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Transfer Pricing 2026

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Luxembourg: Law and Practice & Trends and Developments

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LUXEMBOURG

Law and Practice

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ATOZ Tax Advisers was founded in 2004 and is a high-end independent advisory firm based in Luxembourg, offering a comprehensive and integrated range of direct and indirect tax solutions as well as transfer pricing, corporate and aviation finance and tax litigation services to both local and international clients. ATOZ has a team of carefully selected professionals who possess extensive experience in serving the local market as well as multinational corporations. The firm's entire team works together to ensure consistently high standards of client service from beginning to end. Confirmed experts in their fields, the firm's partners share a common and rigorous approach of researching and understanding the facts before drawing conclusions. They lead each engagement with a steadfast commitment to objectivity and the highest professional, legal, regulatory and ethical standards.

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1. Rules Governing Transfer Pricing

1.1 Statutes and Regulations

Opening Comments

Luxembourg has no integrated transfer pricing legislation. Instead, according to different tax provisions and concepts applicable under Luxembourg domestic tax law, transfer pricing adjustments can be made in order to restate arm's length conditions.

Luxembourg Tax Law and Administrative Guidelines

Article 56 of the Luxembourg Income Tax Law (LITL)

Article 56 of the LITL formalises the application of the arm's length principle under Luxembourg tax law in accordance with Article 9 of the OECD Model Tax Convention and provides a legal basis for transfer pricing adjustments (upward and downward adjustments) when associated enterprises deviate from the arm's length standard.

Article 56bis of the LITL

Article 56bis of the LITL formalises the authoritative nature of the OECD Transfer Pricing Guidelines. It provides definitions of several terms that are relevant in a transfer pricing context (eg, the arm's length principle, controlled transaction, comparable uncontrolled transaction), as well as guiding principles in relation to the application of the arm's length principle that closely follow some of the key paragraphs of Chapter I (arm's length principle) of the OECD Transfer Pricing Guidelines. It clarifies that the arm's length principle has to be met whenever a Luxembourg company enters into a transaction with an affiliate. This requires calculation of the taxable income that may reasonably be expected if the parties are dealing with one another at arm's length. It does this by contrasting the choices made and the outcomes achieved by the taxpayer with those that would have resulted from market forces.

Article 56bis of the LITL explicitly addresses transactions that may not be observed between independent enterprises. It provides that the fact that a specific transaction cannot be observed between independent enterprises does not mean that a transaction does not adhere to the arm's length standard. This is a provision of great importance as related parties may, in practice, enter into transactions that are not undertaken by independent enterprises. Article 56bis of the LITL introduces the concept of comparability analysis through the replication of some of the guidance provided in the OECD Transfer Pricing Guidelines. Article 56bis of the LITL also deals with circumstances in which a transaction, as structured by a taxpayer, may be disregarded because there is a lack of valid commercial rationality, and a third party would not have entered into such a specific transaction. Nevertheless, the non-recognition of a transaction should only occur in very exceptional situations.

Circular 56/1 – 56bis/1 of the Luxembourg tax authorities (LTA) on the tax treatment of intra-group financing activities

The Circular of the LTA dated 27 December 2016 provides guidance on the practical application of the arm's length principle to intra-group financing activities. It also details some specific formal requirements applicable to financing companies when requesting an advanced pricing agreement (APA).

Concepts of hidden dividend distributions and hidden capital contributions and their interaction with Article 56 of the LITL

The concepts of hidden dividend distributions (Article 164 (3) of the LITL) and hidden capital contributions (Article 18 (1) of the LITL) also play an important role in ensuring that associated enterprises adhere to the arm's length standard.

According to Article 164 (3) of the LITL, hidden dividend distributions arise when a shareholder partner or interested party receives advantages directly or indirectly from a company that a third party would not have received. Article 164 (3) of the LITL states that such profit distributions have to be included in the company's taxable income, meaning that they are not deductible for tax purposes and may be subject to withholding tax if no exemption applies.

A hidden capital contribution refers to an advantage shifted by a shareholder to a company. While the concept is not defined in Luxembourg tax law, hidden capital contributions bear the following characteristics in accordance with the relevant case law:

- a shareholder or a related party of the shareholder;
- grants motivated by the shareholding relationship;
- an advantage to a company that may be reflected in the balance sheet – ie, either an increase in assets or a decrease in liabilities (insofar as the shareholder does not receive an arm's length compensation); and
- the contribution is not a regular contribution (pursuant to Luxembourg commercial law).

In principle, contributions increase the net equity in the receiving company's balance sheet. The object of a hidden capital contribution should therefore directly relate to balance sheet items, namely an increase in assets or a decrease in liabilities. In contrast, any advantage (including free services) shifted by the company to its shareholder(s) should be classified as a hidden dividend distribution. Consequently, the scope of hidden capital contributions and that of hidden dividend distributions do not mirror each other, though both concepts share the same objective, namely the separation of the realm of the company from its shareholders.

Article 56 of the LITL and the concepts of hidden dividend distributions and hidden capital contributions operate independently of one another and may apply concurrently. In case of an overlap, however, the concepts of hidden dividend distributions and hidden capital contributions should take precedence over Article 56 of the LITL. This is because the only tax consequence of Article 56 of the LITL is an adjustment of the taxable income of the company (in order to restate arm's length conditions), whereas the concepts of hidden dividend distributions and hidden capital contributions may require additional tax adjustments at the level of the company and the shareholder.

Transfer pricing documentation

Duty of co-operation of taxpayers

Since the introduction of Section 3 of paragraph 171 of the Luxembourg General Tax Law (LGTL), the duty of co-operation of taxpayers set out in paragraph 1 thereof has been expressly extended to transactions between associated enterprises. This means that transfer pricing documentation is identified in the Luxembourg tax law as information that taxpayers should provide to the LTA upon request in order to support the positions they take in their tax returns.

Country-by-country (CbC) reporting

The Law of 23 December 2016 implemented the provisions of Council Directive (EU) 2016/881 of 25 May 2016 into Luxembourg law, which extended administrative co-operation in tax matters to CbC reporting. Multinational enterprise (MNE) groups with a consolidated revenue exceeding EUR750 million are required to prepare a CbC report. The entity of the group in charge of the reporting is either the Luxembourg resident ultimate parent entity of the MNE group or, in certain circumstances, any other reporting entity – a Luxembourg subsidiary or a Luxembourg permanent establishment (PE) – as defined in Annex 2 of the law. The CbC report follows the OECD recommendations provided in Chapter V of the OECD Transfer Pricing Guidelines.

