

## Ratification of the new tax treaty between Luxembourg and France



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Today, the Luxembourg parliament ratified the new double tax treaty signed on 20 March 2018 between Luxembourg and France, which will replace the current double tax treaty dated 1 April 1958. The new provisions should enter into force as from 1 January 2020.

The Luxembourg parliament also ratified a double tax treaty with Kosovo, as well as protocols to the double tax treaties with Belgium and Uzbekistan.

### Ratification of the new double tax treaty between Luxembourg and France

Today, the Luxembourg parliament ratified the new double tax treaty signed on 20 March 2018 between Luxembourg and France (the “New Treaty”). The New Treaty will replace the current double tax treaty dated 1 April 1958, which has been amended several times (the “Old Treaty”). The provisions of the New Treaty will apply as from 1 January 2020 if both countries exchange their instrument of ratification before 31 December 2019, which is expected to be the case.

The New Treaty provisions, together with a comparison with the Old Treaty provisions, are summarised in our Newsflash published at the time of signing of the New Treaty.

The provisions that are expected to have the most significant impact - in particular on cross border investments - and the main outstanding points that need clarification are summarised below.

### Real estate vehicles – withholding tax on dividends

The new article 10 on dividends is expected to have the most significant impact on existing cross-border investments. It notably provides that dividends originating from income or capital gains derived from real estate assets by an investment vehicle situated in a Contracting State (i) that distributes the major portion of this income annually and (ii) whose income and gains derived

from such real estate assets are exempt from tax, may benefit from a 15% withholding tax rate, provided that the beneficial owner thereof is a resident in another Contracting State holding a direct or indirect participation representing less than 10% of the share capital of the distributing investment vehicle. If the beneficiary of such dividends holds a direct or indirect participation representing 10% or more of the share capital of the distributing investment vehicle, the dividends will be subject to tax at the rate foreseen by the domestic tax laws of the source Contracting State.

This means that distributions made by French exempt real estate vehicles (typically established as organismes de placement collectif en immobilier or OPCI, or as sociétés d'investissement immobilier cotées or SIIC) to a Luxembourg company directly holding at least a 25% participation in the distributing vehicle, which had been subject under the Old Treaty to a reduced withholding tax rate of 5%, will now, under the New Treaty and French domestic law, be subject to withholding tax at a rate of 30%.

Such distributions could nevertheless still benefit from a 15% withholding tax rate under French domestic law, provided that the beneficiaries are collective investment vehicles ("CIV") that can be assimilated to French CIV. To determine whether a Luxembourg CIV can be assimilated to a French CIV, reference can be made to the French guidelines<sup>1</sup> that detail the conditions of application of this rule per type of CIV. It remains to be clarified whether certain Luxembourg investment funds such as the reserved alternative investment fund or RAIF (which are not subject to approval or registration with a competent authority but have to be managed by an authorised AIFM) can be assimilated to a French UCI.

### **CIVs – comparable analysis**

More globally, under the New Treaty, with respect to dividends paid by a company resident in one of the Contracting States to a CIV located in another Contracting State, the exemption of withholding tax or the reduced treaty rate may apply<sup>2</sup>, provided that such CIV can be assimilated to a CIV located in the Contracting State of the paying company. The New Treaty and the parliamentary comments have unfortunately not provided any details for the comparative analysis. One could certainly refer to the above mentioned French guidelines with respect to dividends distributed by French companies to Luxembourg CIVs.

### **Real estate investments – French partnerships**

Another point of attention relating to French real estate investments concerns the interpretation of item 5 of the Protocol to the New Treaty, and in particular the tax treatment of income derived by Luxembourg corporate investors from French partnerships<sup>3</sup>, including inter alia the non-application of a tax credit on a potential municipal business tax charge. Taxpayers concerned are advised to closely monitor any developments in this respect.

## **Permanent establishment**

The new provisions on permanent establishments and commissionaire arrangements<sup>4</sup> are also expected to have a significant impact on Luxembourg taxpayers carrying out activities in France via agents (in particular insurance companies, banks and asset managers). For instance, under the new provisions, a Luxembourg insurance company having operations in France may be deemed to have a permanent establishment in France as soon as one of its dependent agents “habitually plays the principal role leading to the conclusion of contracts that are routinely concluded without material modification by the enterprise”. Any developments relating to the practice of the French tax authorities in this respect (i.e., the extent to which France will invoke these new provisions to recognize there a taxable presence) will have to be closely followed.

## **Commuters**

Finally, item 3 of the Protocol to the New Treaty will be of significant interest for the 95,000 French commuters who are employed in Luxembourg: if they are professionally active in France or in a third State (being neither France nor Luxembourg), they will remain taxable only in Luxembourg provided their activity outside Luxembourg does not exceed 29 days within the fiscal year.

In addition, French commuters will not be exempt in France on their Luxembourg salaried income, but subject to tax there with a tax credit for the amount of Luxembourg tax imposed<sup>5</sup>.

## **Other points**

The Luxembourg parliament also ratified today the following agreements:

i,§ The tax treaty signed on 8 December 2017 between Kosovo and Luxembourg. The new tax treaty mainly follows the OECD Model Convention, and its provisions will apply as from 1 January 2020 if both countries exchange their instruments of ratification before 31 December 2019.

ii,§ The protocol to the double tax treaty between Belgium and Luxembourg signed on 5 December 2017, which will amend the double tax treaty of 1970, as amended by the 2002 and 2009 protocols. The amendments formalize a political agreement reached in 2016, which broadly aimed at granting a 24-day tolerance of professional presence in Belgium or in a third country for Belgian residents employed by a Luxembourg employer, without triggering any taxation in Belgium on their salaried income. The protocol will apply to all salaries, wages and other remuneration relating to taxable periods beginning on or after 1 January 2015.

iii,§ The protocol to the double tax treaty between Uzbekistan and Luxembourg signed on 18 September 2017, which will amend the double tax treaty of 1997. The amendments mainly

concern the update of provisions on exchange of information in order to align them with the OECD Model Convention. A new article deals with the assistance in the collection of taxes. The protocol also introduces anti-abuse provisions in line with BEPS action 6, namely a new preamble and a principle purpose test.

### **Concluding remarks**

Following the ratification by the Luxembourg parliament of the New Treaty with France, its provisions will most likely apply as from 1 January 2020. As initially anticipated, the new provisions on dividends, in particular those related to dividends distributed by French exempt real estate vehicles to Luxembourg residents are likely to have the most significant impact on cross-border transactions. A few points (such as the comparable analysis for CIV) need clarification, and corporate taxpayers are advised to closely monitor any developments in this regard.

The ratification of the tax treaty with Kosovo and of the protocols to the tax treaties with Belgium and Uzbekistan demonstrates Luxembourg's continuing political will to develop and adapt its treaty network (mostly) in line with OECD-BEPS developments.

1 BOI-RPPM-RCM-30-30-20-70.

2 Pursuant to item 2 of the Protocol to the New Treaty.

3 That is sociétés de personne, such as sociétés civiles immobilières or SCI, and sociétés en nom collectif or SNC.

4 Article 5.

5 Under Article 22.