AUXADI

COMPLEXITIES IN NEW MARKETS

LUXEMBOURG

In this series, we discuss some of the complexities to consider when expanding your business across borders, or if you're looking at multinational investment. There are many issues for investigation, and different countries have very different legislation, regulation and tax regimes.

Here, we delve into the complexities to keep in mind when expanding or investing into Luxembourg.

Introduction

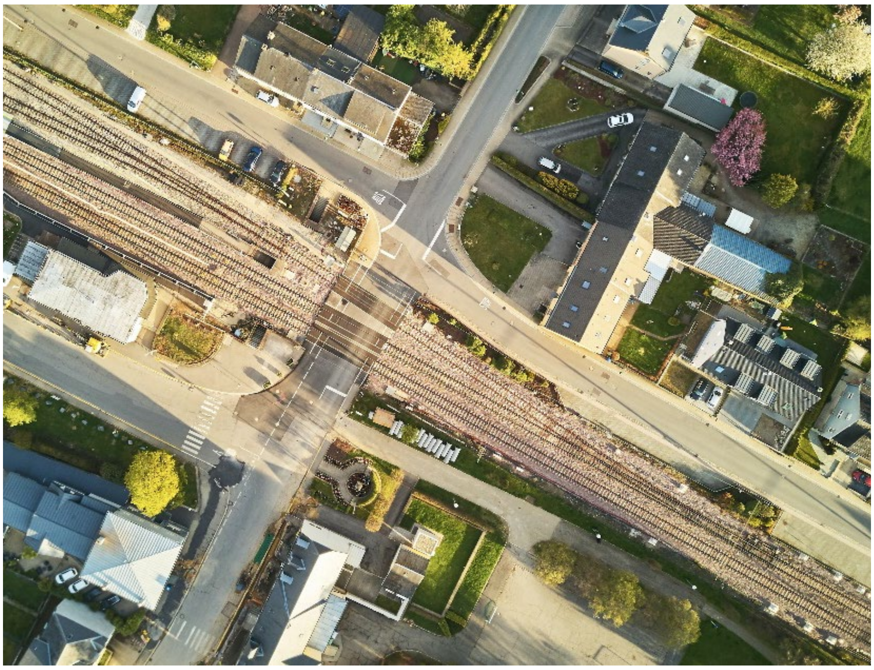
Luxembourg is home to one of the most stable economies in the EU and, despite its small size, ranks as one of the wealthiest countries in the world in terms of GDP per capita. The transport infrastructure is well developed, with direct access to the rest of Europe and North Sea ports, and its technology infrastructure is renowned. Luxembourg hosts the majority of the EU's Tier IV data centres and in 2020 the country ranked third in the EU for connectivity. And, its status as the home of the European Court of Justice makes it an important EU centre.

Widely recognised as one of the most competitive financial centres in Europe, the services sector comprises around 80% of Luxembourg's GDP, and the success of the financial industry is thanks to its cross-border financial expertise, range of financial services offered, political stability, and its qualified multilingual workforce holds significant purchasing power.

Luxembourg is the second-largest fund domicile in the world and assets under management of Luxembourg-domiciled funds hit a record €5 trillion in January 2021. Luxembourg's investment funds have a dominant share in Europe and are the vehicle of choice in many parts of Asia, Latin America and the Middle East – indeed, they're distributed into over 70 countries. Luxembourg is also a major centre for alternative assets with more than €843 billion of assets managed by alternative fund managers. Luxembourg-based funds also benefit from the European passport, which means that funds (and their managers) comply with the UCITS Directive, the AIFM Directive (AIFMD), and can be marketed to investors in the European Economic Area (EEA).

Luxembourg only ranks 72/190 for Ease of Doing Business, however, so there are issues to be aware of. The incorporation process is somewhat complicated compared to other EU members, with different steps required based on specific business activities. The process of registering a company is relatively easy, though a business licence is required before operations begin, and that can take 15 days. Fund setup, approval, and formation can take many months.

Luxembourg is definitely one of the most favourable domiciles in Europe, but local knowledge is essential to navigate the lengthy processes and intensive regulations.



Foreign Direct Investment (FDI)

According to figures from OECD, half the FDI received by Luxembourg comes from the countries of the European Union, although the main investor is Bermuda (13.5%), followed by the UK (13.1%), Ireland (12.1%) and the Netherlands (9.3%). Financial and insurance activities attract more than four-fifths of all investments (81.6%), with manufacturing accounting for only 2.8%.