Article 164ter of the LITL – transfer pricing aspects of the Controlled Foreign Company (CFC) Rules

Article 164ter of the LITL, which implemented the CFC Rules of the Council Directive (EU) 2016/1164 into Luxembourg tax law with effect as from 1 January 2019, includes some transfer pricing-related aspects. This is because Luxembourg is one of the few EU member states that opted for the transactional approach when introducing the CFC rules. Article 164ter of the LITL provides that a Luxembourg corporate taxpayer or a Luxembourg PE of a non-Luxembourg tax resident entity will be taxed on the non-distributed income of an entity or PE that qualifies as a CFC, provided that the non-distributed income arises from non-genuine arrangements that have been put in place for the essential purpose of obtaining a tax advantage. An arrangement or a series thereof will be regarded as non-genuine if the entity or PE does not own the assets or has not undertaken the risks that generated all or part of its income if it were not controlled by a Luxembourg corporate taxpayer when the significant people functions, which are relevant to those assets and risks, are carried out and are instrumental in generating the CFC's income, were carried out. While no further clarification is provided on the concept of significant people functions and the interaction between the Luxembourg transfer pricing rules and the CFC Rules, in Circular 164ter/1 of 17 June

2022, the tax authorities are imposing an additional documentation requirement, not required by the law, according to which a transfer pricing analysis following the OECD Transfer Pricing Guidelines has to be performed for each of the CFCs of the taxpayer – and has to be updated on an annual basis. Based on the Circular, even though the taxpayer does not assume any people function generating the CFC's income, transfer pricing documentation needs to be available and updated on an annual basis.

Luxembourg Double Tax Treaty Network

As of early 2026, Luxembourg boasts one of the world's most robust and expansive tax treaty networks, with 92 double tax treaties currently in effect. Almost all Luxembourg double tax treaties are based on the OECD Model Tax convention and thus include the arm's length principle, as further defined in the OECD Transfer Pricing Guidelines.

OECD Transfer Pricing Guidelines

As a member of the OECD, Luxembourg adheres to the organisation's Transfer Pricing Guidelines, which reflect the consensus of OECD member countries towards the application of the arm's length principle, as provided in Article 9 (1) of the OECD Model Tax Convention. Since the Luxembourg legislation does not provide for any integrated transfer pricing legislation, the OECD Transfer Pricing Guidelines play an extremely important role for Luxembourg taxpayers with respect to analysing their transactions from a transfer pricing point of view. Reference to these guidelines is made in both parliamentary documents (such as ones related to the draft laws introducing Article 56 and Article 56bis of the LITL) and in Circular 56/1 – 56bis/1 of the LTA on the tax treatment of intra-group financing activities.

1.2 Current Regime and Recent Changes

Over the past few years, transfer pricing and the need for related documentation have become increasingly important in Luxembourg. Before 2011, Luxembourg domestic tax law did not provide any specific transfer pricing rules or documentation requirements. On 28 January 2011, the LTA issued the first circular dealing with transfer pricing, Circular 164/2, which provided guidance on how Luxembourg companies performing financing activities should determine their arm's length margin. This Circular already explicitly referred to the OECD Transfer Pricing Guidelines.

The Law of 19 December 2014 amended Article 56 of the LITL in order to formalise the application of the arm's length principle and provided a legal basis for transfer pricing adjustments when associated enterprises do not meet the arm's length standard. The same law also amended paragraph 171 of the LGTL in order to explicitly extend the duty of co-operation of taxpayers to transactions between associated enterprises, reflecting the increasing importance of transfer pricing documentation.

The Law of 23 December 2016 introduced Article 56bis of the LITL, which provided, for the first time, definitions and guiding principles in relation to the application of the arm's length principle. These definitions and guiding principles are in line with the OECD Transfer Pricing Guidelines. To reflect the changes introduced by Article 56bis of the LITL, on 27 December 2016, the LTA released a new Circular, Circular 56/1 – 56bis/1, on the tax treatment of intra-group financing activities, which provides guidance on the practical application of the arm's length principle to intra-group financing activities and repealed and replaced the former Circular of 28 January 2011 with effect from 1 January 2017.

Further changes are in the pipeline with draft law No 8186, presented to Parliament on 28 March 2023, which would introduce a new procedure for requesting an advanced bilateral or multilateral agreement on transfer pricing pursuant to the double tax treaties concluded by Luxembourg and additional transfer pricing documentation requirements (master file and local file, in line with Action 13 of the Base Erosion and Profit Shifting (BEPS) Action Plan).

2. Definition of Control/Related Parties

2.1 Application of Transfer Pricing Rules

The scope of Article 56 of the LITL is limited to transactions between associated enterprises and does not apply to transactions between individual shareholders and Luxembourg companies. Article 56 of the LITL

further applies to both cross-border transactions and transactions between Luxembourg companies.

Article 56 of the LITL defines "associated enterprise" in accordance with Article 9 (1) of the OECD Model Tax Convention, namely:

- an enterprise that participates directly or indirectly in the management, control or capital of another enterprise; or
- the same persons participate directly or indirectly in the management, control or capital of two enterprises.

Thus, Article 56 of the LITL includes a flexible definition, which is not defined further (neither in the related parliamentary documents nor in the related Circular 56/1 – 56bis/1 of the LTA).

The concepts of hidden dividend distributions and hidden capital contributions apply not only to shareholders but also to related parties of the shareholder.

"Associated enterprise" is also defined in other provisions of Luxembourg tax law, such as the CFC Rules of Article 164ter of the LITL and the Anti-Hybrid Rules of Article 168ter of the LITL – some of which include more technical control criteria of 50% or 25%.

3. Methods and Method Selection and Application

3.1 Transfer Pricing Methods

The Luxembourg transfer pricing provisions of Luxembourg tax law do not include any specific lists of transfer pricing methods that are to be applied. However, paragraph 6 of Article 56bis of the LITL defines general principles that are to be followed depending on the transfer pricing method used. The method to be used to determine the appropriate comparable price must take into account identified comparability factors and must be consistent with the precisely defined nature of the transaction. The price identified by comparing the precisely defined transaction with comparable transactions on the open market will be the arm's length price applicable to the transaction under analysis, in order to comply with the arm's length principle. The comparison method chosen must be the one that provides the best possible approximation of the arm's length price.

The parliamentary documents related to the draft law that introduced Article 56bis of the LITL state that paragraph 6 of Article 56bis of LITL implements Chapters II and III of the OECD Transfer Pricing Guidelines into Luxembourg tax legislation. Chapters II and III set out the various techniques and methods to be used, with the transaction having been analysed in accordance with the instructions in Chapter I of the OECD Transfer Pricing Guidelines, in order to determine the arm's length price. Thus, reference has to first be made to the five methods, as defined in the guidelines, which can be used to establish whether a controlled transaction adheres to the arm's length standard. These are divided into two groups, namely the traditional transaction methods and the transactional profit methods. However, in addition to these five methods, as stated in the commentary to the draft law introducing Article 56bis of the LITL, the OECD Transfer Pricing Guidelines also allow any other method to be applied, as long as it enables a price to be set that satisfies the arm's length principle. In such case, the taxpayer will have to evidence why this other method is the most appropriate method.

3.2 Unspecified Methods

As a principle, the most appropriate method has to be applied, namely either one of the methods defined in the OECD Transfer Pricing Guidelines or any other method that enables a price to be established that is in line with the arm's length principle.

3.3 Hierarchy of Methods

Since the Luxembourg legislation only refers to the OECD Transfer Pricing Guidelines without specifying the different methods, the only principle that should be followed is that the most appropriate method should be applied, meaning there is no hierarchy of methods. In practice, the most commonly used method is the comparable uncontrolled price (CUP) method, mainly for a wide range of financial transactions and licence fees. However, other methods such as the cost-plus method (for low value-adding services) and the profit split method (eg, for highly integrated fund manage-

ment activities) are regularly relevant in practice as well.

