



MERGERS AND ACQUISITIONS

Luxembourg

Taxation of Cross-Border
Mergers and Acquisitions

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TAX

Luxembourg

Introduction

To strengthen Luxembourg's financial sector and attract more cross-border transactions the Luxembourg legislature has passed several laws designed to simplify the legal framework for cross-border mergers and acquisitions (M&A) involving Luxembourg entities and create more flexible restructuring possibilities.

Luxembourg companies may be involved in domestic and cross-border mergers de-mergers in various ways. Luxembourg has implemented the European Union (EU) Merger Directive to create several possibilities of tax neutral company reorganizations.

This chapter provides a general overview of tax and other issues relating to cross-border M&A in Luxembourg and clarifies the frameworks within which the different operations may take place. The following aspects are analyzed in particular:

- the opportunities available to the acquirer when purchasing of shares or assets;
- the choice of acquisition vehicles available to the acquirer; and
- questions relating to the funding of the acquisition.

Recent Developments

The law of 10 August 1915 on commercial companies has been amended by the law dated 23 March 2007, which provides a new framework and facilitates mergers and divisions of Luxembourg companies.

Since 2007 cross-border mergers involving Luxembourg companies without forming a European company (*societas europaea*) permitted under Luxembourg law, but there has been no clearly defined legal framework for them. A 2008 amendment made good this deficiency. More recent developments relate mainly to the legal framework in which the transactions take place. The new law of 10 June 2009 introduces a new legal framework for cross-border mergers in Luxembourg applicable to both to intra-EU and extra-EU mergers.

Any Luxembourg company can be merged into a foreign company if:

- the foreign company or economic interest group is formed in accordance with the law of a foreign state;
- the law governing the foreign entity allows cross-border mergers as a matter of principle; and
- the foreign entity complies with the national provisions and formalities of the foreign state.

Asset Purchase or Share Purchase *Purchase of Assets*

The purchase of an asset usually increases the cost base of the asset and is taxable in the hands of the seller, but Luxembourg tax law differs in its treatment of transfers of 'private' and 'business' assets. With business assets (held by a company), a capital gain on disposal must be included in the business profit of the seller, and is not subject to a specific tax rate.

Capital gains realized on assets other than real estate or a substantial participation held as private property (that is, not held by a company) are exempt unless they qualify as speculative gains under Art. 99bis of the Income Tax Law, which is to say unless the gain is realized within the six months of the acquisition of the asset or the disposal precedes the asset's acquisition.

It should be noted that the liabilities associated with the transferred asset remain with the seller and are not transferred with the asset.

Purchase Price

When a Luxembourg entity directly acquires a business, the acquisition price of the assets will normally represent the basis for their depreciation for Luxembourg tax purposes and the (depreciated) acquisition costs will determine gains or losses arising on a subsequent disposal. If, however, a business is acquired from a related party at a price deemed not to be arm's length, a tax adjustment may be made.

Goodwill

Under Luxembourg tax law, each asset transferred should be allocated its own distinct value, which forms the base cost for depreciation purposes. It may be that the total value exceeds the sum of the values attributed

to each asset; in such a case, the excess is deemed to constitute goodwill. Goodwill is depreciable under Luxembourg tax law, and the normal practice is to write goodwill off over 10 years.

Financial fixed assets, such as participations, are not generally depreciable even if there is a goodwill element in the purchase price, but a deductible write-down in value is permitted following a prolonged reduction in the value of the participation. The minimum value to which participation may subsequently be written-up is the acquisition value.

Depreciation

Fixed assets are, in principle, subject to an annual depreciation that should be deductible from the taxable income of the Luxembourg company. Generally, the straight-line method is applied for the computation of the amount of depreciation. The declining-balance method may also be used in certain cases, but not for buildings and intangible assets.

With the approval of the tax administration, depreciation on the basis of asset use may be applied to assets whose annual use fluctuates widely. Extraordinary depreciation may also be permitted if there is excessive wear and tear, or other sharp reductions in value of the assets. Buildings used for business purposes may be depreciated over their useful lives, but land may not be depreciated.

Apart from a few assets covered by administrative circulars, there are no specified rates of depreciation. The depreciation period should reflect the useful life of the asset. Rates commonly used in practice are:

Depreciated Item	Rate (%)
Buildings	1.5-5
Vehicles	20-25
Machinery and equipment	10-25

Reference is generally made to German rules for depreciation periods.

Tax Attributes

Losses which arise on the disposal of assets may offset other taxable income of the Luxembourg company. If the losses exceed the taxable income, they may be carried forward indefinitely against future profits of the Luxembourg entity. It is important to note, however, that any tax loss carry-forwards of the Luxembourg company selling the assets may not be transferred to the buyer of the assets.

Value-Added Tax (VAT)

The normal VAT rate is 15 percent. When assets are transferred individually, the transferred items within the scope of VAT are subject to the normal VAT rules for goods and services.

However, a merger or division is, in general, not subject to VAT, because the transfer of all assets forming the whole or part of a business is not deemed to constitute a supply of goods for VAT purposes. There is deemed to be continuity between the transferee and the transferor.

Transfer Taxes

No stamp duty is generally payable on the transfer of assets, but the transfer of immovable property is subject to registration duty of 6 percent of the value of the real estate, plus an additional transfer duty of 1 percent, and for certain real estate in Luxembourg City, there is a supplementary municipal duty of 3 percent. A registration duty of 0.24 percent may apply on debt if it is mentioned in notarized deeds or presented to certain Luxembourg public authorities.

