § 10 (2) BewG then defines the estimated realizable value **as being the price, which in the normal course of business, would be obtained in the event of sale of the economic asset**, taking into account the nature of said asset, and specifies that it is necessary to take into account all circumstances which influence the Participations’ value.

In this case, the Debt Securities related to listed shares so that their realizable value, according to the Higher Administrative Court, **could be determined based on their stock market prices** (and not based on the Debt Securities’ nominal value as argued by the Company). Indeed, the Court considered that **the stock price should be considered as a floor value** for determining the unitary value of the Company for NWT purposes.

EUROPEAN COUNCIL: UPDATE OF THE EU LIST OF NON-COOPERATIVE JURISDICTIONS FOR TAX PURPOSES

On 20 February 2024, the European Council updated the list of non-cooperative jurisdictions for tax purposes. This list was previously updated on 17 October 2023 (please refer to our newsletters here for more details). The main change from the previous version is the withdrawal of the Bahamas, Belize, Seychelles and the Turks and Caicos Islands from the EU list of non-cooperatives jurisdictions.
As a result of these updates, the EU list now includes 12 jurisdictions:

- American Samoa
- Anguilla
- Antigua and Barbuda
- Fiji
- Guam
- Palau
- Panama
- Russia
- Samoa
- Trinidad and Tobago
- US Virgin Islands
- Vanuatu

This list, which is subject to bi-annual updates, serves inter alia as a basis, not only for certain hallmarks under the EU directive 2018/822 ("**DAC 6**") reporting obligations, but also under the refusal of deductibility on payments made to non-cooperative jurisdictions for tax purposes (please refer to our newsletters dated 1 April 2021 and 29 June 2022 for more details).

The next revision of the list is scheduled for October 2024.

TAX AUTHORITIES' OBLIGATIONS IN RELATION TO TAXPAYER'S RIGHT TO BE HEARD | JUDGMENT OF HIGHER ADMINISTRATIVE COURT

In a judgment of 11 January 2024, the Luxembourg Higher Administrative Court annulled tax assessments issued to a taxpayer for breach of the adversarial principle set out in §205(3) AO (the *Abgabenordnung*), which foresees the right for the taxpayer to be heard by the tax office before issuance of an unfavourable tax assessment.

The case concerned royalties paid to the Luxembourg taxpayer. In his Luxembourg tax return the taxpayer requested the application of the partial exemption on intellectual property income applicable at the relevant time. The tax office was of the opinion that the taxpayer was not entitled to benefit from the preferential regime for intellectual property income. In the first two letters issued by the tax office, it had based its refusal on the absence of justification for the application of the regime due to a lack of sufficient accounting documentation. Following the second letter issued by the tax office, the taxpayer was able to retrieve the necessary accounting documents from his former accountant and forward them to the tax office.

Once the tax office had received the documents, it could no longer base its refusal to apply the favourable regime on the absence of the accounting documents. As a consequence, in a third letter sent to the taxpayer, the tax office justified its refusal to apply the favourable regime on the grounds that the arm's length principle had not been respected, arguing that the royalties had been paid between related parties on terms that would not have applied between unrelated parties. In his reply to this third letter the taxpayer requested, in a 65-page response, a reasonable extension of the deadline in order to be able to prove, with the help of an external expert, that the royalties paid complied with the arm's length principle. The tax office refused to grant an extension and issued the tax assessments in accordance with the announced adjustments shortly thereafter. The Lower Administrative Court ruled in favour of the tax office, confirming that the taxpayer did not meet the conditions for benefiting from the favourable regime.

According to the Higher Administrative Court, the tax office's approach violated the adversarial principle and the taxpayer's right to be heard. According to that Court, the tax office should have granted the request for additional time to allow the taxpayer to express his views on the arm's length nature of the royalties, in particular by requesting an external expert opinion. Indeed, the previous exchanges did not concern the same aspects raised by the tax authorities at the subsequent stage and on those new aspects the taxpayer did not have the possibility to fully share his observations, thus disallowing the right for the taxpayer to be heard before issuance of an unfavourable tax assessment. The Higher Administrative Court also rejected the tax authority's argument that the tax return filed had not been signed. According to the Higher Administrative Court, this argument should have been raised before the issuance of the tax assessments and can no longer be raised in the litigation phase to deny the taxpayer a procedural guarantee intended to protect his interests.

