

Bill 7020 approved by the Luxembourg Parliament: general 2017 tax measures for corporations and individuals

15 December 2016

In brief

On 14 December 2016, the Luxembourg Parliament approved (subject to confirmation by the Luxembourg Conseil d'Etat that no second hearing is required) a law making changes to the Luxembourg corporate, personal and value added tax systems. For companies, the changes include, notably, a reduction of the basic corporate income tax rate from 21% to 18% (in two steps).

For individuals, the reform involves a wide range of measures, encouraging aspects such as access to housing and private pension schemes. There are modifications to the income tax scales, and an increase in the tax rates for individuals earning more than EUR 150,000.

Most of the measures enter into force as from 1 January 2017. However, some changes for individuals are only applicable as from tax year 2018. Nearly all these measures have already been foreseen in our previous Flash News reports dated 26 February 2016, 3 May 2016 and 2 August 2016.

In detail

1. Corporations

1.1. Reduction of the corporate income tax rate

The corporate income tax (**CIT**) rate per se is to be reduced from 21% to 18% over the next two years. There are no changes to the “solidarity surtax” rate levied on the CIT rate, or to the rate of municipal business tax (**MBT**) payable by companies.

More specifically, the CIT tax rate for companies having a net taxable base of more than EUR 30,000 is reduced to **19%** for **FY 2017**, and **18%** for **FY 2018**, resulting in an overall tax rate of **27.08%** for companies in Luxembourg City for **FY 2017**, and **26.01%** for **FY 2018** (taking into account the solidarity surtax of 7% on the CIT rate, and including the 6.75% MBT tax rate assumed as remaining applicable).

In addition, a reduced CIT rate of 15% will be applicable as from **FY 2017** for companies with a tax base of less than EUR 25,000. For companies with a tax base between EUR 25,000 and EUR 30,001, the corporate income tax charge will be EUR 3,750 plus 39% of the basis above EUR 25,000 for **FY 2017**, and EUR 3,750 plus 33% of the basis above EUR 25,000 for **FY 2018**.

1.2. Increase of the minimum net wealth tax

A minimum net wealth tax (NWT) charge was introduced on 1 January 2016, for all corporate entities having their statutory seat or central administration in Luxembourg. The measures imposing this new charge are very similar to the previous provisions for the minimum CIT charge, which was abolished with effect from the same date.

As from FY 2017, for holding and finance companies (often referred to as “SOPARFIs”) whose sum of fixed financial assets, intercompany loans, transferable securities and cash at bank (as reported in their commercial accounts presented in the standard Luxembourg form) exceeds both 90% of their total gross assets and EUR 350,000, the minimum NWT has been increased from EUR 3,210 (including the solidarity surtax) to EUR 4,815 (including the solidarity surtax).

The minimum NWT applicable to all other corporations, having their statutory seat or central administration in Luxembourg, remains unchanged.

1.3. Restrictions on the use of future losses

The use of losses generated as from FY 2017 is limited. Losses generated during and after FY 2017 will only be able to be carried forward for a maximum period of 17 years.

Losses that arose before FY 2017 are not affected by this time limit.

Contrary to the measures the Government initially announced, any loss offset will not be limited to 75% of the net taxable profits of each subsequent year.

1.4. Deferred depreciation

The rules governing depreciation of fixed assets for tax purposes are amended, in order to offer the possibility for taxpayers to defer deductions related to depreciation for any given tax year. For this purpose, a specific request needs to be made when filing the tax return for the year concerned. The deduction can be deferred until, at the latest, the end of the depreciation life of the asset (i.e., any depreciation amounts deferred from previous years have to be deducted at the latest for the last year for which depreciation is allowed).

The application of this measure could potentially result in a timing difference that would increase the CIT and MBT to be paid by a taxpayer for any given year. However this might allow the taxpayer to reduce its NWT base – assuming certain conditions apply, and that the taxpayer decides to book a special NWT reserve to reduce its NWT liability for the year concerned. This measure might also allow taxpayers to use investment and other tax credits during a tax year, whereas the company might otherwise have been unable to do this because it was in a tax loss position.