No proportional registration duties apply to the transfer of other assets (for example, shares in Luxembourg companies) if the transfer is subject to VAT.

Purchase of Shares

As a rule, the purchase of a target company's shares should not affect the book values of its assets, and the assets of the target company cannot be revalued to reflect fair market values.

The acquirer should record the participation acquired in its balance sheet at the acquisition price, plus costs directly connected with the acquisition.

Tax Indemnities and Warranties

Since the purchaser is taking over all the liabilities, including contingent liabilities, he/she will require more extensive indemnities and warranties than in the case of an acquisition of assets. Due diligence of the target company's tax position is advisable, particularly when the amounts involved are significant.

In principle, indemnity payments received by a Luxembourg company pursuant to a warranty clause are subject to tax in the hands of the company and a Luxembourg company making such an indemnity payment is, in principle, entitled to deduct it for tax purposes.

Tax Losses

As a rule, tax losses may only be deducted by the company that originally incurred them. It follows that where a Luxembourg company is absorbed by an existing or a newly incorporated company, its tax loss carry-forward may not be transferred. It may, however, be possible to disclose latent capital gains of the absorbed company, to be offset by unused tax losses. Accordingly, the absorbing company may acquire assets on a stepped-up basis and benefit from higher depreciations.

As long as a Luxembourg company continues to exist following these types of restructuring, its tax losses may, under certain conditions, be carried forward. Conversely, should two or more Luxembourg companies be merged to create a new company, the tax loss carry-forward of each disappearing entity would be lost.

Crystallization of Tax Charges

Whilst there are no specific rules under Luxembourg tax law, a purchaser should perform a due diligence to assess the tax position of the target company and risks it may entail.

Pre-Sale Dividend

The treatment of pre-sale dividends (distributions by the subsidiary of retained earnings before disposal) may benefit from the participation exemption. When the subsidiary company distributes dividends to its parent company any write-down in value of the participation held by the parent company in the subsidiary is not deductible to the extent of the amount of dividends distributed.

Transfer Taxes

No stamp duty is payable on the transfer of shares in capital companies. Registration duty may be levied on the transfer of all or most of the shares in certain vehicles that hold only real estate. In some cases, the tax authorities may apply a look-through and consider that the real estate rather than the company has been transferred and duty will be levied accordingly. Special rules apply in the case of a transfer of partnership interests with underlying real estate.

Tax Clearances

The taxpayer can, in general, ensure the Luxembourg tax treatment of a restructuring by applying for a written advance tax clearance from the tax authorities.

Choice of Acquisition Vehicle

There are several potential acquisition vehicles available to a foreign purchaser and tax factors will often influence the choice. Following the abolition of Luxembourg duty on capital contributions as from 1 January 2009, the incorporation of Luxembourg companies and subsequent increases in capital are no longer subject to capital duty.

Local Holding Company

Instead of acquiring the assets and liabilities comprising a business, which is often not tax-efficient, purchasers may choose to set up a holding company to acquire the shares of the target company.

The two legal forms of limited liability companies widely used in Luxembourg are the following:

- Public limited company (société anonyme); a joint-stock company with freely transferable shares. Since 25 August 2007 the one-person public limited company (société anonyme unipersonnelle) has been introduced to Luxembourg company law. The conditions are the same except that, at the organization level, the board of directors may be represented by one director, and the general shareholders meeting may be attended by only one shareholder.
- Limited liability company (société à responsabilité limitée); a private limited company with restrictions on the transfer of shares. Since 28 December 1992, the one-person limited liability company ('société à responsabilité limitée unipersonnelle) has been introduced to Luxembourg company law, which may have also only one shareholder.

These companies are fully taxable corporations with equity investments, and may benefit from the Luxembourg participation exemption regime, unless they are subject to a specific tax regime

Following the abolition of the 1929 holding regime Luxembourg tax legislation also provides for the private family asset holding company (société de gestion de patrimoine familiale – SPF); an investment vehicle for individuals introduced by the law of 11 May 2007. This type of company has been specially designed to meet the business needs of family-owned holding companies managing financial assets. The exclusive objective of an SPF is the acquisition, holding, management and disposal of financial assets, to the exclusion of any commercial activity.

In addition, the Luxembourg domestic law provides for other types of entities, including in particular:

- Partnership limited by shares
- Societas europaea
- Partnership
- Limited partnership
- Joint ventures
- A cooperative society
- A civil company and
- An economic interest grouping

Foreign Parent Company

The foreign purchaser may choose to make the acquisition itself, perhaps to shelter its own taxable profits with the financing costs. This should generally not trigger any adverse Luxembourg tax consequences. Interest payments are, in principle, not subject to Luxembourg withholding tax (WHT). Although dividend payments are in general subject to 15 percent Luxembourg dividend WHT, a WHT exemption is provided under domestic tax law if certain conditions are met. Since 1 January 2009, the scope of this WHT exemption has been extended (subject to certain conditions) to parent companies resident in countries with which Luxembourg has concluded a double tax treaty (DTT).

Non-Resident Intermediate Holding Company

If the foreign country taxes capital gains and dividends received from the Luxembourg target company, an intermediate holding company resident in another jurisdiction could be used, inter alia, for tax deferral purposes. It should be noted that Luxembourg tax treaties often do not include extensive anti-treaty shopping rules.

