Flash News

Tax Reform 2017

On 14 December 2016, the draft bill no. 7020 on the 2017 tax reform was approved by the Luxembourg Parliament and subsequently adopted on 23 December 2016[1]. The tax measures concern individuals as well as corporations and most changes are in accordance with the announcements made by the Prime Minister on 26 April 2016.

We are pleased to summarize hereafter the major tax changes for individuals and corporations which are, in principle, applicable as from 1 January 2017.

Individuals

In terms of personal income taxation, the main focus is on the relief of the middle class. The most important changes for individual taxpayers are the following:

Modifications of the income tax scale

Two new top tax rates have been introduced. The new tax rates for individuals in tax class 1 are 41% on income exceeding EUR 150,000 and 42% on income exceeding EUR 200,004 (plus contribution to the employment fund). Before, a maximum tax rate of 40% (plus contribution to the employment fund) was applied in these cases.

Changes in relation to real estate

The ceilings for mortgage interest deductions related to the individual's main residence increased from EUR 1,500 to EUR 2,000 for the first year of occupation and the following five years, from EUR 1,125 to EUR 1,500 for the next five years and from EUR 750 to EUR 1,000 for the subsequent years.

Rental income arising from approved social organizations will be tax exempt by 50% in order to stimulate the supply of social housing.

The taxation of deemed rental income of the owner's main residence has been abolished.

The contributions to a home savings scheme (contrat d'épargne-logement) is now tax-deductible up to EUR 1,344 instead of EUR 672 for individuals aged between 18 up to 40 years. For individuals older than 40 years, the maximum tax deduction remains EUR 672.

[1] Published in Mémorial A – No. 274, p. 5139 on 27 December 2016

Increase of the individual's household purchasing power

The tax credit for employees, for pensioners and for self-employed individuals has increased up to EUR 600 per year for gross salary/pension or net income between EUR 11.265 and EUR 40.000. For gross salary/pension or net income between EUR 936 and EUR 11.265, the tax credit is calculated in function of the gross salary/pension or net income and ranges between EUR 300 and EUR 600. For income or pensions between EUR 40.001 and EUR 79.999, the tax credit is calculated in function of the gross salary/pension or net income and ranges between EUR 600 and EUR 0. For an annual income higher than EUR 80,000, the tax credit will no longer be granted.

The tax deduction for contributing to the education and maintenance costs of a child that is not part of the taxpayer's household has been increased from EUR 3,480.00 to EUR 4,020.00 per child and per year.

The lump-sum allowance for domestic fees (e.g. cleaning lady or childcare) has been increased from EUR 3,600 to EUR 5,400 per year.

The face value of the luncheon vouchers has been increased from EUR 8.40 to EUR 10.80. However, the taxable fringe benefit of the employee does not increase correspondingly and remains at EUR 2.80.

Single parents whose annual taxable income does not exceed EUR 35,000 enjoy a tax credit of maximum EUR 1,500 instead of EUR 750 per year. This credit remains at EUR 750 when the annual taxable income exceeds EUR 105.000. For taxable income between EUR 35.000 and EUR 105.000 the tax credit is calculated in function of the taxable income and ranges between EUR 750 and EUR 1.500. The tax credit for single parents is not granted if the single parents live with the child in a common domicile.

Private old-age pension plan

For all tax payers, there is now an annual tax deduction for private old-age pension plans with a maximum amount of EUR 3,200. Before, the deduction depended on the taxpayer's age and ranged from EUR 1,500 to EUR 3,200.

Special expenses

The ceilings for the deduction of debit interest payments and insurance premiums like death, accident or civil liability have been merged and are now limited to an aggregated maximum of EUR 672 per household member. Before, the deduction for debit interest payments was up to EUR 336 per household member and for insurance premiums it was up to EUR 672 per household member.

Temporary budget-balancing tax

The 0.5% temporary budget-balancing tax (for example on pensions, wages and salaries) has been abolished.

Final flat tax rate under the "RELIBI" law

Interest income paid by a Luxembourg or EU resident paying agent and received by a tax resident individual in Luxembourg was subject to a 10% final flat withholding tax under the so called "RELIBI Law". This final flat withholding tax has now been increased to 20%.

<u>The following tax changes will be applicable starting **1 January 2018**</u>

Optional separate taxation regime for married couples and registered partners

As of the tax year 2018, resident and non-resident married taxpayers will have the choice to be taxed separately or jointly. If married taxpayers opt for a separate taxation, they are assigned to tax class 1. Accordingly, each type of remuneration is allocated individually and the deductions and potential increase of ceilings with dependent children would be split equally between the spouses.

