Flash News

Proposed new IP regime in Luxembourg

On 4 August 2017, the Luxembourg government introduced a draft law (projet de loi no. 7163), which provides for the introduction of a new intellectual property regime (IP regime) in Luxembourg.

As a reminder, based on 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 old IP regime was abolished with effect from 1 July 2016, respectively from 1 January 2017 for the determination of business assets (taxpayers who already applied the former IP regime could however continue to benefit from the IP Regime for a transitional period of 5 years starting on 1 July 2016 and ending on 30 June 2021).

As already earlier announced by the government, the new IP regime shall comply with the new international standards and the OECD recommendations by applying the so-called "Nexus Approach" which requires a direct link between expenses, the IP right and the respective income.

It is intended that the provisions on the new IP regime will become effective as from 1 January 2018. Similarly to the old rules, the new IP regime shall also provide for an 80% tax exemption of the net income and capital gains generated by specific qualifying IP rights. These qualifying IP rights shall also benefit from a 100% exemption from net wealth taxes. In case a taxpayer qualifies for the transitional rules of the old IP regime and the new IP regime, he may irrevocably opt to apply the new system.

Compared to the old regime, the scope of qualifying IP will be more restricted in the new regime ***(reduced scope)***. Whereby e.g. protected patents, utility models and software protected by copyrights will still qualify for the new IP regime, while trademarks, domain names and other marketing related rights will not qualify anymore.

Also, the basis for the exemption will be different ***(distinct basis for 80% exemption)***. In order to apply the 80% tax exemption, the respective net income needs to be determined. Such income is then multiplied with a specific cost ratio. The resulting amount is then the eligible income, of which 80% is tax exempt.

When determining the basis for the exemption, all expenses directly linked to the R&D, development or improvement on the qualifying IP assets and incurred by the taxpayer (including its permanent establishment located in the EEA) or outsourced to third parties, represent qualifying expenses. In this context it is important to mention that the expenses not directly linked to the qualifying IP have to be disregarded. This is also the case for acquisition costs, interest and other financing costs as well as building costs.

The specific ratio referred to above represents the proportion between qualifying and total related expenses whereby the qualifying expenses may be calculated with an up-lift of 30% (capped at the total expenses). In other words, if the total expenses consist exclusively of directly linked IP expenses, the total qualifying net income can be exempt by 80%, otherwise only a part of the net income will benefit from the 80% exemption.

In principle, the direct link needs to be evidenced per IP right (under certain circumstances a product based approach may be allowed). Positive and negative net income of qualifying IP rights have to be set-off against each other before applying the tax exemption. This applies also to negative net income still existing from prior years.

Qualifying IP income includes royalties, capital gains and IP income embedded in sold products and services as well as certain indemnities in relation to the qualifying IP.

IP rights to be registered may apply the tax exemption as from the year when filing the application. In case of a subsequent non-registration the exempt amounts have to be reintegrated in the result of the year in which the taxpayer is informed about the rejection of the registration.

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

Partner	**Michael Probst**	**Phone: +352 26 86 63-318**
Directors	**Christel Begué**	**Phone: +352 26 86 63-325**
	Alexia Christodoulou	**Phone: +352 26 86 63-321**
	Matthias Gutknecht	**Phone: +352 26 86 63-330**

*   *   *