Local Branch

As an alternative to the direct acquisition of the target's trade and assets, a foreign purchaser may structure the acquisition through a Luxembourg permanent establishment (PE). The income attributable to the PE is subject to Luxembourg taxation, but dividends and capital gains realized on disposal of a shareholding in a Luxembourg company may, under certain conditions, benefit from the Luxembourg participation exemption regime. The repatriation of profits to the foreign head office will not trigger additional taxes on branch profits.

Joint Ventures

Whenever a joint venture takes a form in which the company is legally and fiscally recognized as an entity distinct from the participants, it is taxed according to the regime applicable to corporations (see above).

In other cases, the income is taxable in the hands of the individual venturers under the rules applicable to partnerships (see above). This is in particular the case for a European economic interest grouping (groupement Européen d'Intérêt économique – GEIE).

The profits are allocated on the basis of the joint venture agreement.

Choice of Acquisition Funding

To fund an acquisition, the acquiring company may issue debt notes, equity, or a combination of the two. The following describes the tax aspects to be considered when deciding the funding structure.

Debt

Interest expenses incurred to fund the acquisition of assets are, in general, deductible as long as the arm's length principle is satisfied.

In the case of an acquisition of shares, the interest deduction may be restricted or subject to claw-back (a recapture provision which may lead to taxation of part of the capital gain on a disposal of the shareholding) if the acquiring company benefits from the participation exemption. Expenses relating to a participation qualifying for the participation exemption are deductible only to the extent that they exceed exempt income (dividends) arising from the participation in a given year. Depending on the specific circumstances, however, there are several ways to achieve a deduction of interest even if the debt is used to finance participation.

No WHT is levied in Luxembourg on interest payments unless the loan is a direct profit-participating loan, bonds and similar securities. Furthermore should the recipient of the interest payments be EU resident individuals or Luxembourg resident individuals, withholding tax may be due on the grounds of the EU Savings Directive or Luxembourg domestic final withholding tax.

Deductibility of Interest

Luxembourg tax law does not stipulate a specific debt-to-equity ratio, but the tax authorities require companies to comply with the arm's length standard. With a holding company they require a debt-to-equity-ratio of 85:15 to finance shareholdings. Provided no guarantees are given by the shareholders, third party debt is

disregarded in this computation. Moreover, no debt/equity minimum applies to back-to-back loans or assets other than shareholdings or real estate.

If the required ratio is not met, the portion of interest paid in excess of the ratio could be regarded, for Luxembourg corporate tax purposes, as a hidden distribution of profits, which is in principle not tax deductible and subject to 15-percent WHT, unless the EU Parent-Subsidiary Directive or a DTT provides relief.

Withholding Tax on Debt and Methods to Reduce or Eliminate

According to Luxembourg domestic tax law, no WHT is levied on arm's length interest payments with the exception of interest on profit participating bonds or similar securities. Interest payments on such financing instruments would, in principle, be subject to Luxembourg WHT of 15 percent if:

- the loan is structured in the form of a bond or similar security; and
- in addition to the fixed interest, supplementary interest varying according to the amount of distributed profits is paid, unless the supplement is stipulated to vary inversely with the fixed interest.

It is, however, possible to use profit-participating financing instruments that do not fall within the aforementioned scope and whose interest payments should not, therefore, be subject to Luxembourg WHT.

If recipients of interest payments be EU-resident individuals, however, WHT tax may be due under the EU Savings Directive.

Checklist for Debt Funding

- Interest payments are, in principle, not subject to Luxembourg WHT.
- The maximum 85:15 debt-to-equity ratio must be respected when financing participations.
- No debt-to-equity ratio has to be respected in back-to-back financing.

Equity

From 1 January 2009, the cumulative corporate tax (municipal business tax plus corporate income tax) for companies established in Luxembourg City amounts to 28.59 percent. If the investor wants to fund the acquisition as far as possible with debt, the Luxembourg tax law is, in general, very flexible, since it does not impose any strict debt-to-equity ratios on ordinary taxable companies. Informal limits are, however, applied

by the tax authorities for the financing of an acquisition of a subsidiary (participation) by inter-company loans. In this situation, the tax authorities generally consider a ratio of 85:15 as being in line with the arm's length principle, which means that 85 percent of the purchase price of participation may be financed by an inter-company loan. Interest rates must not exceed market rates, otherwise part of the interest may be treated as a hidden profit distribution.

For the purposes of determining the debt-to-equity ratio, a zero-rate loan from shareholders may be treated as equity for corporate income tax purposes, so it may be possible to structure funding with a 92:8 debt-to-equity ratio:

Scenario	Equals
Subscribed and paid in capital	1
Zero-rate shareholders loan	14
Total equity for debt-to-equity purposes	15
Maximum interest-bearing liabilities	85

Source: KPMG in Luxembourg, 2008

Such a funding structure should be analyzed on a case-by-case basis. It is generally accepted that non-interest-bearing loans, properly documented and accounted for, should not be subject to the 1 percent capital contribution tax as long as the loan has all the required legal characteristics (date of repayment, etc.).

Any excess interest payments that result from an excess over the above debt-to-equity ratio would be reclassified as hidden dividend distributions.

Dividends are subject to WHT at a rate of 15 percent. If the participation exemption applies (see below), there may be an exemption from WHT.

No WHT tax is levied on liquidation or partial liquidation proceeds.