Moreover, the married taxpayers as well as registered partners will be able to apply for an individualization with reallocation of income. If not otherwise indicated, the total adjusted taxable income will be allocated equally between the spouses irrespective of the level of their respective income.

In order to be effective for the tax year concerned, the request to be taxed individually is irrevocable and has to be filed jointly in the previous tax year, except for couples who get married or become Luxembourg tax residents during the year. In these cases, there is an additional deadline up to 31 December of the same year in order to get taxed separately.

In case of a separate taxation, each spouse is allocated to tax class 1 and receives a separate assessment notice. In case one spouse objects to a joint filing, the tax authorities will automatically conduct a separate taxation.

Change of taxation of non-resident married couples

As of 1 January 2018 as well, non-resident married couples will be taxed by default in tax class 1, unless they are subject to tax in Luxembourg for at least 90% of their worldwide income and apply for a taxation as if they were tax residents. In this case, they can keep the beneficial tax class 2. However, then they also have to report their tax exempt non-Luxembourg income which will be taken into consideration for the determination of their global tax rate (taxation under progression). Upon request, this option is also available in case only one spouse meets the 90% threshold with his or her total income.

Corporations

Reduction of the corporate income tax rate

According to the new measures, it is foreseen to reduce the corporate income tax rate over the years 2017 and 2018 from 21% to 18%. The solidarity surcharge tax on the corporate income tax or the municipal business tax has not been amended.

The tax rate for companies with a net tax base of more than EUR 30,000 is reduced to 19% for the tax year 2017 and to 18% for the tax year 2018. For companies with a net tax base between EUR 25,000 and EUR 30,001, the corporate income tax is composed of EUR 3,750 plus 39% of the tax base above EUR 25,000 for the tax year 2017 and EUR 3,750 plus 33% of the tax base above EUR 25,000 for the tax year 2018. For companies with a tax base of less than EUR 25,000, a reduced corporate income tax rate of 15% is applicable for the year 2017 onwards.

Consequently, the global tax rate (corporate tax, solidarity surcharge tax and municipal business tax for Luxembourg-City) for 2017 is 27,08% and 26,01% as from 2018.

Restrictions on future tax loss carry forwards

As from the tax year 2017 on, there now exists a restriction on the use of losses carried forward for corporate income tax as well as for municipal business tax purposes. Losses may still be carried forward but for a maximum period of 17 years instead of an unlimited period of time. The limitation in time does, however, not apply to losses which have arisen prior to the tax year 2017. The oldest tax loss carry forwards have to be used first.

Minimum net wealth tax

As already reported in our Newsletter about major tax changes 2016, a minimum net wealth tax charge was introduced on 1 January 2016, replacing the minimum tax for corporate tax purposes. The new tax measures have increased the minimum amount from EUR 3,210 to EUR 4,815 (including solidarity surcharge tax) for holding and finance companies (sum of transferable securities, cash at bank, intra-group receivables and fixed financial assets exceeding EUR 350,000 and 90% of their total gross assets) as from the financial year 2017.

The minimum tax amounts for companies not falling in this category remain unchanged.

Investment tax credits

The complementary investment tax credit increased from 12% to 13%.

At the same time, the global investment credit increased from 7% to 8% whereas the tax credit for investments exceeding EUR 150,000 remains at 2%.

For assets which fall under a special depreciation regime, the investment tax credit increased from 8% to 9% whereas the tax credit for investments exceeding EUR 150,000 remains at 4%.

Electronic filing of corporate tax returns

As from the tax year 2017 on, it is mandatory to file the corporate tax return electronically.

Other tax measures

The tax deductibility for provisions for the Deposit Guarantee Association in Luxembourg (Association pour la garantie des dépôts, Luxembourg – AGDL), which financial institutions could set-up, has been abolished. Existing provisions can be reversed during a transition period, at the latest until the end of the tax year 2026. However, the reversed amount has to correspond at least to the amounts contributed to the “Fonds de guarantie des dépôts Luxembourg” and the “Fonds de resolution Luxembourg” in the same tax year.

As from the year 2016 (retroactive application), the deferred taxation of foreign-exchange gains on certain assets denominated in a foreign currency is extended to all companies. Before a respective provision could only be set up by banks, insurance or finance companies.

Under certain conditions taxpayers can, upon request, defer the deduction related to the depreciation of a fixed asset. The deferral can be done at the latest until the end of the depreciation period.

A tax deferral may now be granted in the framework of the transfer of a family business. Realized capital gains linked to real estate assets (land and building) can, in this case, be treated as tax neutral.

The registration duty of 0.24% on transfers of claims has been abolished.

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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