3.4 Ranges and Statistical Measures

The Luxembourg legislation does not require the use of ranges or statistical measures. However, since the LTA follow the OECD Transfer Pricing Guidelines, reference has to be made to these in this respect.

3.5 Comparability Adjustments

Based on paragraph 4 of Article 56bis of the LITL, transactions are sufficiently comparable when there are no material differences between the transactions being compared that could have a significant methodological influence on the determination of the price, or when reasonably reliable adjustments can be made to eliminate the impact on price determination. Thus, comparability adjustments have to be reliable and reasonable, and may be performed ("in accordance with internationally recognised standards", as Circular 56/1 – 56bis/1 states) if they are necessary to improve the reliability and quality of the comparability analysis.

4. Intangibles

4.1 Notable Rules

Luxembourg tax legislation does not include any specific rules relating to the transfer pricing of intangibles. Thus, reference has to be made to Chapter VI of the OECD Transfer Pricing Guidelines in this respect. However, Circular 50ter/1 of 28 June 2019 dealing with the Luxembourg intellectual property (IP) regime (ie, 80% corporate income tax and municipal tax exemption of the net qualifying income and capital gains derived from eligible IP assets and 100% exemption of qualifying IP assets for net wealth tax purposes) specifies that the arm's length principle defined in Article 56 and Article 56bis of the LITL applies in case of application of the IP regime.

4.2 Hard-to-Value Intangibles

Luxembourg tax legislation does not include any specific rules relating to hard-to-value intangibles (HTVI), so the OECD Transfer Pricing Guidelines have to be followed in this respect. Based on the Luxembourg questionnaire on the Implementation of the HTVI Approach included in the Luxembourg country profile released by the OECD, even though the HTVI approach defined in Chapter VI is to be considered as not implemented in domestic legislation, the general provisions of Chapters I–III can be used for audit purposes with regard to transactions involving intangibles.

Attention should be paid to the fact that arrangements involving the transfer of HTVI between associated enterprises belong to the transfer pricing arrangements, which may have to be reported under the Luxembourg Law of 25 March 2020 implementing Council Directive (EU) 2018/822 (DAC6), as amended, regarding reportable cross-border arrangements. HTVI are defined in Part 2 of the Annex to the Law of 25 March 2020, which deals with the "hallmarks" (ie, characteristics or features of a cross-border arrangement that indicate a potential risk of tax avoidance) as follows: "Intangibles or rights in intangibles for which, at the time of their transfer between associated enterprises, (a) no reliable comparables exist and (b) at the time the transaction was entered into, the projections of future cash flows or income expected to be derived from the transferred intangible, or the assumptions used in valuing the intangible, are highly uncertain, making it difficult to predict the level of ultimate success of the intangible at the time of the transfer".

4.3 Cost Sharing/Cost Contribution Arrangements

Luxembourg tax legislation does not include any specific rules relating to cost sharing or cost contribution arrangements. Therefore, the guidance included in the OECD Transfer Pricing Guidelines in this respect (ie, Chapter VIII) has to be followed.

5. Adjustments

5.1 Upward Transfer Pricing Adjustments

While both upward and downward adjustments may be made in application of the arm's length principle, according to the LGTL, amended tax returns may only be filed (or may even have to be filed) by taxpayers under certain limited conditions and circumstances.

As long as no tax assessment has been released, the taxpayer has the possibility to file an amended tax

return reflecting the adjustment, regardless of whether the adjustment is positive for the taxpayer or not. Based on paragraph 85 of the LGTL, the tax authorities will have to assess the taxpayer based on the newly filed tax return.

- Once a tax assessment has been released, based on paragraph 94 of LGTL, at the taxpayer's request, the tax office may amend the tax assessment, but only to the extent that the deadline for challenging this tax assessment (ie, three months by means of a so-called *réclamation*) has not elapsed.
- Once the three month-deadline for challenging the tax assessment has elapsed, the tax authorities have no obligation to take the amended tax return into consideration, even if it includes a correct adjustment – ie, even in case the initial tax assessment (which did not take this adjustment into consideration) was wrong.
- Lastly, every time a tax assessment is issued based on an inaccurate tax return where the mistake/s made in the tax return lowered the tax due by the taxpayer, there is an obligation for the taxpayer to file an amended tax return reflecting the adjustment. This obligation remains as long as the statute of limitations of five years has not elapsed.

5.2 Secondary Transfer Pricing Adjustments

Luxembourg's domestic tax law does not include explicit provisions regarding secondary transfer pricing adjustments, such as deemed dividends and constructive loans. However, such adjustments may arise indirectly through other tax provisions, particularly in the context of hidden dividend distributions, hidden capital contributions and interest-free loans (IFLs). For more information, please refer to **1.1 Statutes and Regulations** and **14.2 Significant Court Rulings**.

In a cross-border context, tax treaties concluded by Luxembourg generally include a provision drafted along the lines of Article 9 of the OECD Model Tax Convention. This allows for primary adjustments in the case of non-arm's length conditions and requires secondary adjustments to consider arm's length conditions. Should the tax administrations of the contracting states not be able to agree on an arm's length pricing, taxpayers may set in motion a mutual agreement procedure (MAP). Please refer to **7. Advance Pricing Agreements (APAs)** and **16. Transparency and Confidentiality** for more information.

6. Cross-Border Information Sharing

6.1 Sharing Taxpayer Information

There are a multitude of legal instruments for exchanging information on Luxembourg taxpayers with foreign tax authorities. The exchange can take place upon request, automatically or spontaneously.

Exchange of Information Upon Request

As far as exchange of information upon request is concerned, it can mainly take place either on the grounds of the double tax treaty (Luxembourg has an extensive tax treaty network, and almost all tax treaties include a provision on exchange of information in line with Article 26 of the OECD Model Tax Convention) concluded by Luxembourg with the jurisdiction of the foreign requesting authority, or based on Council Directive 2011/16/EU of 15 February 2011 on administrative co-operation in the field of taxation (DAC) if the exchange is requested by an authority of another EU member state. The procedure for exchanging information on request in these cases, as well as under the Law of 26 May 2014 approving the Convention on Mutual Administrative Assistance in Tax Matters, is governed by the Law of 25 November 2014. To avoid so-called "fishing expeditions", only "foreseeably relevant" information can be exchanged. In 2023, the Luxembourg authorities received 911 requests from other jurisdictions, compared to 1189 requests in 2021 and 1038 requests in 2022. Thus, the number of requests has been decreasing since 2021, which is probably due to the fact that foreign authorities are already receiving an ever-increasing amount of information automatically.

Automatic Exchange of Information

The scope of information to be exchanged on a mandatory and automatic basis has been increasing consistently over the past few years through several amendments to the DAC that have been implemented into Luxembourg law.

The most important scope extensions for transfer pricing purposes are as follows.

- Advance pricing agreements (APAs): Council Directive (EU) 2015/2376 (DAC3), implemented by the Law of 23 July 2016, which extended the automatic exchange to tax rulings and APAs.
- CbC reporting: Council Directive (EU) 2016/881 (DAC4), implemented by the Law of 23 December 2016, which extended the automatic exchange to CbC reports.
- Cross-border arrangements: DAC6, implemented by the Law of 25 March 2020, which introduced mandatory disclosure rules for intermediaries on certain reportable cross-border arrangements. The following cross-border transfer pricing arrangements are covered:
  (a) arrangements that involve the use of unilateral safe harbour rules (Hallmark E1);
  (b) arrangements involving the transfer of HTVI (Hallmark E2); and
  (c) arrangements involving intra-group cross-border transfers of functions and/or risks and/or assets, if the projected annual earnings before interest and taxes (EBIT) during the three-year period after the transfer of the transferor(s) are less than 50% of the projected annual EBIT of such transferor(s) if the transfer had not taken place.