Share-for-Share Exchange

Description

A share-for-share exchange is the contribution of shares by the shareholders of the target company to the acquiring company against allocation of shares in the acquiring company to the shareholders of the target company, or the exchange of shares in the target company against shares in the acquiring company in the context of a merger/division at the level of the shareholder of the target.

Tax Treatment

Basically, a share-for-share exchange constitutes a taxable sale followed by an acquisition for the disposing shareholder. However, Luxembourg tax law provides for tax-neutral restructuring in the following circumstances.

Article 22bis of the Luxembourg income tax law provides a limited list of share exchanges at book value that may be tax-neutral at the level of the Luxembourg shareholder (that is, no realization of capital gains):

- Transformation of the legal form of corporation to another legal form of corporation.
- Merger/de-merger of resident companies or EU-resident companies (entities that are covered by Article 3 of the EU Directive 434/90) or capital company or cooperative company resident in a EEA State other than an EU Member State fully subject to a tax corresponding to the Luxembourg corporate income tax.
- Exchange of shares (in a company being a EU/EEA-resident company or a capital company fully taxable subject to a comparable effective tax rate of 10.5 percent on a similar base of the Luxembourg ones) in the case the acquiring company (being a EU-resident company or a capital company fully taxable subject to a comparable effective tax rate of 10.5 percent on a similar base of the Luxembourg ones) obtains the majority in the voting rights in the acquired company or increases the majority of voting rights already held.
- Article 166 LIR provides for a participation exemption for qualifying investments held by resident taxable companies and qualifying branches of non-resident companies—the exemption is extensive and covers capital gains in case of share-share exchange at fair market value triggering a capital gain.
- Article 54 LIR provides for rollover relief if sales proceeds are invested in a qualifying asset or participation under certain conditions.

In the event none of the above tax-neutrality, exemption, or rollover provisions can be applied, the share-for-share exchange will, in principle, be fully taxable (specific structuring may still be possible to achieve tax neutrality, depending on the economic circumstances). However, if the shareholders are resident individuals, the gain would be taxed in accordance with Luxembourg tax law only if the participation realized represented at least 10 percent of

the shares of the target company. Such a gain may be taxable at half the normal rate.

Non-resident shareholders would be taxed only if a participation representing at least 10 percent of the shares of the target company were sold within a period of six months following the acquisition of the shares, or if the investor were a Luxembourg tax resident for a period of more than 15 years and had ceased such residency less than five years previously. Most of Luxembourg's bilateral tax treaties provide for capital gains to be taxed in the state of residence of the entity or individual realizing the gain.

Transfer of Assets at Book Value

Article 170 paragraph 2 LIR provides for the possibility of transferring assets at their book value, or at a value between book value and their market value. This allows for the transfer of assets without the realization and thus taxation of underlying capital gains. This provision does not give a definitive tax exemption of the capital gains attached to the transferred assets, but merely allows a deferral until their subsequent realization.

The following conditions must be fulfilled:

- the absorbed and absorbing company must be resident in Luxembourg within the meaning of Article 159 of the LIR and fully subject to Luxembourg corporate income tax;
- the shareholders of the absorbed company must receive, in consideration of the transfer of its shares, shares by the absorbing company newly issued for this particular purpose; if the absorbing company has a participation in the absorbed company, then this participation must be canceled. The absorbed company must be dissolved;
- the parties must take steps to ensure that the capital gains (hidden reserves) ultimately will be taxable; that is, the absorbing company must make an entry in its fiscal financial statements reflecting the book value of the assets transferred to it by the absorbed company; and
- in cases where the absorbing company holds a participation in the absorbed company, the former must produce evidence to the tax administration to the effect that the merger is based on sound business principles.

If the transfer is not made at book value, but to the extent that the value attributed to the assets exceeds their book value, this will create taxable income in the

absorbed company (this can provide a useful way of absorbing losses of the absorbed company, which would otherwise disappear along with the company). The higher reported amount of the assets transferred in the balance sheet of the recipient company would therefore result in a higher depreciation of the acquisition costs of the transferred assets.

Transfer of a Business by the Target Company

Description

Contribution of the entire business of the target company or contribution of only an independent branch of activity of the target company can be made to an acquiring company in exchange for shares in the acquiring company (a share capital company). In this case, the target company remains in existence and, depending on the size of the companies involved, the company acquiring the business may become a subsidiary of the target company whose sole remaining activity is the holding of shares in the acquiring company.

Tax Treatment

Article 59 LIR, which is applicable if either all assets and liabilities are transferred by the target company or a branch of activity is transferred (the target company remaining in existence), provides that, in principle, hidden reserves cannot be transferred to the acquiring company, because the assets involved are revalued to market value, thus exposing any increase in value over book value to taxation at normal rates at the level of the target company. The minimum value at which the acquiring company may value the assets transferred is thus book value.

However, if both the target and acquiring companies are fully taxable companies, resident in Luxembourg or in another EEA/EU Member State, Articles 59(3) and 59 bis (1) LIR provide that the assets may be transferred to the acquiring company at book value, market value, or an intermediate value at the election of the target company, thus deferring taxation. The maximum value at which the acquiring company may value the assets transferred is market value.

If the receiving company is resident in another EU country, any Luxembourg-based assets must be transferred to a Luxembourg permanent establishment of that company to benefit from a tax neutral treatment.

