

Directors' liability in event of non-compliance with company tax obligations: case law reversal

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Introduction

Case law reversal

Difficulties in applying new case law

Introduction

Under Sections 103 and 108 of the General Tax Law, directors are held personally liable for the fulfilment of their company's tax obligations (ie, direct income taxes). Further, directors are held jointly and severally liable for direct tax claims (eg, payroll withholding tax). Thus, if a company is declared bankrupt, the Tax Administration may sue its directors to settle the company's social tax claims and debts.

Prior to a case law reversal, the Administrative Court took a strict approach towards directors and systematically held that they had breached their duties by simply failing to withhold, declare or pay company taxes.

However, on 4 April 2017 the Administrative Court of Appeal held that the wrongful character of any alleged tax breaches must be demonstrated by law and factually proved by the Tax Administration.

Case law reversal

Luxembourg case law was reversed when Dominique Strauss Kahn – a director of a Luxembourg company that had been declared bankrupt and who was thus held liable for the company's tax breaches – filed a hierarchical appeal against the director of the Tax Administration, which was subsequently followed by an administrative appeal.

On 8 November 2016 the Administrative Court confirmed that the Tax Administration director had been right in claiming that Strauss Kahn, in his capacity of company director, should be held liable for unpaid company withholding taxes. The judgment stated that "as a director, [Strauss Kahn] was guilty of negligence for not having withheld and paid the company's taxes".

However, in his appeal of the abovementioned decision, Strauss Kahn claimed that he "had not held any management position", although he had been chair of the company's board of directors. On 4 April 2017 the Administrative Court of Appeal decided that "the wrongful nature of the appellant's alleged breaches were not sufficiently demonstrated by law and factually proved by the State party". The court also stated that the breach of a company's tax obligations is insufficient to trigger its directors' personal liability.

Difficulties in applying new case law

The Administrative Court is reluctant to apply the so-called 'Strauss Kahn' case law due to its restrictive interpretation of the notion of a fault or mistake, which completely contravenes Administrative Court of Appeal case law.

In the event of an appeal against a tax form concerning a warranty claim addressed to a director, a hierarchical appeal must first be filed against the Tax Administration. The latter, for the time being, continues to apply the old case law and ignore the Strauss Kahn case law, which forces accused directors to file an administrative appeal.

With this new case law, the Luxembourg administrative courts have moved closer towards the notion of liability applied in Belgium and France, where tax administrations must demonstrate a director's wrongful behaviour in fact and by law.

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The Belgian Income Tax Code deals with the notion of a fault or misconduct by withholding tax on wages and salaries (ie, withholding tax on earned income). Thus, a company director must have committed fraud in order to avoid taxes. Article L.267 of the French Tax Procedures Book also establishes a mechanism of tax solidarity between a company and its directors. Thus, in the event of fraudulent operations or serious and repeated non-compliance with the company's tax obligations, a director may be held personally liable for the company's tax debts.

This new approach has seen Luxembourg move towards a shared, wider interpretation of directors' liability. However, the Tax Administration and some courts oppose this approach.

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