LUXEMBOURG 2024 BUDGET BILL

On 6th March 2024, the Luxembourg government filed the 2024 budget bill ("**Budget Bill**") and announced that it will continue to work towards the implementation of a tax policy aimed at strengthening the competitiveness of the economy and increasing household purchasing power.

While certain measures have already been legislated on earlier this year, the Budget Bill has recalled the 2024 tax agenda of the government and introduced excise taxes for certain previously untaxed products assimilated to tobacco.

Luxembourg 2024 tax agenda

- **Implementation of the 2023-2028 coalition program**: a series of tax measures in favour of the Luxembourg real estate sector have already been issued in February 2024 (see our previous newsflash) and the investment tax credit have been extended to investments and expenses incurred in the context of digital transformation as well as energy and ecological transition (see our previous newsflash). Further measures will be taken during 2024 notably to reduce the tax burden of taxpayers belonging to class 1a (mainly widowed individuals, taxpayers with children and taxpayers aged at least 65). As a reminder, the government is working on setting up a single taxation class for individual taxpayers and the proposal should be published in 2026. Regarding corporate income tax ("**CIT**"), the coalition program included a reduction of applicable rate to reach OECD countries' average rate. The Minister of finance announced a potential 1% reduction of the CIT rate as from 2025, with more details coming in the next months.
- **Continuation of Pillar 2 implementation**: the Luxembourg government remains involved in the Luxembourg implementation of Pillar 2 (see our previous newsflash). As a reminder, Luxembourg already implemented Pillar 2 with the income inclusion rule and qualified domestic top up tax applicable as from 1st January 2024 and the undertaxed payment rule applicable as from 1st January 2025. Measures introduced by the OECD December 2023 administrative guidance have not been integrated yet.
- **Involvement in EU tax initiatives:** (i) Unshell Directive proposal, also known as ATAD III, pertaining to the minimum level of substance of certain EU companies (see our previous newsflash), (ii) BEFIT Directive proposal aimed at implementing a harmonized tax base for large MNEs active in the EU and simplifying certain transfer pricing compliance for low-risk distributors and contract manufacturing (see our previous newsflash), (iii) HOT Directive proposal aimed at simplifying the tax compliance obligations of SMEs operating in other EU member states through permanent establishments (see our previous newsflash), (iv) the EU Commission initiative "VAT in the Digital Age" aimed at (a) modernising VAT reporting obligations and introducing e-invoicing for cross-border transactions, (b) addressing the challenges of the VAT treatment applicable to the platform economy, and (c) avoiding the need for multiple VAT registrations in the EU (see our previous newsflash), and (v) EU initiatives in the field of energy taxation.
- **Involvement in OECD tax initiatives:** OECD Pillar One pertaining to a tax base reallocation towards consumers countries for in-scope MNEs (see our previous newsflash).

Taxation of emerging products assimilated to tobacco

The Budget Bill also introduced taxation though excise duty for new products similar to manufactured tobacco: e-cigarettes (e-liquids: maximum of EUR 200 per litre), nicotine sachets (maximum of EUR 100 per kilogram) and heating tobacco (maximum of 41.50% of retail price for the *ad valorem* part and a maximum of EUR 35 per kilogram).

These products will be subject to excise duty as from 1st October 2024 to leave sufficient time to manufacturers to take appropriate compliance steps.

UPDATE TO THE COMMENTARY ON ARTICLE 26 OF THE MODEL TAX CONVENTION

On 19 February 2024, the OECD Council allowed an update to the **Commentary 26 of the OECD Model**, which relates to the **exchange of information**, more specifically to the question of administrative assistance.

As a reminder, the exchange of information process was set up in 2009 in order to improve the rules on tax transparency. The aim of the exchange of information is to prevent tax fraud and tax avoidance. However, Article 26 of the OECD Model was considered incomplete regarding the information obtained through administrative assistance.

As a result of the update, it has been specified that information received under administrative assistance may be used in tax matters concerning persons other than those in respect of whom the information was originally received. The requesting State will not be obliged to inform the requested State of such use, or to request its authorization.

In addition, the update provides an **interpretative guidance on confidentiality** and more precisely regarding the access of taxpayers to information exchanged when such information has a bearing on their tax situation and regarding reflective non-taxpayer specific information, including statistical data, about or generated on the basis of exchanged information.

For example, the update takes the following forms:

"(…) The confidentiality rules also apply to reflective non-taxpayer specific information (…) However, such reflective non-taxpayer specific information may be disclosed to third parties if the information does not, directly or indirectly, reveal the identity of one or more taxpayers and the sending and receiving States have consulted with each other and it is concluded that the disclosure and use of such information would not impair tax administration in either the sending or the receiving State. (…).

