

Luxembourg Newsflash

February 2023

“ALPHABET SHARES” AND PARTIAL LIQUIDATION: NOT THE FINAL WORD YET...

The Administrative Court of Luxembourg issued an interesting ruling on 27th January 2023, in a case involving the purchase of an entire class of its own shares by a Luxembourg resident entity, followed by their cancellation.

Although hailed by many as the long-awaited confirmation of the tax treatment of the so-called “*alphabet shares*”, this ruling does not validate the position taken by the doctrine. Further, it relates to a very specific case and it might appear somewhat adventurous to draw too general conclusions, especially at this stage as the decision sends the case back to the Tax Authorities for a part, and might still be appealed in front of the Administrative Court of Appeal.

The Luxembourg resident company was holding a participation in a Welsh operational entity and was fully held by a company resident of the Cayman Islands. The share capital of the Luxembourg resident company was divided in ten classes of shares (from A to J) and, shortly after the realisation of its participation in the Welsh subsidiary not being followed by the reinvestment of the proceeds of the sale, the Company redeemed the entire Class J for a price exceeding the nominal value of the shares.

The Luxembourg Tax Authorities (“LTA”) considered that the positive difference between the redemption price and the nominal value of the shares could not be considered as liquidation proceeds in the scope of a “*partial liquidation*” assimilated to a tax-exempted liquidation under article 101 LIR. Strangely enough, the reason given was that the shares in each different class did not attract different economic rights. Consequently, such allocation was re-characterised as a distribution and subject to 15% withholding tax. The taxpayer appealed to the Administrative Court.

The Court underlined that all classes of shares were held by the same shareholder and that the creation of the different classes of shares did not happen as per the very creation of the company but was set up afterwards. Interestingly, such three characteristics (number of shareholders, existence of the classes as from the inception of the company, and different economic rights) were the typical conditions set by the LTA before confirming the application of the partial liquidation tax treatment to “*alphabet shares*”, under the previous advance tax agreements policy.

In the absence of these elements, the Court concludes that the operation of purchase of its own shares by the company, followed by their cancellation, had been rightfully characterised as a distribution. Surprisingly, the Court further considers that such characterisation only applied to the part of the purchase price which exceeds the “*fair market value*” of the shares. The case is further referred back to the Tax Authorities for the purposes of determining such “*fair market value*” and hence the amount of the purchase price to be characterised as distribution.

One is curious to see how such will be determined in the case of a cash company after disposal of its sole asset...



Jean-Luc Dascotte
Partner

jean-luc.dascotte@strelia.com
+352 2088 2310



Stanislas Bunetel
Partner

stanislas.bunetel@strelia.com
+352 2088 2310