Flash News

Major tax changes for corporations and individuals in Luxembourg

On 17 December 2015, the draft bills no. 6847, no. 6891 and no. 6900 were voted by the Luxembourg Parliament. They have been subsequently adopted on 21 December 2015. Hereafter, some of the most important changes are briefly described.

- **Changes to the minimum tax for corporations and the net wealth tax**

Up to and including the tax year 2015, Luxembourg based corporations are subject to a minimum tax for both corporate tax (reference is made to our Flash News dated 5 January 2015) and net wealth tax purposes (EUR 62 for S.A. Société anonyme /Public limited company, S.C.A. Société en commandite par action / Partnership limited by shares and S.E. Société Europénne / European company as well as EUR 25 for S.à r.l. Société à responsabilité limitée / Limited liability company).

With introduction of the new tax rules, the minimum tax for corporate tax purposes will be abolished from 2016 onwards and replaced by a minimum net wealth tax which is assessed on the basis of the balance sheet total. The current minimum net wealth tax will no longer apply. The new minimum net wealth tax corresponds to the previous minimum corporate tax (including the contribution to the employment fund). The distinction between “finance and holding companies” (financial assets, marketable securities and cash > 90% of balance sheet total) and “other companies” has been maintained, as well as the assessment based on the balance sheet total. However, an additional tariff level was added.

Balance sheet total	Other companies	Finance and holding companies
0 to 350.000	535 €	535 €
350.001 to 2.000.000	1.605 €	3.210 €
2.000.001 to 10.000.000	5.350 €	3.210 €
10.000.001 to 15.000.000	10.700 €	3.210 €
15.000.001 to 20.000.000	16.050 €	3.210 €
20.000.001 to 30.000.000	21.400 €	3.210 €
Exceeding 30.000.000	32.100 €	3.210 €

As before, the regular net wealth tax may be reduced in respect of the prior year’s corporation income tax payable (including contribution to the employment fund and after crediting the investment tax credit) if a special reserve is constituted and maintained (subject to conditions).

In case of a tax group for income tax purposes, each company within the tax group continues to be subject to net wealth tax in relation to its own taxable assets (no tax group for net wealth tax purposes).

Also in this situation, the alternative to credit prior year's corporate tax of the controlling company of the tax group to the net wealth tax of each of the controlled subsidiaries in the tax group remains possible. In a first stage, the corporate tax has to be credited at the level of the controlled subsidiaries in descending order of their assets before crediting the corporate tax at the level of the controlling company / controlling subsidiary.

However, there is a cap on the minimum net wealth tax for the entire tax group with a maximum of EUR 32,100. Again, in a first stage, the excess of the minimum net wealth tax is to be deducted at the level of the controlled subsidiaries in descending order of their assets before deducting it at the level of the controlling company / controlling subsidiary.

In order to apply the minimum net wealth tax to securitization vehicles, SICARs, ASSEPs and SEPCAVs, the respective legal provisions, which provide for the general exemption of these companies from net wealth tax, have been limited to such an extent that the exemption from net wealth tax now only applies subject to this minimum tax.

Moreover, a graduated net wealth tax rate will become applicable as from 01.01.2016.

- 0.5% for a tax base of up to EUR 500 million
- For a tax base of over EUR 500 million, the net wealth tax consists of the sum of EUR 2.5 million and 0.05% of the portion of the tax base exceeding EUR 500 million, whereby there is no cap.

- **Changes in the tax exemption of intercompany dividends**

As part of the amendment, two EU directives, directive 2014/86/EU (avoidance of double non-taxation) and directive 2015/121/EU (introducing a common minimum anti-avoidance rule), which change the parent-subsidiary directive (2011/96/EU), have been transposed into national law.

From 2016 on, the withholding tax exemption for dividends pursuant to Art. 147 no. 2 (a) and (d) ITL[1] will no longer apply, when, taking objectively all facts and circumstances into consideration, artificial arrangements are implemented, whose primary objective or one of their primary objectives is to obtain a tax advantage, or if they violate the principles of the Parent-Subsidiary Directive.

Accordingly, the exemption as laid down in Art. 166(2bis) ITL and § 9 no. 2a MBTL[2] will no longer apply insofar as the underlying income is tax deductible in another EU Member State or, when, taking objectively all facts and circumstances into consideration, dividend distributions are part of artificial arrangements, whose primary objective or one of their primary objectives is to obtain a tax advantage, or if they violate the principles of the Parent-Subsidiary Directive.