As an example, in the context of an exchange of information that contains information with respect to multiple taxpayers, the principle (…) means that a taxpayer is a "person concerned" only to the extent that the information has a bearing on the outcome of a tax matter concerning that particular taxpayer (…)

(…) Such use is not limited to the assessment or collection of, the enforcement or prosecution in respect of, or the determination of appeals in relation to the taxes referred to in paragraph 1 in respect of the person or persons for which the information was received, but also includes the use for such purposes in respect of any other person. The receiving Contracting State is not required to inform or to request authorisation from the sending Contracting State regarding such use (…)".

This update of Article 26 of the Model Convention is particularly welcome, as it provides further clarification of the exchange of information, especially regarding administrative assistance.

ECON OPINION ON EC PROPOSAL FOR TRANSFER PRICING DIRECTIVE

Urgent need to implement harmonized transfer pricing framework for the EU according to ECON

On 22 February 2024, the Economic Monetary Affairs Committee ("**ECON**") of the European Parliament adopted its opinion on the European Commission's ("**EC**") proposal for a Directive on transfer pricing ("**TP Directive**") introduced on 12 September 2023 (the "ECON Report"). For further information on the proposed TP Directive, please refer to our previous newsflash.

The ECON Report which received strong support in committee will be considered by Parliament's plenary before advancing to the Council for further deliberation.

The ECON Report emphasizes the urgent need to promptly implement harmonised transfer pricing rules to prevent multinational enterprises from exploiting the lack of EU harmonisation on the matter.

According to the rapporteur, Kira-Peter Hansen, the opinion emphasizes democratic and future-proof measures to combat transfer pricing abuses within the EU. The proposal underscores the importance of reinstating the EU Joint Transfer Pricing Forum and acknowledges the potential relevance of alternative guidelines, such as those from the United Nations, alongside the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations ("**OECDTPG**").

Key amendments of the ECON Report to EC's proposal

The proposed amendments to the TP Directive aim at enhancing the effectiveness and consistency of transfer pricing regulations within the EU and covers the following key points:

- **Shortening entry into force**: the proposal advocates for bringing forward the entry into force from 2026 to 2025.
- **Reinstatement of the EU Joint Transfer Pricing Forum**: there is a call for reinstating the EU Joint Transfer Pricing Forum to enhance cooperation and coordination among EU member states in transfer pricing matters, fostering consistency and effectiveness in regulatory enforcement.
- **Alignment with OECD TPG**: emphasis is placed on aligning as closely as possible the TP Directive rules with the latest OECD TPG to ensure regulatory coherence and harmonization with international standards.
- **Empowerment of the EC**: ECON Report seeks to empower the EC to propose additional implementing rules on transfer pricing matters, enhancing regulatory agility and capacity to address emerging challenges effectively.
- **Dispute Resolution Mechanisms**: introducing of "fast-track" mechanisms which can respond to all demands. The proposal outlines the importance of having access to dispute resolution mechanisms to prevent double taxation and ensuring greater tax certainty for taxpayers involved in cross-border transactions within the EU. It suggests strengthening the use of Mutual Agreement Procedures and invites the Members States to allocate resources on this tool.
- **Simplification and mitigation of double non-taxation**: introducing the possibility for the EC to adopt further rules, such as safe harbours, to simplify the application of the arm's length principle in the EU, to ensure more tax certainty and mitigate the risk of double non-taxation and double taxation, and to reduce tax disputes and tax abuse.
- **Sunset Clause**: according to which it should first cease to apply to companies falling under the scope of the proposal for a Council Directive on Business in Europe: Framework for Income Taxation (see our previous newsflash on BEFIT) as of 2035 and as of 2040, for all other multinational enterprises operating in the EU, except for their transactions with third countries.

Conclusion

In a nutshell, the proposed amendments focus on shortening the implementation, promoting tax transparency and coordination, outlining dispute resolution mechanisms, and empowering the EC to take further measures in the field of transfer pricing. The ECON Report is expected to be voted on at the plenary session of the European Parliament on 10 April 2024, representing a significant step in shaping the final text of the Directive.

RELEASE OF PILLAR ONE AMOUNT B REPORT

On 19 February 2024, the OECD/G20 Inclusive Framework ("**IF**") on BEPS released its report on Amount B of Pillar One intended to simplify transfer pricing aspects of baseline marketing and distribution activities, alleviate administrative burden, cut compliance costs, and enhance tax certainty.

