ATOZ ALERT

Luxembourg Tax Administration publishes FAQ on Pillar Two transition rules regarding deferred tax assets and liabilities

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Introduction

On 25 March 2024, the Luxembourg Tax Administration ("**LTA**") published an FAQ aiming to clarify the application of the law of 22 December 2023 transposing the Council Directive (EU) 2022/2523 of 14 December 2022 on ensuring a global minimum level of taxation for multinational enterprise groups and large-scale domestic groups in the Union (the "**Pillar Two Law**").

In this FAQ, the LTA provides welcomed clarifications addressing the transition rules regarding the tax treatment of deferred tax assets and liabilities. This FAQ will further be completed as soon as new information becomes available.

Clarifications brought by the FAQ

The Pillar Two Law states that when determining the effective tax rate for a jurisdiction in a transition year, and for each subsequent fiscal year, the MNE group or a large-scale domestic group shall take into account all the deferred tax assets and deferred tax liabilities ***reflected or disclosed*** in the ***financial accounts*** of all the constituent entities in a jurisdiction for the transition year. The transition year is defined as the first fiscal year in which a group falls within the scope of the Pillar Two rules.

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FINANCIAL ACCOUNTS CONCERNED

The FAQ specifies that the "financial accounts" concerned are the financial accounts of the Luxembourg constituent entity concerned (i.e. annual accounts) and/or the consolidated financial accounts of the ultimate parent entity.

In the latter case, it is important that the information can be reliably and consistently traced back to the Luxembourg constituent entity concerned.

Reference is also made to the "Q&A 24/032" of the *Commission des Normes Comptables* ("**CNC**") concerning the option to disclose deferred tax assets and liabilities in the notes to the 2023 annual accounts, acknowledging that a Luxembourg constituent entity has the ability to disclose deferred tax assets and liabilities based on the applicable Luxembourg corporate tax rate, and does not need to perform a specific analysis of the recoverability of tax losses in order to disclose the related deferred tax assets in the context of the Pillar Two Law.

"REFLECTED" OR "DISCLOSED"

The FAQ further precises that the terms "reflected in the financial accounts" refer to deferred tax assets or liabilities that are recognised in the balance sheet of the financial accounts while the terms "disclosed in the financial accounts" refer to deferred tax assets or liabilities that are disclosed in the notes to the financial accounts.

In this respect, the LTA acknowledges that disclosure in the notes to the financial accounts is sufficient in order to benefit from these transition rules. In practice, it should allow under certain conditions the deferred tax assets on pre-existing tax losses carried forward to be taken into account for the computation of the effective tax rate under Pillar Two Law, even though the future use of such tax losses is uncertain and these deferred tax assets would probably not be recognised under IFRS under IAS 12.

With regard to the possibility for a Luxembourg company which is part of a group of MNEs or a large national group within the meaning of the Pillar Two Law to present its deferred tax assets and liabilities in the notes to its financial accounts, the CNC repeated that it is the responsibility of the company to provide in the notes to its annual accounts any additional information, including on potential deferred tax assets or liabilities, to contribute to the objective of a true and fair view of the financial accounts.

TIMING

The first effect of the transitional measures under the Pillar Two Law occurs from the transition year onwards. To benefit from these measures, it is recommended by the LTA that all deferred tax assets and liabilities be reflected or disclosed in the financial accounts for the year preceding the transition year. For instance, for a transition year covering the period from 1 January 2024 to 31 December 2024, it is recommended that all deferred tax assets and liabilities be reflected or disclosed in the financial accounts for the year ending 31 December 2023.

Do you have further questions?

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