Artificial arrangements in the meaning of this provision shall exist if there are no strong commercial reasons which reflect the economic reality. An artificial arrangement can also take place in several steps.

[1] Income tax law
[2] Municipal business tax law

According to the wording only direct investments in EU corporations should be affected. In principle, dividends from non-EU corporations, liquidation proceeds or capital gains should not fall under this regulation. It should also not apply to the net wealth tax exemption rules for qualifying participations.

- **Extension of the scope of the tax group**

With retroactive effect from 2015, the possibility of a horizontal integration has been introduced. Basically, fully taxable resident corporations or domestic permanent establishments of fully taxable foreign corporations may create a tax group with fully taxable resident corporations or a domestic permanent establishment of a fully taxable foreign corporation.

Alternatively, a tax group can now also be established via a non-integrated parent company, in as much as it is a fully taxable resident corporation, a domestic permanent establishment of a fully taxable foreign corporation, a fully taxable foreign EU corporation or a foreign permanent establishment of a fully taxable foreign EU corporation. In these cases, the aggregation for tax purposes will take place at the level of a so-called controlling subsidiary. Only those subsidiaries in the tax group can qualify as controlling subsidiary which are closest to the non-integrated parent company in the group's hierarchy. If several subsidiaries in the tax group are equally close to the non-integrated parent company in the group hierarchy, one of them can be selected as the controlling subsidiary.

For the creation of a tax group, a continuous direct or indirect participation in the capital of at least 95% at each level from the beginning of the first fiscal year of the tax group is required. As far as intermediary companies are concerned, they have to be fully taxable corporations and partnerships are treated as tax transparent.

Furthermore, a joint written request of all corporations involved in the tax group (incl. the non-integrated parent company) has to be submitted before the end of the first tax year of the tax group. In a tax group with a non-integrated parent company, the controlling subsidiary has to be determined in the application. The tax group must be maintained for a minimum period of 5 years.

Tax loss carry forwards existing from periods prior to the tax group may only be offset insofar as the company, which has suffered the losses in the past, is in a profit situation. After a tax group has been terminated, tax loss carry forwards accumulated during the existence of the tax group can only be used at the level of the controlling company or the controlling subsidiary.

Each company of the tax group is liable for the taxes, late filing fees, charges and penalties of the controlling company or the controlling subsidiary. The companies forming part of a tax group can only be members of one tax group.

SICARs (Sociétés d'investissement en capital à risque) and securitization vehicles are excluded from the tax group rules.

- **New rules on tax deferral in exit scenarios**

For taxes on capital gains in case of the relocation of an entity within the meaning of Art. 38 ITL or the relocation of the registered office together with the center of management of a corporation within the meaning of Art. 172 ITL to other EU member states or to countries with which Luxembourg has concluded a double tax treaty and agreed on an exchange of information, a tax deferral may be granted upon request (without assessment of late interest and without collaterals). The deferral applies until the transferred goods are sold abroad. In case of qualifying contributions, mergers etc. in the meaning of the EU merger directive, the deferral will remain in place insofar as the beneficiary entity will assume the obligations related to the tax deferral (annual documentation in due form). The tax payer may, however, terminate the deferral at any time.

- **Abolition of the IP-Regime**

Until now, certain intellectual property rights (software copyrights, patents, trademarks, internet domain names, patterns and designs) could benefit from a privileged tax treatment as 80% of the respective net income (license fees and capital gains) could be treated as tax exempt income and the respective assets were 100% exempt from the net wealth tax.

Following the OECD report published on October 5, 2015 on action 5 of the Action Plan on Base Erosion and Profit Shifting (BEPS Action Plan), the Luxembourg IP-Regime, as laid down in Art. 50bis ITL and §60bis BewG[3], will be abolished as from 1 July 2016 (respectively as from 1 January 2017 for the determination of business assets).

In line with the OECD recommendations, a grandfathering rule may be applied by tax payers who already make use of the IP-Regime (created or acquired before 1 July 2016), for a transitional period of 5 years starting on 1 July 2016 and ending on 30 June 2021 (respectively on 1 January 2021 for net wealth tax purposes).

However, this grandfathering rule is not applicable if the intellectual property rights have been acquired after 31 December 2015 by a related person, unless the IP was previously qualifying for a privileged treatment in Luxembourg or abroad. However, the privileged treatment abroad has to be comparable with the Luxembourg regulations (so-called back-end regimes). It should be noted that for the determination of a related party as defined by this regulation, the definition of Art. 56 ITL (direct and indirect participation > 50%) is decisive, not Art. 50bis ITL.