Spontaneous Exchange of Information

The LTA may also exchange information spontaneously with other jurisdictions based on the DAC (in an EU context) or based on the Convention on Mutual Administrative Assistance in Tax Matters (which 152 jurisdictions have signed as of April 2026). Information can only be exchanged if the LTA have grounds for supposing that there may be a loss of tax in the other jurisdiction.

Circular 56/1 – 56bis/1 of the LTA on the tax treatment of intra-group financing activities states that companies that opted for the simplification measure that may apply to Luxembourg companies acting as mere intermediaries will be subject to spontaneous exchanges of information.

6.2 Joint Audits

While transfer pricing joint audits are not yet widespread in Luxembourg, the country participates in EU and OECD initiatives that promote them, as follows.

EU Joint Audit Initiatives

Under the EU Joint Audit Framework, Luxembourg can engage in joint audits with other EU member states as part of the Fiscalis 2020 and Fiscalis 2027 programmes.

The Directive on Administrative Cooperation (DAC 7) enhances tax transparency and co-operation among EU tax authorities, facilitating more joint audits.

OECD and BEPS Initiatives

Luxembourg adheres to the OECD BEPS Action 13, which promotes international tax co-operation and joint audits.

The OECD's Forum on Tax Administration (FTA) encourages the use of joint audits to improve tax compliance in cross-border transfer pricing cases. In addition, Luxembourg has an extensive tax treaty network with more than 80 jurisdictions, which includes MAP provisions that allow for joint tax examinations.

Luxembourg is also part of the Joint International Taskforce on Shared Intelligence and Collaboration (JITSIC), which enables global tax authorities to co-ordinate on high-risk tax issues, including transfer pricing.

6.3 Simultaneous Controls

Luxembourg co-operates in simultaneous controls at both EU and international levels under the DAC, as implemented into domestic law, as well as under applicable bilateral and multilateral tax treaties. While Luxembourg does not currently operate a formal enhanced or co-operative compliance programme, its tax authorities increasingly participate in co-ordinated and – where appropriate – joint or simultaneous audits under EU and OECD frameworks. During such audits, communication is typically ensured through designated contact points and central co-ordination between the competent authorities, with information exchanged on an ongoing basis.

6.4 International Compliance Assessment Programme (ICAP)

Luxembourg participates in the OECD ICAP on a voluntary basis through its competent authority. While there is no separate domestic multilateral risk assessment programme, the Luxembourg tax administration may engage in ICAP cases alongside other participating jurisdictions, allowing for a co-ordinated, upfront risk assessment of transfer pricing and PE issues. Participation remains discretionary and case-specific, depending on the profile of the taxpayer and the agreement of the relevant tax authorities. In addition, Luxembourg is also participating in the European Trust and Cooperation Approach (ETACA) Pilot 2, a multilateral transfer pricing risk assessment initiative led by the European Commission, further demonstrating its commitment to co-operative compliance and transparency in international taxation.

7. Advance Pricing Agreements (APAs)

7.1 Programmes Allowing for Rulings Regarding Transfer Pricing

Unilateral APAs

With effect as from 2015, Luxembourg has formalised its procedure applicable to tax rulings, including those related to transfer pricing (unilateral APAs). This procedure is included in paragraph 29a of the LGTL, as well as in Grand Ducal Regulation of 23 December 2014. On top of the requirements applicable under the procedure of paragraph 29a, Luxembourg companies performing intra-group financing activities have to provide the additional information listed in Circular 56/1 – 56bis/1 of the LTA, dated 27 December 2016.

Bilateral or Multilateral APAs

Based on the legal provisions currently in force, no formal programme has been implemented by Luxembourg for bilateral and multilateral APAs, and Luxembourg considers that these can be concluded by its competent authority based on the first sentence of Article 25 (3) of the OECD Model Tax Convention. Circular L.G. - Conv. D.I. No 601 of the LTA, dated 11 March 2021, provides guidance in this respect.

Draft Law No 8186 introduces a new procedure (new paragraph 29c of the LGTL and related Grand-Ducal Regulation) for requesting an advanced bilateral or multilateral agreement on transfer pricing pursuant to the double tax treaties concluded by Luxembourg. However, it is uncertain at this stage whether this draft law will ever become law since the draft provision on bilateral and multilateral APAs belongs to a broader piece of draft legislation that has been giving rise to discussions and criticism of the legislative process in many respects.

Still, Luxembourg taxpayers are able to request bilateral or multilateral agreements in transfer pricing based on the EU Arbitration Convention and the Law of 20 December 2019 implementing Council Directive (EU) 2017/1852 of 10 October 2017 on tax dispute resolution mechanisms in the EU, or based on a double tax treaty.

7.2 Administration of Programmes

APA requests have to be sent to the head of the tax office in charge of the taxpayer. However, if the APA request deals with company taxation issues, the request will first be submitted for opinion to the advance tax clearance commission (*Commission des décisions anticipées*).

Based on Circular L.G. - Conv. D.I. No 601 of the LTA, dated 11 March 2021, transfer pricing MAP requests have to be sent to the economic division of the LTA (which is the authority in charge of transfer pricing cases) or to the *Comité de Direction* of the LTA, which is in charge of all MAP cases.

7.3 Co-Ordination Between the APA Process and Mutual Agreement Procedures

While there is no provision dealing with this question, in practice, there should be co-ordination between the APA process and the MAP, even though the competent authorities administrating the two are not the same. Co-ordination between the MAP procedure and other procedures (such as a legal procedure before the administrative courts) is also covered in Circular L.G. - Conv. D.I. No 601 of the LTA, dated 11 March 2021.

7.4 Limits on Taxpayers/Transactions Eligible for an APA

An APA can be requested by any type of taxpayer and can deal with any type of transaction.

7.5 APA Application Deadlines

Unilateral APA requests have to be filed before the transaction takes place. As far as bilateral and multilateral APAs are concerned, they generally have to be requested within three years starting from the first notification of the action resulting in:

- taxation not in accordance with the provisions of the covered tax agreement;
- the question in dispute; or
- double taxation, depending on whether the request is made during a MAP initiated based on a double tax treaty, the law implementing the EU Directive on tax dispute resolution mechanisms in the EU or the EU Arbitration Convention.

7.6 APA User Fees

In the same way as any other advance tax clearance dealing with company taxation issues, unilateral APAs are subject to a fee that is determined by the LTA upon receipt of the request. The fee ranges between EUR3,000 and EUR10,000, depending on the complexity and the amount of work required. In practice, in transfer pricing matters, the fee very often reaches EUR10,000. The fee is payable within one month.

Based on the legislation in force, no fee applies to bilateral or multilateral APAs. However, should draft law No 8186 (introducing a new procedure for requesting an advanced bilateral or multilateral agreement on transfer pricing pursuant to the double tax treaties) become law in its current form, a fee ranging between EUR10,000 and EUR20,000 (depending on the level of complexity and the amount of work required) would apply.