The government of Luxembourg has been working to make the country even more attractive to FDI, offering fiscal benefits for equipment and construction projects, focused on key innovative industries like: logistics, ICT, health technologies (including biotech and biomedical research), clean energy, space technologies, and financial services tech.

81,6%

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Doing business and establishing a company/fund

As stated above, Luxembourg rates 72/190 in the 2020 World Bank Ease of Doing Business report, so there are definite hurdles to clear. Incorporation takes around 16 days and will require a Notary Public.

The most common **company structure** is the S.A. or Public Limited Company, though the country also allows cooperative companies and limited partnerships.

Public Limited Company (Société Anonyme SA)	Private Limited Company (Société à responsabilité limitée SARL)	Limited Partnership (Société en commandite simple/ spéciale)	General Partnership (société en nom collectif SENC)	Cooperative Company (société coopérative SCOP)
One or more natural or legal persons, no maximum.	Minimum 1 (single member SARL), maximum 100. (1 member for a sole proprietorship).	Minimum 2, no maximum.	At least two partners (a legal person may be a partner.)	At least two partners. No legal limit.
€30,000 with 25% released on creation.	€12,000 fully subscribed.	No minimum.	No minimum.	No minimum.
The shareholders are liable up to the level of their contributions. The founders are jointly and severally liable to third parties: • for the capital not validly subscribed and for the difference between the minimum capital requirements and the subscribed amount; • for the effective payment of 25% of the subscribed shares and for the payment, within 5 years, of shares issued for non-cash contributions; • for the redress of damage arising from either the nullity of the company or the absence or non-conformity of statements in the company deed or object.	The founders of the company and, in the event of an increase in capital, the managers, are jointly liable in respect of third parties for: • any part of the capital that is not validly subscribed, and for the difference between the minimum capital and the subscribed capital; • the full payment of the shares and the portion of the capital for which they have subscribed; • remedying any damages arising from: - the company's nullity; or - omissions or inaccurate statements in the company's deed of incorporation. The shareholders are liable to the extent of the amount of their contribution.	General Partner liability is joint. Limited Partner limited to the amount contributed.	Partners' liability is joint and unlimited on obligations and debts. The managers, as representatives of the company, are liable for their misconduct while carrying out their mandate.	Partners' liability depends on the status. If the articles of association say nothing in this regard, the partners shall be indefinitely and jointly liable. Each year, one half of the company's profits and losses are to be shared equally among the partners, and the other half in proportion to their stake in the company. The founding partners are jointly liable for certain commitments made at the time of the company's formation, and also for any misdeeds committed at the time of the company's formation.

In addition, the government has taken measures to encourage new businesses, including a 25% exemption on income and business taxes for eight years.

Luxembourg is a popular domicile for all fund asset classes including private equity, real estate, debt and infrastructure funds. There are several categories of investment vehicles to choose from, based on the target assets, the target investors, and the region and manner of marketing. These include:

- Part II UCI (undertakings for collective investment)
- SIF (specialised investment fund)
- SICAR (investment company in risk capital)
- RAIF (reserved alternative investment fund)
- Soparfi (non-regulated ordinary commercial company)

Part II UCIs, SIFs and SICARs are so-called regulated investment vehicles, and therefore subject to direct supervision of the Commission de Surveillance du Secteur Financier (CSSF). These structures require CSSF approval before they can be set up.

RAIFs and Soparfis are unregulated investment funds, so not subject to direct supervision of the CSSF and not needing CSSF approval. These structures can be formed as soon as the constitutive documents have been finalised and arrangements with service providers are complete.

The CSSF approval process can take many months, and the information required is extensive. Drafts of the constitutive documents, offering documents, key service providers agreements (agreements for depositary, central administration, management, advisory, audit, global distributor, etc,), and key policies (risk management, conflicts of interest, anti-money laundering policies, etc,). The CSSF also needs information on the members of the governing body and the manager and/or adviser. Upon completion of the regulatory review, regulated investment vehicles receive the authorisation to establish. Once formed, vehicles are registered on an official list maintained by the CSSF.

Part II UCIs, SIFs, SICARs and Soparfis which qualify as Alternative Investment Funds (AIFs) under the AIFM Law (12 July 2013) must be managed by an alternative investment fund manager (AIFM) authorised or registered under the AIFM Directive (AIFMD). Authorised AIFMs can opt for any form of commercial company under Luxembourg law, but usually take the form of an S.A. or a SarL.

Another fund area popular in Luxembourg is distressed debt and NPLs.

Gaining CSSF approval can be harrowing and it's always best to have an experienced advisor guide you through the process.