If the grandfathering rule cannot be applied, the privileged tax treatment just remains valid for the year 2016.

Acquisitions as defined by this regulation include all transfers for value but also all tax neutral transfers (contributions, spin-offs, merger – initial acquisition dates will not be considered).

Furthermore, it should be noted that the Luxembourg tax authorities will spontaneously and without prior request provide information on the identity of the beneficiaries with regards to all privileged IP rights created or acquired after 6 February 2015 (date of the OECD publication on the agreement on the "Nexus Approach") to the competent foreign tax authorities.

[3] Bewertungsgesetz (valuation law)

To the extent that information is obtained as part of the tax return, it will be forwarded to the other state no later than 1 year after the filing of the tax return. In case the information is obtained prior to this, it will be forwarded within a period of 3 months after the notification.

Currently, no draft bill for introducing new regulations for a new IP-Regime has been submitted yet, which then would be in accordance with the so-called "Nexus Approach" provided for by the OECD. It is however expected that a respective draft bill will be presented in the near future.

- **Changes with respect to individuals which are tax resident during part of the year**

There are also retroactive tax changes as from the year 2015 for individuals, who are only tax resident in Luxembourg during part of the year. So far, in the event of a partial tax residency, only pensioners and employees could opt to be treated as if they were tax resident for the entire year. This option might be advantageous, as only in this case various lump-sum amounts, limits, allowances, etc. can be taken into account in the tax assessments.

However, at the same time all domestic and foreign income received during the period of non-residency has to be considered when determining the global tax liability. This option is now available to all partial resident taxpayers, regardless of the type of income generated.

- **Introduction of a step-up for immigrating individuals**

Likewise as of the tax year 2015, individuals, who transfer their tax residence to Luxembourg, can opt for a so-called "step-up" in relation to their qualifying participation in corporations (> 10%) and the respective convertible loans. This measure has been introduced in order to prevent possible double taxation in case e.g. an exit tax is levied on such securities in the exit country. This step-up, however, can be applied independently of the country a tax payer is immigrating from and of the effective occurrence of double taxation.

With this step-up, the purchase price of the respective securities, from a tax point of view, will be revalued to their market value at the time of the immigration to Luxembourg. Thus, part of a possible subsequent capital gain, relating to the period prior to the immigration, remains tax-free in Luxembourg.

Whereas the initial date of acquisition prior to the immigration is used for the calculation of the respective holding period, the year of arrival in Luxembourg should be taken as a basis for the calculation of the revaluation coefficient as laid down in Art. 102 (6) ITL.

The step-up is, however, not allowed if persons were tax resident in the past for more than 15 years in Luxembourg and have not been tax resident for less than 5 years before (re-)immigration.

- **Abolition of the voluntary disclosure regulations and introduction of a temporary tax amnesty for individuals**

With effect from 1 January 2016, the regulation on voluntary disclosure according to § 410 AO[4] will cease to exist. Thus, in case of intentional non-compliance with tax regulations (tax fraud acc. to § 396 AO) and negligent tax avoidance (tax evasion acc. to § 402 AO) respective penalties have now to be paid (in particularly severe cases of systematic tax fraud, the penalties may be assessed up to 10 times the evaded tax and include imprisonment up to 5 years).

Simultaneously with the abolition of the voluntary disclosure regulations, transitional rules for the period from 01.01.2016 to 31.12.2017 (§ 489 AO) will come into force (temporary tax amnesty).

Every tax payer who submits, on a voluntary basis, a complete and uniform subsequent tax declaration pertaining to income, net wealth and inheritance/donation to the tax authorities within this period should be granted impunity if the offences committed are those defined by §§ 396 and 402 AO. However, an additional payment will be levied further to the tax payable on income and net assets. If the subsequent tax declaration is submitted in the course of the year 2016, the penalty will amount to 10% of the additional tax payable. For disclosures made in the year 2017, the penalty will increase to 20% of the additional tax payable.

In order to benefit from the special conditions, such declarations have to be filed voluntarily and the underlying income and assets must not have been detected or disclosed yet nor form part of administrative or legal proceedings.

As from 1 January 2018, a voluntary disclosure to avoid penalties will no longer be possible.

For further information, do not hesitate to contact one of our team members, who will be glad to assist you at any time:

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[4] Abgabenordnung (General Tax Code)