7.7 Duration of APA Cover

The APA is valid for a maximum five tax years and has a binding effect on the tax authorities, except when:

- the situation or operations described are not accurate;
- the situation or operations performed differ from those described in the APA request; or
- it appears that the APA is not, or is no longer, in line with Luxembourg, EU or international tax law.

7.8 Retroactive Effect for APAs

Given that unilateral APA requests have to be filed before the transaction they relate to takes place, in principle, there is no possible retroactive effect.

8. Penalties and Documentation

8.1 Transfer Pricing Penalties and Defences

Luxembourg legislation does not provide for penalties that are transfer-pricing-specific or linked to the preparation and maintenance of transfer pricing documentation. If a transaction has been priced in such a way that it does not reflect the arm's length principle, the tax authorities will perform an adjustment based on Article 56 of the LITL.

However, penalties might apply in the context of mandatory reporting requirements, which include transfer pricing data, such as under the CbC reporting requirements, where the LTA may levy, on a discretionary basis, a fine of up to EUR250,000 in cases of non-filing, late filing or incomplete or incorrect filing of the CbC report – as well as in cases of non-compliance with the filing rules. The same level of penalties also applies in case of breach of the reporting requirements under the law implementing DAC6, which also covers transactions that are transfer pricing-related.

As far as transfer pricing documentation is concerned, based on paragraph 171 of the LGTL, it only has to be provided to the tax authorities upon request, and there is no general obligation to prepare such documentation. However, given that taxpayers have to be in the position to justify the positions they take in their tax returns, including when they enter into transactions with related parties, they have to be in a position to present, upon request, documentation illustrating how the arm's length price of these transactions was determined. Therefore, from a practical point of view, even if it is not required by the law, taxpayers should prepare their transfer pricing documentation upfront.

Lastly, the general administrative penalties that apply in any other tax matters – ie, in the case of late filing of a tax return, late payment of the tax due or fraud – might also apply.

8.2 Transfer Pricing Documentation

Luxembourg tax law does not explicitly provide for transfer pricing documentation requirements. However, this does not mean that Luxembourg taxpayers are not required to demonstrate the arm's length nature of their controlled transactions through robust transfer pricing documentation.

Instead, the pressure to prepare transfer pricing documentation for Luxembourg tax purposes may come from several directions, such as the magnitude of the intra-group transaction and the associated tax risks, the rules on the burden of proof and the ability of the LTAs to challenge the transfer pricing.

Whenever the LTAs can reasonably evidence that the transfer pricing of an intra-group transaction is not in line with the arm's length principle, it is up to the taxpayer to disprove this rebuttable presumption. Similarly, if a taxpayer wishes to claim a downward adjustment or a hidden capital contribution, it is for the taxpayer to prove the amount of the deduction or contribution.

In particular, where Luxembourg companies carry out financing activities that fall within the scope of the Luxembourg Circular on transfer pricing aspects of financing activities (Circular 56/1 – 56bis/1 of 27 December 2016), the LTAs expect the taxpayer to substantiate the arm's length margin in a transfer pricing study.

Moreover, there is a requirement to file CbC reports, based on the Law of 23 December 2016 implementing Council Directive (EU) 2016/881 of 25 May 2016. This obligation applies to MNE groups with a consolidated revenue exceeding EUR750 million, whereby the entity of the group in charge of the reporting is generally the ultimate parent entity of the group. Luxembourg entities that are members of an MNE group are also required to notify the LTA of the identity and tax residence of the reporting entity (whether this reporting entity is the Luxembourg entity itself or any other entity of the group).

However, there is no requirement to prepare a master file or a local file, as defined in Action 13 of the BEPS Action Plan and Chapter V of the OECD Transfer Pricing Guidelines.

In 2023, a draft Grand-Ducal Regulation was released that closely resembles the three-tier documentation standard defined in the OECD Transfer Pricing Guidelines. However, it remains to be seen whether this regulation will ultimately be adopted. Multinationals can already rely on the guidance in Chapter V of the OECD Transfer Pricing Guidelines if they prefer the master file/local file format to preparing separate transfer pricing reports for different intra-group transactions.

9. Alignment With OECD Guidelines

9.1 Alignment and Differences

Since Luxembourg legislation does not provide for any integrated transfer pricing legislation, the OECD Transfer Pricing Guidelines play an extremely important role for Luxembourg taxpayers when analysing their transactions from a transfer pricing point of view, and for tax authorities in assessing the transfer pricing policy of taxpayers. Reference to these guidelines is made in the parliamentary documents related to the Luxembourg transfer pricing legislation, as well as in the related guidance of the LTA. Therefore, the position of the LTA should be fully aligned with the OECD guidelines, and taxpayers should use these guidelines as a reference.

9.2 Arm's Length Principle

Luxembourg tax law follows the arm's length principle.

9.3 Impact of the Base Erosion and Profit Shifting (BEPS) Project

The development of the Luxembourg transfer pricing legislation from 2015 is a direct effect of the outcome of the BEPS project in respect of transfer pricing matters. As such, the BEPS project has impacted Luxembourg legislation significantly. The wording of Article 56bis of the LITL closely follows some of the key paragraphs of Chapter I (arm's length principle)

of the OECD Transfer Pricing Guidelines, which were updated in order to reflect the outcome of Actions 8–10 of the BEPS Action Plan.

9.4 Impact of BEPS 2.0

Luxembourg has implemented the EU Pillar Two Directive by means of the Law of 22 December 2023, so the Pillar Two rules of the Directive are now in force in Luxembourg. As far as Pillar One is concerned, its impact will mainly depend on the scope of exclusions for the financial services industry.

9.5 Pillar One Amount B

The OECD/G20 Inclusive Framework has finalised and published the consolidated Amount B guidance and incorporated it into the OECD Transfer Pricing Guidelines – this framework remains optional for jurisdictions to adopt from fiscal years beginning on or after 1 January 2025. Luxembourg has not implemented Pillar One Amount B in its domestic legislation, nor introduced specific rules to apply it. Consistent with many EU peers, Luxembourg may forgo adoption in the near term.

9.6 Entities Bearing the Risk of Another Entity's Operations

A Luxembourg entity may bear the risk of another entity's operations to the extent that the transaction is concluded under arm's length conditions, providing the risk-bearing entity with an arm's length remuneration. Explicit guarantees in financial transactions have to be remunerated in line with Chapter X of the OECD Transfer Pricing Guidelines.

9.7 Allocation of Profits to Permanent Establishments (PEs)

In Luxembourg, the allocation of profits to PEs is governed by the arm's length principle as defined in Articles 56/56bis of the LITL. These provisions treat a PE as a "functionally separate entity" requiring an analysis of the functions performed, assets used and risks assumed by the PE as if it were an independent enterprise. Luxembourg's framework is closely aligned with the Authorised OECD Approach (AOA). For tax treaties following the 2010 OECD Model (or later), Luxembourg recognises internal "dealings" (such as internal services or capital allocation) between the head office and the PE. For older treaties, the approach remains grounded in the arm's length principle but may be more restrictive regarding certain internal charges. Finally, there are no specific safe harbour rules in the LITL for PE profit allocation.

