

Luxembourg: new VAT rules on directors' fees

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On 21 December 2023, the Court of Justice of the European Union (CJEU) delivered a landmark judgment determining that directors' fees received as independent board members of a Luxembourg public limited company are not subject to value added tax (VAT).

The Case (Case C-288/22) originated from the Luxembourg District Court (*tribunal d'arrondissement de Luxembourg*), which sought the CJEU's interpretation on the following questions:

- Does a natural person serving as a board member of a Luxembourg public limited company perform an "economic" activity as defined by Article 9 of the Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax (VAT Directive)?
- Does such a board member carry out his or her activity "independently", within the meaning of Articles 9 and 10 of the VAT Directive?

An overview of the CJEU judgement

To address these two core questions concerning the VAT Directive's interpretation, the CJEU provided the following reasoning.

Economic activity of board members

The CJEU clarified that a board member of a Luxembourg public limited company is engaged in an economic activity where a service is supplied in exchange for remuneration on a continuing basis. To determine whether the supply of services qualifies as an economic activity, the conditions under which the supply of services is delivered have to be analysed.

In the case under review, given a six-year renewable term for board members, their activity was deemed to have a continuing basis, hence constituting an economic activity within the meaning of the VAT Directive.

Independent nature of the activity

The CJEU further interpreted that the activity of a board member does not qualify as "independent" if the member does not act on its own behalf, under its own responsibility, nor bear the economic risk associated with the activity. The judgement specified that the board member in question did not have a decisive vote within the board meetings.

According to CJEU precedents, the absence of a subordination link and the bearing of economic risk are essential in determining whether an activity is carried out independently. In this case, the board member did not assume personal obligations for the company's debts, implying no economic risk born.

Therefore, the activity was not deemed as carried out independently and, as a result, VAT should not be applied to directors' fees in Luxembourg.

Implications of the CJEU judgement

On 30 September 2016, the Luxembourg VAT authority (AEDT) issued Circular n°781 to detail the VAT treatment of independent directors' fees. This circular specified that, as the board member's activity is considered as an economic activity by the AEDT, the corresponding remuneration is subject to VAT.

Following the CJEU decision essentially contradicting this interpretation, the AEDT issued Circular n°781-1 on 22 December 2023, which suspends with immediate effect Circular n°781 until the decision of the Luxembourg District Court is delivered. In practice, independent board members should deregister from VAT and cease filing VAT returns, but it also means that they will no longer be able to deduct VAT in the context of their board member activity.

On 15 January 2024, the AEDT published further guidance on its website regarding the CJUE decision. If people consider themselves affected by the decision, they are responsible for issuing rectified invoices to the taxable persons who are the recipients of their services. This justifies to the AEDT their right to the reimbursement of the VAT unduly charged.

Individuals can invoke this decision in their favour for fiscal years for which the standard limitation period of 5 years has not yet been reached. However, the AEDT indicated that it waives, on an exceptional basis, the limitation period for the 2018 fiscal year as the persons concerned may not have had an adequate period of time to assert any rights arising from the application of that CJEU decision. Therefore, the VAT unduly charged could be reimbursed as from the fiscal year 2018.

The AEDT should publish a new detailed circular at the time the Luxembourg District Court will have delivered its judgement. This circular should address companies whose VAT has been invoiced by their administrators and who will be required to adjust their right to deduct based on

the new legal situation.

The AEDT also indicated on its website that it will ensure a "non-bureaucratic" regularisation of the tax in the hands of the administrators, and announced it will set up a dedicated electronic procedure for this purpose.

This judgement may also impact other European member states, which may need to adapt their legislation and/or administrative practice in case of a conflict with this judgement.

Should you have any questions or require further clarification, please do not hesitate to contact us.

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