During the passage of the Bill for this legislation the State Council, in reviewing the text of the Bill, noted that, while this deferred depreciation mechanism could be beneficial for taxpayers for CIT purposes (investment and other tax credits can be used only against a CIT liability), it would not be for MBT purposes, because any increase of an MBT liability cannot be offset by tax credits. Opting for deferral of depreciation could thus cause a taxpayer to incur additional net cash MBT liabilities, unless the company also has brought forward tax losses.

1.5. Other new tax measures

Other measures in the legislation which could benefit companies are as follows:

- The scope of the article 54bis LITL regime (deferral of taxation on foreign exchange gains on certain assets denominated in a foreign currency) will be extended to any company as from FY 2016.
- Investment, especially in research and development, is further encouraged, through the increase of investment tax credits. Complementary and overall investment tax credits are increased from 12% to 13%, and from 7% to 8%, respectively. The rate of overall investment tax credit for investment exceeding EUR 150,000 however remains at 2%. The investment tax credit for assets eligible for the special depreciation regime is increased from 8% to 9% - here the tax credit for investment exceeding EUR 150,000 remains at 4%. In addition, the scope of eligible investments has been extended to include investments made anywhere within the European Economic Area.
- In order to make inter-generational transfers of family businesses easier, capital gains linked to real estate assets (both land and buildings) will benefit from a tax-neutral treatment.
- Farming businesses may deduct 30% of the amount of any new investment up to a total of EUR 250,000. Investment above this amount is eligible for a deduction of 20% of the difference between the investment amount and the EUR 250,000 limit.
- As from FY 2017, tax returns for companies liable to CIT no longer have to be filed via regular mail. The legislation effectively foresees that it will be mandatory to file CIT and related returns electronically.

2. Indirect tax measures

2.1. VAT measures

2.1.1. Personal and joint liability of the managers of VAT taxable persons

New provisions pursuant to which delegated administrators and directors, as well as any “*de jure*” and “*de facto*” managers in charge of the day-to-day management of VAT taxable persons, can be held jointly and personally liable in the event of breach of VAT compliance obligations and/or non-payment of the VAT due by the taxpayer that they manage.

The Director of the Luxembourg VAT Authorities now has the power to launch a guarantee call procedure (“*appel en garantie*”) against the persons listed above. This procedure is introduced into the Luxembourg VAT regime for the first time, but is not completely new, as it is already applicable for direct taxes.

These new measures will apply if the delegated administrators, directors or the “*de jure*” or “*de facto*” managers who are in charge of the taxpayer's day-to-day management have failed in the performance of their duties (“*inexécution fautive*” in French).

Persons who are right-holders (“*ayants-droits*”), liquidators, and curators of VAT taxable persons who are respectively dead, in liquidation, or in bankruptcy, were initially encompassed but have finally been removed from the scope of these new measures.

2.1.2. General increase of penalties

	Current penalties	New penalties
Breach of VAT compliance rules (such as VAT registration, invoicing, VAT filing and accounting rules) and VAT payment obligations	Between EUR 50 and EUR 5,000 per infraction	Between EUR 250 and EUR 10,000 per infraction
Absence of / delay in communicating documents / information upon request by the Luxembourg VAT authorities	Daily penalties from EUR 50 to EUR 1,000	Daily penalties of maximum EUR 25,000 per day
Breach of VAT compliance rules (such as VAT registration, invoicing, VAT filing and accounting rules) and VAT payment obligations - if the aim or result is to evade the payment of VAT or recover VAT in an irregular manner	10% of the VAT avoided or improperly reclaimed	Between 10% and 50% of the VAT avoided or improperly reclaimed
New! Aggravated tax fraud – “ <i>fraude fiscale aggravée</i> ” (depending on the amount of VAT due / or VAT improperly reimbursed per filing period)	n/a	Imprisonment from 1 month to 3 years, and a fine of between EUR 25,000 and six times the amount of VAT avoided or improperly reimbursed
New! Tax swindle – “ <i>escroquerie fiscale</i> ”	n/a	Imprisonment from 1 month to 5 years, and a fine of between EUR 25,000 and ten times the amount of VAT avoided or improperly reimbursed.