10. Relevance of the United Nations Practical Manual on Transfer Pricing

10.1 Impact of UN Practical Manual on Transfer Pricing

While the UN Practical Manual on Transfer Pricing may be used as a source of information (reference is even made to it in the commentary to Draft Law No 6722 introducing Article 56 of the LITL), in practice, it is not relevant since Luxembourg closely follows the OECD Transfer Pricing Guidelines.

11. Safe Harbours or Other Unique Rules

11.1 Transfer Pricing Safe Harbours

Luxembourg tax law does not include any transfer pricing-related safe harbours. However, as far as Luxembourg companies performing intra-group financing activities are concerned, Circular 56/1 – 56bis/1 provides for the following simplification measure for Luxembourg companies acting as mere intermediaries – ie, on-lending funds received without bearing any significant (credit) risks: transactions entered into by these companies are deemed to comply with the arm's length principle if the analysed entity realises a minimum return of 2% after tax on the amount of the financing volume. In practice, this simplification measure is rarely applied as the 2% after-tax margin is significantly higher than the arm's length remuneration for such activity that can be determined and applied on a case-by-case basis.

Attention should be paid to the fact that arrangements involving the use of unilateral safe harbour rules belong to the specific arrangements concerning transfer pricing, which may have to be reported under the Luxembourg Law of 25 March 2020 implementing DAC6 regarding reportable cross-border arrangements. However, given that Circular 56/1 – 56bis/1 of the LTA on the tax treatment of intra-group financing

activities states that companies opting for the simplification measure that may apply to Luxembourg companies acting as mere intermediaries will already be subject to spontaneous exchanges of information, reporting under DAC6 in this specific situation would mean that the information would be exchanged twice (once under the spontaneous information exchange and once under the automatic exchange of DAC6).

11.2 Rules on Savings Arising From Operating in the Jurisdiction

Luxembourg does not have any specific rules governing savings that arise from operating in Luxembourg.

11.3 Unique Transfer Pricing Rules or Practices

Luxembourg does not have any notable unique rules or practices applicable in the transfer pricing context.

11.4 Financial Transactions

Luxembourg has issued specific local guidance on financial transactions, as outlined in Circular 56/1 – 56bis/1 of the LTA (see **1.1 Statutes and Regulations**). This Circular provides detailed instructions on the transfer pricing treatment of intra-group financing activities. According to the Circular, a financing entity should possess the capacity to assume risks related to its financial intermediation activities, exercise control over risks (including credit risk management) and maintain sufficient equity levels to absorb potential losses.

From a wider perspective, Luxembourg generally adheres to the OECD Transfer Pricing Guidelines, particularly Chapter X, which emphasises the accurate delineation of financial transactions and the assessment of risk control functions.

12. Co-Ordination With Customs Valuation

12.1 Co-Ordination Requirements Between Transfer Pricing and Customs Valuation

While there is no specific provision in Luxembourg law in respect of the arm's length value for customs duty purposes, Article 70-3 (d) of the Union Customs Code applies the arm's length principle in order to determine the customs value, stating that the transaction value shall apply provided that "the buyer and seller are not related or the relationship did not influence the price".

The Law of 19 December 2008 provides a legal framework for the exchange of information between the different LTA – ie, the direct tax authorities (*Administration des contribution Directes*), the indirect tax authorities (*Administration de l'Enregistrement, des Domaines et de la TVA*) and the customs and excise duties administration (*Administration des Douanes et Accises*) – as well as with other public authorities such as the supervisory authority of the financial sector (*Commission de Surveillance du Secteur Financier*). However, in practice, to date, the use of transfer pricing documentation for customs duty purposes is uncommon.

13. Controversy Process

13.1 Options and Requirements in Transfer Pricing Controversies

There is no dedicated procedure applicable to transfer pricing matters, meaning that the same procedure as for any other direct tax matters applies when it comes to transfer pricing audits or to legal proceedings.

In a first step, the tax authorities may consider performing a tax audit that can take the form of either a general information request or a more formal tax audit, involving several steps. In practice, an increasing number of tax audits (in the form of a general information request) are being performed, especially when it comes to intra-group financing transactions. The tax audit is performed by the local inspector in charge of the taxpayer. Besides the statute of limitations (of five years in principle), there is no timeline for performing a tax audit, and the tax authorities set the deadline for the taxpayer to provide the information requested (generally two to four weeks). The taxpayer has the obligation to provide the information requested and must answer any additional questions the tax authorities may ask during the audit process. In practice, the tax authorities request the transfer pricing documentation supporting the intra-group transactions performed by the taxpayer as well as the related agree-

ments. They often also request information related to substance.

Once the audit is completed, the tax authorities will release a tax assessment (or a revised tax assessment if the taxpayer has already been taxed automatically based on its initial tax return, as is the case for companies in principle). If the tax assessment differs from the position taken in the tax return, the tax authorities will first have to send a notification to the taxpayer explaining that they will deviate from the position taken in the tax returns and briefly explain the rationale behind this deviation. The taxpayer is able to take a position on the envisaged deviation. Then, the tax assessment is released. The taxpayer then has three months to challenge the tax assessment before the director of the direct tax authorities.

Even if the tax assessment is challenged, the tax fixed in the tax assessment must be paid. The director can then issue a new tax assessment, reject the claim of the taxpayer or even remain silent. If the director remains silent, the appeal is deemed to be rejected after six months. As soon as the appeal is rejected or deemed to be rejected, the taxpayer has the possibility to appeal against the decision (or the initial tax assessment itself in case of deemed decision) of the director of the tax authorities before the Administrative Tribunal (first instance in direct tax matters). The taxpayer can appeal against the decision of the Tribunal before the Administrative Court (second instance in direct tax matters) within 40 days following the notification of the decision. The decision of the Administrative Court is final and cannot be appealed, as the Administrative Court is the highest instance in direct tax matters.

Draft Law No 8186 aims to simplify and modernise the rules governing the direct tax procedure in Luxembourg and amends, among other things, some aspects of the formal conditions to challenge tax assessments.

14. Judicial Precedent

14.1 Judicial Precedent on Transfer Pricing

Luxembourg does not recognise the rule of precedent so the Luxembourg courts are not bound by decisions handed down in other cases, even when these cases are very similar. Still, decisions of the director of the tax authorities very often make reference to the case law of the administrative courts, which is generally followed by the tax authorities.

14.2 Significant Court Rulings

Besides the rulings of the administrative courts regarding hidden dividend distributions and hidden capital contributions, which are very numerous, the Luxembourg case law in transfer pricing matters is rather limited. There is some case law on the computation of interest rates for financing activities, but its relevance is limited since these rulings concern tax years prior to 2015 (before Luxembourg introduced its transfer pricing legislation). There is, however, some recent case law on intra-group financing transactions and the qualification (as debt versus equity) of related instruments – including, in particular, the following case law regarding the qualification of IFLs.