Although IF members' work on Amount B is still ongoing with further information to be released later in 2024, certain sections of the report have already been integrated in the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations 2022 as an Annex to Chapter IV.

Scope of Amount B

Under Amount B the following transactions are considered as "Qualifying Transactions":

- **Buy-sell marketing and distribution transactions** where the distributor purchases goods from one or more associated enterprises for wholesale distribution (i.e., distribution to any type of customer except end consumers) to unrelated parties; and
- **Sales agency and commissionaire transactions** where the sales agent or commissionaire contributes to one or more associated enterprises' wholesale distribution of goods to unrelated parties.

These "Qualifying Transactions" are then subject to two further scoping rules:

- The qualifying transaction must exhibit economically relevant characteristics: it can be reliably priced using a one-sided transfer pricing method, with the distributor, sales agent or commissionaire being the tested party.
- The tested party in the qualifying transaction must not incur annual operating expenses lower than 3% or greater than an upper bound of between 20% and 30% of the tested party's annual net revenues.

Further exclusions apply where the qualifying transaction involves the distribution of non-tangible goods, services or the marketing, trading, or distribution of commodities or the tested party carries out non-distribution activities in addition to the qualifying transaction, unless the qualifying transaction can be adequately evaluated on a separate basis and can be reliably priced separately from the non-distribution activities.

Further qualitative criteria are being developed and shall be released by 31 March 2024.

Amount B as the simplified and streamlined ("S&S") approach

The determination of the arm's length remuneration for transactions in scope is made under the S&S approach:

- **Transfer pricing method:** the transactional net margin method ("**TNMM**") shall be applied to transactions in scope without any further justifications or analysis of other transfer pricing methods. The report acknowledges that in certain cases the comparable uncontrolled price method using internal comparables might be more appropriate and shall be used in due place.
- **Determination of the arm's length return under the S&S approach:** a pricing matrix is provided by the report to determine the arm's length return based on the tested party's industry (divided in three groups), operating expense intensity and operating asset intensity. A 0.5% tolerance applies.
- **Profitability adjustment:** two control points shall apply that can lead to an adjustment, (i) the return on operating expenses that is checked based on a predetermined cap-and-collar range and (ii) a specific adjustment, based on a specific formula provided by the report, which applies for qualifying jurisdictions (list to be published) where relevant data is insufficient.
- **Documentation:** taxpayers shall maintain a certain level of information (though their local file where applicable): explanation on delineation of qualifying transaction (including functional analysis and context), written contract or agreements supporting the delineation, relevant calculations, connection between financial data used and financial statements. Provision of such information should not prevent tax authorities to review taxpayers' self-assessment. Upon first application of the S&S approach, taxpayers should provide relevant tax authority with a consent to apply the approach for a

minimum of 3 years (unless transactions are no longer in scope during that period).
- **Tax certainty and elimination of double taxation:** the report contains further information on Mutual Agreement Procedure ("**MAP**") where a corresponding adjustment cannot be provided under domestic legislations. Notably where one of the jurisdictions involved has chosen to not apply the S&S approach, taxpayers and jurisdictions involved shall justify their positions under the OECD TPG without relying on the S&S approach during the MAP process. Agreements pertaining to a Qualifying Transaction already in place before implementation of the S&S approach would continue to be valid (under Article 25 of the OECD MTC, APAs or MAPs).

A non-binding mechanism

The S&S approach is not mandatory for countries including IF members and jurisdictions choosing to implement the S&S approach can either grant the possibility to use such approach or require taxpayers to mandatorily apply the approach for transactions in scope.

The outcome determined under the S&S approach in a jurisdiction choosing to apply the approach is non-binding on the counterparty jurisdiction. However, members of the IF members committed to respect such outcome when applied by a low-capacity jurisdiction (list to be issued).

Conclusion

Although the scope of Amount B is limited to Qualifying Transactions, it does not set a minimum revenue threshold for taxpayers to fall in scope. The list of countries applying the S&S approach should be monitored notably for those electing a mandatory approach. Further work is ongoing at OECD level notably regarding the qualitative criteria for scoping purposes, update of Article 25 of the OECD MTC, competent authority agreements to be used in the context of double tax treaties and relationship between Amount B and Amount A under Pillar One.