Hybrids

Hybrid financing instruments may be treated in Luxembourg as equity for tax purposes and as debt in

another country, and vice-versa. Some countries have a formal approach to classifying an instrument, while others have an economic approach and analyze the effective characteristics of the instrument. Such differences of approach between countries can give rise to international tax planning opportunities. Typical examples are profit-sharing loans and silent partnerships.

One example of such an opportunity is when a Luxembourg contractual partnership is set up in the form of a typical silent partnership. This type of business participation is treated in Luxembourg as debt, so profit allocations to the silent partner are deductible in Luxembourg if certain conditions are met. By contrast, the foreign partners may be resident in countries where the participation is treated as equity and the distribution of its profits may, therefore, be treated as a dividend and be eventually tax exempted, depending on the foreign tax law and the relevant DTT.

Discounted Securities

The tax treatment of securities issued at a discount to third parties normally follows the Luxembourg GAAP accounting treatment, with the result that the issuer should be able to obtain a tax deduction for the discount accruing over the life of the security.

Deferred Settlement

Where acquisitions involve elements of deferred considerations (that is, the amount of the consideration depends on the business' post-acquisition performance), such future consideration should be regarded as part of the sale price. If the sale price relates to shares disposed of, the deferred settlement may be eligible for the Luxembourg participation exemption regime as an element of a capital gain on shares.

Other Considerations

Concerns of the Seller

A sale of shares of a Luxembourg company may be tax exempt, if the seller is either a Luxembourg corporation under the capital gains substantial participation exemption, or a non-resident, because Luxembourg usually loses the right to tax capital gains under DTTs and non-resident sellers who do not benefit from treaty protection when disposing of shares in a Luxembourg company are not taxable in Luxembourg after a holding period of six months has elapsed.

The sale of shares does not trigger registration or stamp duty (except in some cases if sellers hold Luxembourg real estate).

In an acquisition for cash of all the assets of a Luxembourg company, the seller is subject to Luxembourg corporation tax on any capital gains, but certain techniques are available to the seller to defer taxation, for example, by reinvesting the sale proceeds in fixed assets, or reducing the tax basis if the sale takes place in the course of the liquidation of the seller.

Company Law and Accounting

Merger

Until 1987, mergers under Luxembourg company law (loi sur les sociétés commerciales) involved the liquidation of one or more companies and the subsequent contribution by the liquidator of its assets and liabilities to the other party to the merger. Shares issued as consideration for the contribution were distributed to the shareholders of the liquidated company.

The law of 7 September 1987 adapted Luxembourg company law the Third (1978) and Sixth (1982) European Union (EU) Company Law Directives on the merger and division of public limited companies.

Following the enactment into domestic law of the Third and Sixth EU Company Law Directives in 1987, mergers of two or more Luxembourg public limited companies (S.A.s) can be effected only by absorption of an existing company or by the incorporation of a new entity. In both cases the target companies of the merger are dissolved without liquidation and all assets and liabilities are contributed to the absorbing or newly created entity.

Finally, the Law of 23 March 2007 amended Luxembourg company law to implement the European company and simplify the rules and conditions on mergers and divisions. This law allows a cross-border merger between any Luxembourg company with a legal personality, and companies governed by a European or foreign law if the national law of the relevant country agrees. (Entities with legal personalities are société anonyme, société en commandite par actions, société à responsabilité limitée, société en nom collectif, société en commandite simple, associations en participation, société coopérative, société civile, groupement d'intérêt économique).

A merger can also occur where one or more of the companies or economic interest groupings that are acquired or will cease to exist are the subject of bankruptcy proceedings relating to litigations with creditors or a similar procedure such as the suspension of payments, control of the management of the company or proceedings instituting special

management, or supervision of one or more of such companies.

A merger is effected by the acquisition of one or more companies by another (merger by acquisition) or by the incorporation of a new company (merger by incorporation of a new company). In exchange, the shareholders receive shares and possibly a cash payment not exceeding 10 percent of the nominal value of the shares issued. In both cases the target companies of the merger are dissolved without liquidation and all assets and liabilities are transferred to the absorbing or newly created entity.

Division

The concept of a division was introduced to Luxembourg company law by the law of 7 September 1987, which enforced the European Economic Community (EEC) Sixth Directive (82/891/EEC, dated 17 December 1982).

According to Luxembourg company law, a division is defined as an operation in which a company (the company being divided), after its dissolution, but without going into liquidation, contributes its assets and liabilities to two or more pre-existing or newly formed companies (the recipient companies) in exchange for the issue of shares to shareholders, possibly with a cash payment not exceeding 10 percent of the nominal value of the shares issued.

The Law of 23 March 2007 made some amendments in Luxembourg company law to implement the European company and simplify the rules and conditions for mergers and divisions. This law allows a cross-border division between any Luxembourg company, having a legal personality, and a European or a foreign law-governed company if the national law of the relevant country agrees.

A division can also occur when one or more of the companies or economic interest groupings that are acquired or will cease to exist are the subject of bankruptcy proceedings relating to litigations with creditors or a similar procedure, such as the suspension of payments, control of the management of the company or proceedings instituting special management, or supervision of one or more of such companies.

The law on commercial companies distinguishes between a division by absorption and a division by creation of one or more companies. In exchange, the shareholders receive shares, possibly with a cash payment not exceeding 10 percent of the nominal value

of the shares issued. Under a division by absorption, the company transfers, during its dissolution but without going into liquidation, all assets and liabilities to two or more pre-existing companies in exchange for the issue of shares to its previous shareholders. Under a division by creation of one or more new companies, the company transfers, during its dissolution without going into liquidation, all assets and liabilities to one or more newly-formed companies in exchange for the issue of shares to its previous shareholders.