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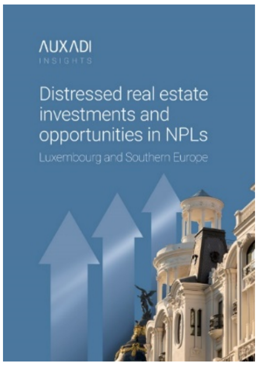
is distressed debt and NPLs.
More on these in our White Paper.



Tax, accounting and regulation

Luxembourg has been working towards harmonising its financial standards, both within the EU and at the international level, including the 2019 implementation of EU BEPS legislation ("Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting" - aimed at combating tax avoidance by multinational companies).

Although Luxembourg has favourable tax treaties with a number of countries and relatively low corporate tax rates, its business tax requirements can be difficult. Companies must face many different taxes each year, which collectively involve c. 55-60 hours annual admin time.

Luxembourg has a 17% VAT rate, though there are reduced rates and excluded items. Excise duties are levied in accordance with EU legislation.

Lux-resident entities are taxed on their worldwide income, though non-resident entities are only taxed on their Luxembourg-sourced income. Resident companies and subsidiaries of foreign companies are also subject to wealth tax of 0.5% up to €500 million. Entities with a taxable base over €500 million are to pay a lump-sum fee of €2.5 million, along with 0.05% of the tax base in excess of €500 million, without any limit.

A subscription tax is levied on transferable securities at a rate of 0.05% for mutual funds, based on net assets at the end of the quarter. This rate is reduced to 0.01% for specialised investment funds and reserved alternative investment funds. Graduated rate reductions also apply for funds that invest in "sustainable" investments.

The rate of municipal business tax levied on income depends on the municipality. The municipal tax for Luxembourg City is 6.75%.

As of 2021, a new Real Estate Levy of 20% (Article 4 – "*prélèvement immobilier*") applies to certain investment fund vehicles.

The Luxembourg fiscal year is 1 January to 31 December, and financial statements must be structured using IFRS and be submitted in one of the country's three administrative languages (French, German, Luxembourger).

Labour and payroll matters

The 2021 monthly minimum wage is €2,202, though the median monthly salary is €4,070, based on a 40-hour working week. Overtime is only permitted in special circumstances as outlined in the labour laws and subject to ministerial authorisation.

Indefinite period contracts are by far the most common, though around half of employees have their pay and conditions set by collective agreements, so employers are obliged to deal with trade unions on request. Trade unions are active in several sectors, mainly defending union interests in collective negotiations during meetings with employers, public and social authorities, and providing judicial aid.

Around 50% of Luxembourg's workers live outside the country's borders and commute in to work – an entirely feasible option given the excellent transport links, high costs of living, and small geographic size of Luxembourg. Known as *frontier workers*, these country-commuters benefit from the best of both worlds for taxes and costs of living, but they can provide payroll headaches for employers.

Frontier workers can come and go with no restriction if they're EU/EFTA nationals; they're under no obligation to register in Luxembourg. However, third-country nationals must hold a valid work permit for Luxembourg, Germany, France or Belgium, as well as a valid employment contract clearly stating that they may need to work some days of the month in Luxembourg.

Frontier workers pay taxes in Luxembourg for the income from the country; they don't pay taxes in Luxembourg for their worldwide income as they are non-residents. They pay Luxembourg social security just like residents, but they are not entitled to the same benefits as residents.

Banking

The Luxembourg banking sector is highly competitive and strongly niched; different banks prefer different types of activity. However, with 128 banks to choose from, you should be able to choose from multiple options – but the focus is on asset management and private banking, not business banking.

Most banks offer remote openings, though expect minimum balance requirements and charges for different business services. Some will only consider EU-based companies and structures or require EU substance or ties, while others will service not only non-EU companies, but offshore, and even trading companies.

Prospective account holders are generally screened and approval is based on the bank's internal policy, what type of account you want to open, your business operations, and so on – which essentially boils down to how profitable the bank expects you to be (and subsequently, how profitable you'll be for the bank).

Thorough research is required to understand a bank's requirements, preferences, and sensitivities before approaching them to open an account, but these can also be difficult to find. Local knowledge and introductions can be invaluable.

Conclusion

Luxembourg is a tiny country with a big reputation. It's a massive financial hub, a first choice for many sectors and a popular jurisdiction for structuring alternative investment funds, but there are quite a few challenges to navigate – it's definitely not as easy as it seems. Knowledge is key.

Local experts can provide you with the inner-working knowledge of Luxembourg's regulations, legislation, and specific peculiarities that you'll need to successfully navigate this EU hub.

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