ECJ RULES ON DEDUCTIBILITY OF INPUT VAT FOR "NON-OPERATING COMPANIES" (C-341/22)

On 7 March 2024, the Court of Justice of the European Union ("**ECJ**") handed down a judgment regarding the right to deduct input value added tax ("**VAT**") for a company which was deemed "non-operational" by the national tax authority.

In the case at hand, a company carried out an economic activity of producing and marketing wine in the Campania region. For the year 2008, the local VAT authority considered that the company was non-operational since its output transactions subject to VAT were below the threshold under which, for the purposes of Italian law, companies were presumed to be non-operational. Italian law provided that in such circumstances the right to deduct input TVA and obtain a refund of such input VAT should be denied.

The questions referred

The national court first asked whether it is compatible with Article 9 (1) of the Directive of 28 November 2006 on the common system of value added tax (the "**VAT Directive**") that the right to deduct input VAT paid may be denied to a company that carries out transactions subject to VAT while not reaching the income threshold provided for by the Italian legislation at issue, where that company does not demonstrate that objective circumstances rendered it impossible to achieve income higher than that threshold.

By its second question, the national court asked, in essence, whether Article 167 of the VAT Directive and the principles of VAT neutrality and of proportionality must be interpreted as precluding national legislation under which the taxable person is denied the right to deduct input VAT on account of the transactions subject to output VAT carried out by that taxable person being considered insufficient.

The ECJ judgment

The ECJ answered the first question by stating that the status of a taxable person is not subject to satisfying a particular threshold of transactions and should only be determined according to whether that person actually carries out an economic activity. The ECJ therefore considered the national legislation at issue to be incompatible with article 9 (1) of the VAT Directive.

With regard to the second question, the ECJ reaffirmed that the right to deduct input VAT is a fundamental principle of the common system of VAT. That right to deduct is subject to meeting two conditions: (i) the person must be a taxable person within the meaning of the Directive and (ii) there must be a direct and immediate link between a taxable person's input transactions and output transactions. The ECJ recalled that the immediate and direct link requirement is met where the cost of goods and services are part of the taxable person's general costs and as such components of the price of output transactions.

The ECJ concluded that no provision of the VAT Directive makes the right of deduction conditional upon the taxable person reaching a certain threshold amount of output transactions subject to VAT and that the right of deduction is ensured irrespective of the results of the economic activities in question. According to the ECJ, the objective of preventing fraud and abuse did not justify the application of a presumption based on a certain income threshold which was unconnected to identifying fraud or abuse. Fraud and abuse must be established according to the facts in the case, in accordance with the requisite legal requirements and cannot rest on assumptions or presumptions.

The ECJ concluded that the VAT Directive and the principles of VAT neutrality and of proportionality prohibit national legislation which denies a taxpayer person's right to deduct on the basis that the taxpayer carried out an insufficient amount of transactions subject to output VAT.

APPRECIATION OF THE 90% THRESHOLD IN THE CONTEXT OF ARTICLE 157TER LITL | THE LOWER ADMINISTRATIVE COURT DECISION

In a judgment dated 7 February 2024 (*docket No. 46783*), the Luxembourg Lower Administrative Court (*Tribunal administratif*) (the "**Court**") handed down a decision concerning the application of the provisions of Article 157*ter* of the Luxembourg income tax law ("**LITL**"), allowing non-resident taxpayers to request, under certain conditions, to be treated as resident taxpayers for tax purposes.

As a reminder, non-resident taxpayers earning taxable income in Luxembourg are, in principle, only authorised to deduct their operating expenses or costs insofar as these expenses or costs have a direct economic link with the relevant Luxembourg income.

However, Article 157*ter* LITL provides that non-resident taxpayers may be taxed, on their income taxable in Luxembourg, at the (effective) rate that would be applicable to them if they were resident in Luxembourg if:

1. they are taxable in Luxembourg on at least 90% of their total income, both Luxembourg and foreign; or
2. the sum of their net income not subject to Luxembourg income tax is less than EUR 13.000.

In these circumstances, a notable consequence is that, contrary to what has previously been stated, non-resident taxpayers are entitled to deduct the expenses in the same conditions as those applying to resident taxpayers. Under this regime, married taxpayers are also taxed collectively unless they request to be taxed separately. In this case, it is sufficient that one of the two taxpayers meet the above conditions.

The main question submitted to the Court in the present case focused on the qualification of a capital gain realised on the disposal of a shareholding for the purposes of the verification of the conditions provided by this Article.