A company being divided can, under company law, transfer all its assets and liabilities to two or more newly-formed or pre-existing companies. The partial division, where only parts of the company's assets are transferred, qualifies as a capital reduction under company law.

The Newly Adopted Law

On May 6 2009 the Luxembourg Chamber of Deputies adopted Bill 5829 relating to cross-border mergers of limited liability companies (the bill is expected to be published as law shortly), which, among other things, implements Directive 2005/56/EC of the European Parliament and of the Council dated October 26 2005.

This law comes at a particularly appropriate time in the current global economic crisis, and completes the introduction of Directive 2005/56/EC, following on from the law of March 23 2007. It completes a simplification of the legislative framework for both Luxembourg and cross-border mergers of limited liability companies, easing restructuring and cooperation across borders on a European and international level.

The principal amendments of the law relate to the Luxembourg law of August 10 1915 on commercial companies.

Scope

The scope of the law is wider than that of Directive 2005/56/EC, in that it allows for cross-border mergers between Luxembourg limited liability companies and EU companies, as well as non-EU companies, insofar as the law of the non-EU country does not prohibit such mergers. If one merging company is operating under an employee-participation system and the company resulting from the merger must also operate under such a system and is a Luxembourg company, it can only take the form of a société anonyme.

Luxembourg did not include the option that the national government could oppose a cross-border merger on

public interest grounds, as was suggested in Article 4 (1) (b) of Directive 2005/56/EC.

Luxembourg included undertakings for collective investment in transferable securities (Ucits) within the scope of the Law, thus allowing for mergers among Luxembourg Ucits, unlike Directive 2005/56/EC, which explicitly excluded Ucits from its scope. Luxembourg also opted for to apply the law to co-operative companies.

Procedural Steps for Cross-Border Merger

Directive 2005/56/EC sets out 12 items to be included in the written common draft terms of cross-border mergers that involve Luxembourg limited liability companies, which must be established by the management of the merging companies. They include the same basic principles required in the common draft terms for mergers of Luxembourg companies, and additional information for cross-border mergers and mergers resulting in the creation of a European company (EC).

The common draft terms of mergers must be published in the relevant national gazette at least one month before the general meeting of shareholders of the merging companies, convened to approve of the merger. The managements of the merging companies must draw up a report explaining the economic and legal aspects of the merger, and the impact on shareholders, employees, and creditors.

For cross-border mergers, this report is to be made available at least one month before the general meeting of shareholders of the merging companies. In the absence of unanimous approval of the merger by the shareholders of both companies an independent expert appointed by the management of the merging companies must prepare a report on the proposed merger.

The expert's and management's reports inform the decision of the general meetings of the merging companies on the proposed merger, which must be approved with the same quorums and majorities required for amending the company's articles. The independent expert's report and relevant documents are only necessary if they are required by the national law of the absorbed or absorbing company, and if the absorbing company holds 90 percent or more, but not all the shares and securities that confer rights to vote in the general meetings of the absorbed company.

Validity and Effect of the Merger

In Luxembourg, the notary is the national authority responsible for the verification of the legality of the merger, and in particular must ensure that the merger proposal has been agreed on the same terms by each merging company. The notary may be required to issue a certificate attesting to the legality of the merger. The merger will be effective in relation to third parties as of the publication of the deed of the general meeting approving it or, if no such meeting is required, on publication of the notary's certificate.

Once merged, the absorbed company ceases to exist and its rights and obligations are transferred to the absorbing company. If the cross-border merger has taken place in accordance with the law, it cannot be declared null and void. (For exceptions to this, see Article 21 of the Law, modifying Article 276 of the 1915 Law.)

Although the concept of mergers was established in the 1915 Law, it was clear that an update in line with current market trends and practices was needed. The 2009 and 2007 laws are both parts of a continuing modernization of Luxembourg company law designed to make Luxembourg more competitive and enable domestic companies to benefit further from the single market and the flexibility and adaptability of Luxembourg company law.

Group Relief/Consolidation

Under Luxembourg tax law, resident companies may be authorized to file consolidated tax returns for corporate income tax and municipal business tax, but not for Net Wealth Tax. An application must be made for a period of at least five years. If a company leaves the group within five years, the overall group results will be adjusted if tax savings have been made through compensation for the losses of the departing company. Qualification for fiscal integration requires financial integration (that is, 95 percent, or in some cases 75 percent, of the shares in the subsidiary or the Luxembourg permanent establishment must be held directly or indirectly by the fully taxable resident capital company, or by a Luxembourg permanent establishment of a non-resident capital company fully liable to a tax that corresponds to Luxembourg corporate income tax). An organizational or economic integration is no longer required, as of 2002.

If the participation is held indirectly, it is necessary for the companies through which the parent company or the Luxembourg permanent establishment holding 95 percent of the share capital of the subsidiary that is to be integrated for tax purposes, to be capital companies

fully liable to a tax which corresponds to Luxembourg corporate income tax; namely a tax compulsorily levied by public authorities at a rate of at least 10.5 percent of a base calculated in accordance with rules and criteria similar to Luxembourg's. The 95-percent shareholding condition must be satisfied continuously from the beginning of the first accounting period for which tax consolidation is requested.