2.1.3. Recommendations

These several new VAT measures underline the importance of being fully compliant at all times with the Luxembourg VAT legislation, and in particular ensuring that all VAT taxable persons always:

- Register for VAT on time
- File accurate and complete VAT returns (both periodic and annual)
- File VAT forms and pay the related VAT within the deadlines
- Comply with other VAT obligations (issuance of valid invoices, FAIA ...)
- Compute amounts of recoverable VAT based on accurate figures
- Promptly provide information and documents, in the event of questions from, or an audit being carried out by, the Luxembourg VAT authorities
- Check and have sufficient comfort on the VAT treatment applied applicable to output and input transactions

2.2. Registration duties

The main changes are positive moves that reduce uncertainties and the administrative burden.

- Rental agreements are no longer subject to any registration obligation. Parties still have the possibility to register these agreements voluntarily, notably to determine the date of an agreement for civil law purpose, or make them enforceable against third parties. If the rental agreement is voluntarily registered, registration duty at 0.6% would remain due, unless a valid VAT option has been duly approved by the Luxembourg VAT authorities.
- Application of the so-called “*théorie de l’usage*” will now be limited to deeds which have mandatorily to be registered. Until now, deeds not subject to a registration obligation were nevertheless subject to registration duty when they were subsequently mentioned in, or attached to, deeds subject to the formality of registration. This is especially the case for private agreements evidencing the existence of a debt claim, which used to give rise to exposure to the 0.24% registration duty based on the *théorie de l’usage* when referred to in a notarial deed (for example in the context of a contribution of the underlying receivable). Such private agreements, which are not subject to mandatory registration, will now be explicitly excluded from the *théorie de l’usage*.
- There is a general increase in penalties for non-compliance or abuse.

3. Personal tax measures

3.1. Measures entering into force on 1 January 2017

The most important changes affecting individual taxpayers are outlined below.

3.1.1. Revisions of the income tax scale

Income tax brackets are revised, with the introduction of new tax rate scales. The overall consequence is a lowering of the average tax rate. However, new tax rates for individuals with higher income are added (tax rates of 41% and 42% on income exceeding EUR 150,000 and EUR 200,004 respectively).

3.1.2. Improving access to real estate

- Increase of the ceiling for deductible contributions to home saving schemes (“*contrat d’épargne-logement*”): tax-deductible contributions increase from EUR 672 to EUR 1,344 for individuals aged up to 40. Beyond the age of 40, the annual deduction remains set at EUR 672 per contributor.
- Residences occupied without rent (e.g. the main residence of an owner): the deemed rental income of a property occupied by the owner is abolished.
- Increase of the ceiling for deductible mortgage interest: tax-deductible mortgage interest incurred to acquire the main residence increases as follows:
 - EUR 2,000 (from EUR 1,500) for the first year of occupation and the following five years;
 - EUR 1,500 (from EUR 1,125) for the next following five years;
 - EUR 1,000 (from EUR 750) for subsequent years.
- Encouragement to rent to approved social organisations: income arising from the rental of housing to approved social organisations (e.g. Agence Immobilière Sociale) is to benefit from a 50% exemption.

3.1.3. Strengthening households' purchasing power

- Depending on the level of income, the tax credit for employees (*crédit d'impôt pour salariés*), for pensioners (*crédit d'impôt pour pensionnés*), and for self-employed individuals (*crédit d'impôt pour indépendants*) is set at EUR 600 (instead of EUR 300 currently), where annual income/pension is between EUR 11,265 and EUR 40,000. This tax credit is reduced to EUR 300 for annual income between EUR 40,001 and EUR 79,999. Above EUR 80,000, the tax credit is no longer granted.
- Single parents are to enjoy a tax credit (*crédit d'impôt monoparental*) of a maximum of EUR 1,500 per year (instead of EUR 750 per year currently), when the annual taxable income does not exceed EUR 35,000. Above EUR 35,000, the tax credit is reduced to EUR 750. Parents sharing a common residence are not eligible for this tax credit.
- The tax deduction granted to a taxpayer contributing to the education and maintenance costs of a child that is not part of his/her household will increase from EUR 3,480 to EUR 4,020 per year, and per child. However, parents sharing a common residence will not be entitled to this deduction.
- The lump-sum allowance for domestic fees (cleaning and childcare expenses, and social assistance for dependent people) will increase from EUR 3,600 to EUR 5,400 per year.
- Employers will be able to provide employees with luncheon vouchers with a face value of up to EUR 10.80 without triggering a higher taxable benefit for the employee. The taxable benefit will remain at EUR 2.80 per voucher.