Facts of the case

At the moment of the filing of their tax return for the fiscal year 2019, the taxpayers expressed their intention to opt for the application of the provisions of Article 157*ter* LITL and for collective taxation.

The taxpayers' income consisted of (i) salary income from a profession exercised in Luxembourg, (ii) net investment income arising from dividend distributions made by Luxembourg resident companies and (ii) a capital gain arising from the disposal of shares held in these Luxembourg companies.

The tax office denied the benefits of Article 157*ter* on the grounds that the taxpayers were taxable in Luxembourg on less than 90% of their total worldwide income and that the annual net income not subject to Luxembourg income tax was greater than EUR 13.000.

Findings of the Court

The Court starts its reasoning by recalling that the determination of domestic income is based on Article 156 of the LITL and that all the income of a taxpayer which is not taxable in Luxembourg on the basis of this provision is considered as foreign income for the application of the regime of Article 157*ter* LITL.

The Court notes that, at the date of the disposal, the shareholdings represented less than 10% of the share capital of the relevant companies and had been held for a period of more than 6 months. These were therefore not disposals of shareholdings that could be considered as "significant" within the meaning of Article 100 LITL. It also notes that the taxpayers had not been resident in Luxembourg for more than 15 years and had become non-resident less than 5 years before the disposal of the shareholdings.

In these circumstances, the capital gain realised on the disposal of these shareholdings is not considered as domestic income within the meaning of Article 156 LITL.

According to the Court, if the source of the income is indeed Luxembourg as raised by the taxpayer, what is decisive for the verification of the 90% threshold is the domestic nature of the income according to Article 156 LITL.

This is not the case for the capital gain realised in this case on the disposal of the shareholdings, so that the taxpayers are not taxable in Luxembourg on at least 90% of their worldwide income.

As the capital gain on the disposal of the shareholdings is not taxable in Luxembourg as explained above, it must also be concluded that the income of the taxpayers not subject to Luxembourg income tax exceeds EUR 13.000, the amount of the capital gain having to be included in the calculation of this threshold.

Conclusion

The Court therefore concludes that the taxpayers are not entitled to claim the application of Article 157*ter* LITL insofar as they do not meet the conditions required by that provision to benefit from the regime of assimilation of non-resident taxpayers to resident taxpayers.

JUDGEMENT OF THE HIGHER ADMINISTRATIVE COURT NO. 49770C – PRINCIPLE OF A SINGLE LAWYER OR REPRESENTATIVE IN TAX LITIGATION

On 23 October 2023, the Lower Administrative Court (*Tribunal administratif*) handed down a judgement in direct tax matters, in which it dismissed as inadmissible an appeal lodged with it, on the grounds that the principle of a single lawyer or representative had been breached. The appeal was indeed lodged with the Lower Administrative Court on behalf of the taxpayer by both a chartered accountant and a foreign lawyer practising in Luxembourg under his original title.

While the single-lawyer principle already existed before the judicial courts, it is was for the first time (to the best of our knowledge) that this principle was applied by the administrative courts.

Subsequently, acting this time through one single lawyer, the taxpayer appealed against the first instance judgement arguing notably that the sanction for breaching the principle of a single lawyer or representative could not be the inadmissibility of the appeal in the absence of any effective prejudice to the rights of defence of the State party.

In a judgment dated 7 March 2024 (docket no. 49770C), the Higher Administrative Court (*Cour administrative*) firstly enshrined the principle of one single lawyer/representative in tax litigation. Secondly, the Higher Administrative Court overruled the decision of the Lower Administrative Court in that the sanction of a violation of said principle may only be an inadmissibility of the appeal lodged with it in case the right of the defence have been effectively prejudiced, which the State party was unable to demonstrate in the case at hand.

PREVIOUSLY PUBLISHED IN TAX

- Newsflash | Pillar Two - The Luxembourg Tax Authorities issue a first FAQ
- Newsflash | Tax measures in favour of the Luxembourg real estate sector

CONTRIBUTORS

Gaston Aguirre Draghi, Marc-Alexandre Bieber, Fahri Can Dogan, Yunus Cekici, Harun Cekici, Mikail Ceylan, Nuala Doyle, Gaëlle Felly, Ali Ganfoud, Chloé Kaizer, Gözde Kitapci, Sophie Labruyère, Evelyn Maher, Djelloul Mansour, Camille Mascolo, Pol Mellina, Alessandro Morini, Ailyn Sandra Pérez Utria, Daniel Riedel, Olivier Schank, Laura Simmonds, Nicolas Widung