Fiscal integration is also allowed for municipal business taxes on profits. The conditions for integration for municipal business tax purposes have been harmonized with those for corporate income tax, as of 2002.

Losses incurred prior to a company's inclusion in a fiscal integration group cannot be set off against other group companies' profits on fiscal integration. Losses may continue to be carried forward by the company that realized them and set off against profits subsequently made by that company within the fiscal integration group.

Transfer Pricing

When a business asset is sold to a non-resident, related party, the Luxembourg tax administration may reassess the transfer value of these assets if it is below market value and results in a shift of taxable profits to the benefit of a non-resident taxpayer linked, directly or indirectly, to the transferor. This is simple an application of common transfer pricing rules.

If transfer prices are exclusively motivated by a relationship between a Luxembourg undertaking and a non-resident taxpayer and by sound business reasons, the Luxembourg tax administration may reassess the undertaking's taxable profit (articles 56 and 164 LIR). A shift of profits outside Luxembourg between related parties, through excessive indebtedness, for instance, which implies excessive deductible expenses, may, therefore, be challenged under common transfer pricing rules.

According to article 164 LIR, a hidden profit distribution arises when a direct or indirect shareholder receives proceeds or other advantages from a company he/she would not have received in the absence of this relationship. No tax deduction is available at the company level for these expenses and the proceeds or advantages are treated as dividends subject to dividend WHT.

Dual Residency

Cases of dual residency may, in very particular cases, be beneficial for tax purposes. Tie-breaker clauses in DTTs

tend to have a direct impact for Luxembourg domestic tax purposes.

Foreign Investments of a Local Target Company

Luxembourg domestic tax law includes no controlled foreign companies (CFC) legislation.

Comparison of Asset and Share Purchases

Advantages of Asset Purchases

- The acquiring company may depreciate the purchase price of assets acquired, including goodwill.
- It is possible to acquire only part of the business.
- Losses within the acquiring group may be absorbed by a profitable business acquired from the target company.
- The buyer is in general not liable for claims on or previous liabilities of the target company.

Disadvantages of Asset Purchases

- The business is effectively being carried on by another entity. This may have required renegotiation of trading and employment contracts, etc.
- Pre-acquisition losses incurred by the target company are not transferred with the business. They remain with the target company or are lost.
- In general, there is a need to renegotiate supply, employment, and technology agreements.
- An asset purchase could be more expensive than a share purchase if, from a tax perspective, it is unattractive for the seller.
- Accounting profits may be affected by the creation and depreciation of goodwill.
- In the case of real estate, transfer registration duties are due.

Advantages of Share Purchases

- Contractual continuity, because the target company may remain active, with only shareholders changing.
- Pre-acquisition tax losses incurred by target company may be retained, despite the change of shareholder, if certain conditions are fulfilled.

- Losses incurred by the target company following an acquisition may be used by the acquiring group companies under fiscal integration provisions.
- Losses incurred by acquiring group companies within fiscal integration may be offset against profits of the target company.
- Registration duties on real estate transfer may be avoided.

Disadvantages of Share Purchases

- Participation cannot be amortized.
- There is liability for claims on or previous liabilities of the target company.
- If the participation exemption applies, direct funding costs related to the acquisition of the subsidiary may not be entirely deductible.

Withholding Tax Rate Chart

The rate information and footnotes contained in this table are from the 2009 IBFD/KPMG Global Corporate Tax Handbook.

Country	Dividends		Interest ¹	Royalties
	Individuals, Companies (%)	Qualifying Companies ² (%)		
Austria	15	5	0	0/10 ³
Belgium	15	10 ⁴	0/15 ⁵	0
Brazil	25	15 ⁶	-/15 ⁷	15/25 ⁸
Bulgaria	15	5	0/10 ⁹	5
Canada	15	0/5 ¹⁰	0/10 ¹¹	0/10 ¹²
China (People's Rep.)	10	5	0	6/10 ¹³
Czech Republic	15	5	0	0/10 ¹⁴
Denmark	15	5	0	0
Estonia	10	5	0/10 ⁹	5/10 ¹³
Finland	15	5	0	0/5 ¹⁴
France	15	5 ¹⁵	10	0
Germany	15	10	0	5
Greece	7.5	7.5	8	5/7 ¹⁴
Hong Kong	10	0 ⁶	0	3
Hungary	15	5	0	0
Iceland	15	5	0	0
Indonesia	15	10	10	12.5
Ireland	15	5	0	0
Israel	15	5 ⁶	5/10 ⁹	5
Italy	15	15	10	10
Japan	15	5	10	10
Korea (Rep.)	15	10	10	10/15 ¹⁶
Latvia	10	5	10	5/10 ¹³
Lithuania	15	5	10	5/10 ¹³
Malaysia	10	0/5 ¹⁷	10	8
Malta	15	5	0	10
Mauritius	10	5 ⁶	0	0
Mexico	15	5 ⁶	0/10 ¹¹	10
Mongolia	15	5 ⁶	0/10 ¹⁸	5
Morocco	15	10	10	10
Netherlands	15	2.5	0/2.5/15 ¹⁹	0
Norway	15	5	0	0
Poland	15	5	0/10 ¹⁸	10
Portugal	15	15	10/15 ⁹	10
Romania	15	5	10	10
Russia	10/15 ²⁰	10 ²⁰	0	0
San Marino	15	0 ⁶	0	0
Singapore	10	5 ⁶	10	10
Slovak Republic	15	5	0	0/10 ¹⁴
Slovenia	15	5	5	5
South Africa	15	5	0	0
Spain	15	5	10	10
Sweden	15	0 ⁶	0	0
Switzerland	15	0/5 ²¹	0/10 ²²	0
Thailand	15	5	10/15 ⁹	15
Trinidad and Tobago	10	5 ⁶	0/7.5/10 ²³	10
Tunisia	10	10	7.5/10 ²⁴	12
Turkey	20	5	10/15 ²⁵	10
United Kingdom	15	5	0	5
United States	15	0/5 ²⁵	0	0
Uzbekistan	15	5	0/10 ⁶	5
Vietnam	15	5/10 ²⁶	7/10 ²⁷	10