3.1.4. Sustainable transport

A new tax deduction, to encourage the use of sustainable transport, is introduced for vehicles and cycles registered or purchased after 31 December 2016. The tax deduction is set as follows:

- EUR 5,000 for zero-emission vehicles
- EUR 300 for cycles (including cycles with pedalling assistance)

In addition, the lump-sum valuation method for determining the taxable benefit in kind arising from the private use of a company car will take account of the car's CO₂ emissions level and fuel type. While currently the monthly taxable benefit is set at a flat 1.5% of the car's value (inclusive of VAT), it will range from 0.5% to 1.8% as from 1 January 2017. This new valuation method will only apply to company cars which are leased as from 1 January 2017.

Cycles (including cycles with pedalling assistance) made available to employees will not generate any taxable benefit.

3.1.5. Other changes

- Interest payments and insurance premiums: The deduction of both interest payments and insurance premiums will be merged, with a maximum of EUR 672 per member of the household (instead of an aggregate ceiling of EUR 1,008).
- Private old-age pension plans: the annual tax deduction for private old-age pension plans (*contrat de prévoyance-vieillesse*) is set at a maximum of EUR 3,200 for all taxpayers, irrespective of their age. Currently, the maximum deduction ranges from EUR 1,500 to EUR 3,200, depending on the taxpayer's age.
- Withholding tax on interest income: under the "Relibi" Law, qualifying interest income derived by a Luxembourg resident is currently subject to a 10% flat and final withholding tax. This withholding tax rate will increase to 20%.
- Abolition of the 0.5% temporary "budget-balancing" tax.

3.2. Measures entering into force from 1 January 2018

3.2.1 Introduction of an optional individual taxation regime for taxpayers (both married couples and civil partners) taxable jointly

As from tax year 2018, resident and non-resident jointly taxable taxpayers will have the possibility either to continue to file a joint tax return, or to opt for separate individual taxation. Under this regime, couples opting for separate taxation will be taxed in tax Class 1. They will be able to apply for either of two regimes.

- A full individualisation (“*individualisation pure*”), where each item of income is allocated individually to each partner based on the applicable matrimonial regime, and where deductions (e.g. for insurance premiums, interest payments, dependent children), and the potential increase in ceilings for married couples with dependent children, are split equally between the spouses;
- An individualisation with reallocation of income (“*individualisation avec réallocation des revenus*”), where the total adjusted taxable income of the household (determined based on the aggregate net income and applicable tax deductions) will by default be allocated equally between the partners, irrespective of the level of their individual income. The partners can also request a different allocation of the total adjusted taxable income. In addition, the law extends this individualisation method to civil partners.

Under payroll withholding, taxpayers will each be taxed under tax Class 1 if they opt for the full individualisation, while taxpayers who choose individualisation with reallocation of income will be taxed at their global tax rate.

3.2.2. Differences in treatment between resident and non-resident married couples

Married non-resident taxpayers will be regarded as being in tax Class 1 by default, and can no longer be treated as tax Class 1a or Class 2.

As an exception to this, married non-resident taxpayers may keep the benefit of tax Class 2 (i.e. as for married resident taxpayers), provided that some specific conditions are met, and that they report their non-Luxembourg sourced income (for example the spouse’s professional income). Such non-Luxembourg sourced income will be exempt for Luxembourg tax purposes but taken into account for the determination of the applicable tax rate on the Luxembourg sourced income (“exemption with progression”).

In practice, married non-resident taxpayers where one spouse works outside Luxembourg will be adversely impacted by this provision, as it will be likely to increase significantly the Luxembourg tax burden.

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