Administrative Court, Case No 50602C, 17 April 2025 – IFL

On 17 April 2025, the Luxembourg Administrative Court (Case No 50602C) ruled on the tax treatment of IFLs and the status of a foreign PE. The case concerned a Luxembourg company that financed the acquisition of two foreign participations held via a Malaysian PE through two IFLs granted by an indirect shareholder. As the Malaysian PE has been disregarded (the company could not evidence a real presence in Malaysia), the participations and loans have been allocated for Luxembourg tax purposes to the Luxembourg company. The company had treated the loans as debt for tax and accounting purposes, including recognising imputed interest deductions. The LTA challenged this treatment, arguing that the loans lacked the essential characteristics of debt, such as a fixed repayment schedule and genuine economic risk transfer, and should be reclassified as equity contributions.

In their decisions, the tribunal and the court applied the substance-over-form principle and appear to have

applied the concept of disguised capital when classifying the loans for Luxembourg tax purposes. However, both the tribunal and the court appear to have confused the classification of financial instruments with the application of the concepts of hidden capital contributions and disguised capital. Notably, under the disguised capital concept, financing instruments can only be reclassified as equity if they are first classified as debt for Luxembourg tax purposes. While the courts relied on some commentaries from 1955, the financial world is much more sophisticated today than in the past, and the Luxembourg legislator did not address the long-standing administrative practice of debt funding for holding activities. Therefore, one could argue that the legislator has implicitly shifted towards a stricter interpretation of the concept of disguised capital.

While the Luxembourg courts held that the financing instruments can only be reclassified in their entirety, according to the interpretation of the concept of disguised capital by the German Reich Tax Court and the German Federal Tax Court (which developed this concept), only the excessive part of the financing instrument should be reclassified (rather than the entire instrument). In this case, a debt capacity analysis could be conducted to support the level of debt funding. For interest-free debt instruments in which no interest is charged, the analysis is expected to result in a very high debt capacity percentage that exceeds the 85:15 debt-to-equity ratio that applies to holding activities based on administrative practice.

Administrative Court, Case No 48125C, 23 November 2023 and Administrative Tribunal No 44902, 23 September 2022 – IFL

On 23 November 2023, the Luxembourg Administrative Court held a decision in a case concerning an IFL that was granted by a Luxembourg company to its wholly owned Luxembourg subsidiary. The case involved a company resident in the Cayman Islands (CayCo) that invested via a Luxembourg investment platform into (distressed) debt owed by third parties. CayCo financed its Luxembourg subsidiary (LuxParentCo) by a mixture of equity and a profit-participating loan (PPL). LuxParentCo used the funds received to finance its Luxembourg subsidiary (LuxSubsidiary; the taxpayer) by a mixture of equity and (mainly) an IFL. LuxSubsidiary (the borrower) invested the funds received from LuxParentCo (the lender) mainly into distressed debt instruments.

In its corporate tax return, in accordance with Article 56 of the LITL, LuxSubsidiary performed a downward adjustment in relation to the IFL in order to account for deemed interest expenses that would have been due at arm's length. LuxParentCo recognised deemed interest income in its corporate tax return (corresponding to the amount of the deemed interest expenses reflected in the corporate tax return of LuxSubsidiary). The upward adjustment was also performed in accordance with Article 56 of the LITL.

Both the LTA and the Administrative Tribunal denied the downward adjustment on the grounds that the IFL was to be considered as an equity instrument. The equity qualification by the tax authorities and the Tribunal was mainly based on the fact that the IFL included a limited-recourse clause providing for no or limited risk in case of default. One additional element was that the loan was only formalised several months after the cash had been made available. Thus, according to the Administrative Tribunal, the intention of the parties was to make a hidden capital contribution.

The Administrative Court overturned the judgment of the Tribunal and recalled that the classification of a financing instrument follows the economic approach (so-called *wirtschaftliche Betrachtungsweise*). This approach involves, for tax purposes, the economic reality prevailing over the legal form (also referred to as the "substance over form" principle). The Administrative Court performed an overall analysis of the transaction and an analysis of all relevant features of the IFL. Since most of the relevant features of the IFL were debt features, the Administrative Court classified the loan as a debt instrument. As the subject matter of the case was the classification of the IFL as debt or equity, and the Administrative Court is limited by the grounds on which it has been involved, it could not itself review the downward (and upward) adjustment in principle (ie, notional interest) and the arm's length nature of the notional interest rate declared by the borrower. However, the Administrative Court stated that it was wrong to recharacterise the IFL as equity and to refuse to admit the amount put forward

as notional interest. Hence, the Administrative Court re-established long-standing principles with respect to the classification of financial instruments as debt or equity (ie, economic approach, substance over form).

15. Foreign Payment Restrictions

15.1 Restrictions on Outbound Payments Relating to Uncontrolled Transactions

The Luxembourg legislation does not include any restrictions on payments relating to uncontrolled transactions. There are only restrictions on the tax deduction of payments, which, in certain cases, like in the case of the interest limitation rules of the EU Anti-Tax Avoidance Directive (ATAD), also apply to payments to third parties.

15.2 Restrictions on Outbound Payments Relating to Controlled Transactions

Luxembourg legislation does not preclude the possibility of making payments relating to controlled transactions. However, certain limitations exist on the possibility of deducting such payments from a tax point of view. This is the case, for example, for interest and royalty payments made to entities located in a jurisdiction considered as noncooperative, based on a list released and updated twice a year by the EU Council. Restrictions may also apply when the Anti-Hybrid Rules of the ATAD, as implemented into Luxembourg law, apply. Lastly, restrictions will apply to the part of the remuneration that exceeds the arm's length price, or when a payment is requalified into a hidden distribution. In such case, withholding tax might also apply on the payment.

15.3 Effects of Other Countries' Legal Restrictions

In Luxembourg, there are no specific rules regarding the effects of other countries' legal restrictions.

16. Transparency and Confidentiality

16.1 Publication of Information on APAs or Transfer Pricing Audit Outcomes

According to the Grand-Ducal Regulation of 23 December 2014 (related to paragraph 29a of the LGTL), advance tax agreements, including those covering transfer pricing aspects – ie, unilateral APAs – are published in a summarised and anonymised form in the annual report of the direct tax authorities. However, in practice, the information published only includes the number of decisions taken on APA requests and whether each decision was positive or negative. Luxembourg taxpayers usually do not rely on the APA procedure but rather on the preparation of robust transfer pricing documentation supporting the positions they take in their tax returns. The very low number of APAs (a single APA in 2023 based on the 2023 annual report of the direct tax authorities) illustrates this quite well.

As far as bilateral MAPs are concerned, the annual report of the direct tax authorities also indicates the number of MAPs launched and closed during the year, including those related to transfer pricing. However, no information is included on the content, outcome, etc. Lastly, in line with its commitment under Action 14 of the BEPS Action Plan ("Making Dispute Resolution Mechanisms More Effective"), Luxembourg provides data and statistics to the OECD on its MAP procedure on a regular basis, including on bilateral APAs. This information is then analysed and published in the form of a peer review report by the OECD.

16.2 Use of "Secret Comparables"

Luxembourg does not use "secret comparables" for transfer pricing assessment purposes.

Trends and Developments

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ATOZ Tax Advisers was founded in 2004 and is a high-end independent advisory firm based in Luxembourg, offering a comprehensive and integrated range of direct and indirect tax solutions as well as transfer pricing, corporate and aviation finance and tax litigation services to both local and international clients. ATOZ has a team of carefully selected professionals who possess extensive experience in serving the local market as well as multinational corporations. The firm's entire team works together to ensure consistently high standards of client service from beginning to end. Confirmed experts in their fields, the firm's partners share a common and rigorous approach of researching and understanding the facts before drawing conclusions. They lead each engagement with a steadfast commitment to objectivity and the highest professional, legal, regulatory and ethical standards.