Notes

1. Many treaties provide for an exemption for certain types of interest, such as interest paid to public bodies and institutions or in relation to sales on credit. Such exemptions are not considered in this column.
2. Unless indicated otherwise, the rate in this column applies if the recipient company holds, directly or indirectly, at least 25 percent of the capital or the voting power of the paying company, as the case may be. Special conditions may apply (such as holding periods and invested amounts).
3. The higher rate applies if the Austrian company owns more than 50 percent of the capital of the Luxembourg company.
4. The rate applies if the recipient company owns at least 25 percent of the distributing company's capital or if the purchase price of the recipient company's direct holding is at least EUR 6,197,338 (LUF 250 million).
5. The zero rate applies if the recipient is an enterprise; this does not apply to interest on bonds and interest paid by a company to a company owning at least 25 percent of the paying company's voting power or shares.
6. The rate applies if the recipient company owns at least 10 percent of the distributing company's capital or voting power, as the case may be. Special conditions may apply (such as holding periods and invested amounts).
7. The domestic rate applies to interest paid by public bodies (under the treaty such interest is taxable only in the source state and there is no reduction). The zero rate applies, inter alia, to interest paid by a public body.
8. The higher rate applies to trademarks and copyrights of films, etc.
9. The lower rate applies, inter alia, to interest paid to a bank or other financial institution. Conditions may apply.
10. The 5-percent rate applies if the Canadian company owns at least 10 percent of the Luxembourg company's voting power. The zero rate applies if the Canadian company has owned directly at least 25 percent of the voting stock of the Luxembourg company for at least two years and the dividends are paid out of profits derived from the active conduct of a trade or business in Luxembourg; and if the dividends are exempt in Canada.
11. The lower rate applies, inter alia, to interest paid by a public body.
12. The lower rate applies to copyrights of literary, dramatic, musical or artistic works (excluding films, etc.), computer software, patents, and know-how.
13. The lower rate applies to equipment rentals.
14. The lower rate applies to copyrights of literary, artistic or scientific work (including films, etc.).
15. The rate only applies if the recipient company owns at least 25 percent of the distributing company's capital, or if two or more recipient companies together do so, provided that one of these owns more than 50 percent of the other(s).
16. The lower rate applies to equipment rentals and to know-how.
17. The 5-percent rate applies if the Malaysian company owns directly at least 10 percent of the capital in the Luxembourg company. The zero rate applies if it has owned directly at least 25 percent of the capital of the Luxembourg company for at least 12 months and the Luxembourg company is engaged in the active conduct of a trade or business in Luxembourg.
18. The lower rate applies to interest on bank deposits and bank loans. Conditions may apply.
19. Interest on loans secured by mortgages on immovable property is exempt. Interest on profit-sharing bonds is treated as dividends.
20. The 10-percent rate applies if the individual or corporate recipient holds directly at least 30 percent of the capital of the Luxembourg company and the price of acquisition of the holding is at least EUR 75,000.
21. The 5-percent rate applies if the Swiss company owns directly at least 25 percent of the distributing company's capital. The exemption applies if it has owned such a holding for a continuous period of two years prior to the payment.
22. The higher rate applies to interest on bonds and other similar securities and to interest on bank deposits.
23. The exemption applies, inter alia, to interest paid by a public body. The 7.5-percent rate applies to interest on bank loans, interest on bank deposits not represented by bearer instruments, and interest paid in relation to sales on credit.
24. The lower rate applies to interest on loans guaranteed or insured by the state of Tunisia or by a Tunisian-resident financial institution, provided that the loan has a term of at least five years.
25. The lower rate applies to interest paid on a loan made for a period of more than two years.
26. The 5-percent rate applies if the U.S. company owns directly at least 10 percent of the voting stock of the Luxembourg company. The zero rate applies if it has owned directly at least 25 percent of the voting stock of the Luxembourg company for at least two years and the Luxembourg company is engaged in the active conduct of a trade or business in Luxembourg.
27. The 5-percent rate applies if the Vietnamese company holds at least 50 percent of the capital of the Luxembourg company or has made a contribution of more than USD 10 million. The 10-percent rate applies if it holds at least 25 percent (but less than 50 percent) of the capital and the contribution does not exceed USD 10 million.
28. The rate is 7 percent as long as Vietnam does not levy WHT on interest.

KPMG in Luxembourg

Jean-Marie Reiser
KPMG Tax S.à.r.l.
10, rue Antoine Jans
L-1820
Luxembourg

Tel. +352 22 51 51 ext. 5590
Fax +352 46 52 27
e-Mail: jean-marie.reiser@kpmg.lu

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