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Introduction

Transfer pricing is a key issue in Luxembourg taxation today and is frequently scrutinised in tax audits, as it is an easily identifiable target for adjustments by the tax authorities. However, having appropriate transfer pricing documentation in place is a useful way of mitigating tax risks in Luxembourg and abroad.

The current international geopolitical environment may also have far-reaching consequences for the global economy, businesses and ultimately, transfer pricing. In particular, the ongoing war involving Israel, the USA and Iran will likely have a significant impact on oil and gas prices, fuelling inflation across a wide range of goods and services. The Strait of Hormuz accounts for a fifth of global oil consumption, so the mere threat of disruption is causing energy prices to rise. Iran has currently blocked this waterway. This will affect every tier of the global supply chain.

Such conflicts have the potential to prompt multinational groups to reconsider their supply chains. Furthermore, even if this conflict were to end soon, it would take decades to rebuild trust in the stability of Gulf countries.

Creation of a New Transfer Pricing Division

In Q4 of 2025, the Luxembourg tax authorities set up a new division specialising in transfer pricing. This initiative reflects a broader effort to professionalise expertise in this increasingly complex area within the tax authorities.

The division is expected to primarily serve as an internal resource, supporting tax inspectors during audits by providing specialised transfer pricing knowledge and contributing to cross-border dispute resolution processes. It will also help develop consistent local guidance on key transfer pricing matters.

The underlying goal appears to be greater coherence, ensuring that the positions taken by Luxembourg are more consistent across cases, and enabling the authorities to engage more effectively with foreign counterparts in discussions or disputes where necessary.

Transfer Pricing in Tax Audits

The Luxembourg tax authorities may review transfer pricing as part of a broader review of a Luxembourg company's corporate tax returns or a formal tax audit spanning several years. Based on experience, whenever the tax position of a Luxembourg company is reviewed, its transfer pricing is systematically scrutinised.

In practice, transfer pricing disputes primarily arise from a lack of proper documentation surrounding significant intra-group transactions. Conversely, thorough transfer pricing documentation provides a robust defence against challenges from the Luxembourg tax authorities.

Taxpayers should ideally take a proactive approach to transfer pricing, preparing documentation when entering into a controlled transaction. This is preferable to waiting until a transaction is identified during a tax audit. Although transfer pricing documentation can be prepared during a tax audit, the level of scrutiny of the assumptions, transfer pricing approach and benchmarking is much higher. After all, if the transfer pricing analysis confirms the pricing of the intra-group transaction, this might be considered a coincidence. However, if the Luxembourg tax authorities can demonstrate that the transfer pricing of an intra-group transaction does not adhere to the arm's length principle, it is the taxpayer's responsibility to disprove this presumption.

Without appropriate transfer pricing documentation, it is difficult to substantiate the arm's length nature of intra-group pricing. Furthermore, when transfer pricing documentation is prepared for a tax audit potentially years after a transaction has taken place, it can be challenging to trace all the necessary information and comparable data.

More Challenges From Foreign Tax Authorities

In recent years, foreign tax authorities have increasingly challenged the arm's length nature of transfer pricing in order to justify transfer pricing adjustments. As transfer pricing is not an exact science and requires judgement, tax authorities can consider different parameters or approaches, resulting in different

outcomes. This often makes transfer pricing the target of foreign tax audits.

Given the high debt levels of EU member states, combined with ambitious spending commitments such as the NATO 5% of GDP military spending target, pressure on national budgets is set to intensify, especially since interest rates on government debt have risen in recent years.

Consequently, it is likely that foreign tax authorities will continue to adopt increasingly assertive positions in transfer pricing audits. The pressure to meet tax revenue targets could lead to the boundaries of the arm's length principle being tested. Taxpayers should therefore prepare for greater scrutiny and less tolerance of undocumented or poorly justified pricing positions.

Impact of Geopolitical Conflicts on Transfer Pricing

In 2026, the global geopolitical landscape is characterised by significant instability. The ongoing war in Ukraine and the Israeli-USA war with Iran, which carries the risk of further escalation, are contributing to this deeply uncertain environment.

Approximately 20% of the world's oil and gas passes through the Strait of Hormuz. If the blockade continues, a sustained disruption would lead to significantly higher oil prices. This would not only affect energy costs, but also the prices of a wide range of goods and services that rely on oil and gas. This has the potential to cause inflation to rise considerably. Although most oil from the Gulf region is consumed by Asian countries, the workbench of the world that is dependent on cheap and reliable energy, the impact would be felt worldwide.

Furthermore, the current geopolitical situation in the Middle East is forcing many cargo ships to reroute around Africa, bypassing the Suez Canal entirely. This increases costs and transit times, posing significant risks to supply chains that rely on just-in-time production models.

This turmoil means that multinational groups must now consider geopolitical developments when assessing supply chain resilience, country risk and the reliability of global transport routes for raw materials and finished goods.

Moreover, if oil and gas prices remain high for an extended period, it is likely that inflation will remain high for a sustained period. This would necessitate more frequent updates to transfer pricing documentation. Ultimately, if the situation leads to a global recession, the implications for transfer pricing, particularly with regard to comparables, profit margins and benchmarking, would need to be carefully assessed.

The question, then, is how these developments specifically affect transfer pricing in Luxembourg. In Luxembourg's financial ecosystem, transfer pricing models focus more on the transmission of financial and regulatory risks resulting from geopolitical shifts than on physical supply chains. Treasury centres, investment platforms and holding companies should therefore ensure that they rigorously price heightened credit, country and currency risks in intra-group loans, guarantees and cash pools.

This requires robust transfer pricing documentation that clearly demonstrates how Luxembourg entities manage these risks and implement group financial strategy. Such documentation is essential to demonstrate how these entities execute and are remunerated for group-wide financial transactions in an increasingly fragmented world. It also serves as a critical defence against audit scrutiny in Luxembourg and abroad.

Conclusion

This article has explored how Luxembourg's transfer pricing is evolving in response to both domestic developments and external pressures. At the same time, new layers of complexity are being introduced by the broader geopolitical environment that cannot be ignored.

The practical implication for multinational groups and international investors is clear: transfer pricing cannot be treated as a static, annual compliance exercise. The assumptions underlying intercompany pricing, whether in financing, treasury or holding structures, may need to be revisited more frequently as economic conditions change. Inflation, supply chain disruptions

and changes in risk profiles all directly affect what constitutes an arm's length outcome.

In this environment, robust and contemporaneous documentation is the most effective defence. It not only serves to satisfy Luxembourg's evolving administrative expectations, but also to withstand scrutiny from foreign tax authorities whose revenue pressures continue to mount. Documentation that tells a credible, well-supported story, grounded in the facts of the business and the economic reality of the time, remains the cornerstone of any defensible transfer pricing position.

Looking ahead, taxpayers will need to be proactive rather than reactive. Those who monitor their transactions, update their analyses and document their reasoning in real time will be better placed to navigate an increasingly uncertain world. Ultimately, while the fundamentals of transfer pricing remain unchanged, the stakes and scrutiny have never been higher.

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