

TAX

TAXATION APPLICABLE TO COMPANIES

2021 - LUXEMBOURG

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THE MAIN DIRECT TAXES IN FORCE AS AT 1ST JANUARY 2021

THE PROFITS OF COMPANIES ARE USUALLY TAXABLE AT AN EFFECTIVE RATE OF 24.94%. THIS RATE IS THE RESULT OF THE CUMULATION OF TWO TAXES:

- the corporate income tax;
- the municipal business tax.

CORPORATE INCOME TAX (CIT)

The applicable rates for CIT purposes are the following:

Total taxable income	Applicable rates
≤ to EUR 175,000	Rate of 15% applicable to the total taxable income
EUR 175,001 – EUR 200,000	Lump sum of EUR 26,250 plus application of a rate of 31% on the portion of the taxable income comprised between EUR 175,000 and EUR 200,000
> to EUR 200,000	Rate of 17% applicable to the total taxable income

The CIT rate is increased by 7% in favor of the employment fund, thus bringing it up to 18.19% for a normal CIT rate of 17%. CIT is not deductible from taxable profits.

MUNICIPAL BUSINESS TAX (MBT)

An allowance of EUR 17,500 is applied to taxable profits. The MBT applied to profits amounts to 6.75% in the municipality of Luxembourg and depends in the other municipalities on the municipal rates voted by them. MBT is not deductible from taxable profits.

EFFECTIVE RATE OF TAXATION

CIT before increase for employment fund	17.00%
+ Employment fund markup (7% of 17%)	1,19%
= Increased CIT rate	18.19%
+ MBT on taxable profits	6,75%
= Effective rate of taxation	24,94%

DETERMINATION OF TAXABLE INCOME

TAXABLE INCOME IS DETERMINED AS FOLLOWS:

- by adding to the book profit of the annual accounts the charges not deductible for tax purposes, such as excessive depreciations, provisions not allowed, directors' fees ("tantièmes"), fines, non-deductible taxes (CIT, MBT and NWT) etc.;
- by deducting all tax-exempt income (exempted by agreements to prevent double taxation, by the scheme applicable to parent companies and subsidiaries, or by the special scheme for income from intellectual property rights, repayments of non-deductible taxes, etc.) and losses that may be carried forward.

Tax losses incurred during financial years closing after 31 December 2016 may only be carried forward for **17 tax years** for CIT and MBT purposes. Tax losses realized during financial years closing between 1st January 1991 and 31st December 2016 may however be carried forward indefinitely. Tax losses are deductible in order of seniority meaning that the oldest losses should be deducted first.

INTEREST DEDUCTIBILITY LIMITATION

Further to the entry into force of the tax provisions linked to the transposition of the ATAD 1 directive, the deductibility of the interest charges will be capped to either 30% of the EBITDA (earnings before interest, taxes, deduction and amortization) or to EUR 3,000,000 €. SMEs are not concerned by this measure, which firstly targets MNE (for example EUR 3,000,000 interest correspond to an interest rate of 2% on a EUR 150 million debt / or 6% on a EUR 50 million debt).

The interest concerned are those linked to intra-group loans, to bank loans or to bond loans. This measure only concerns net interest (interest profits – interest charges) when these are negative (more interest charges than interest profits).

The tax-exempt revenues (typically the dividends / capital gains exempted under participation exemption regime) are not taken into account for EBITDA calculation (concept of "tax EBITDA"). This approach can reduce the result taken into account for EBITDA calculation (tax result and not accounting result) and decreases the amount of deductible interest.

A double deferral system also exists:

- For the unemployed deduction capacity on the one hand, when the 30% EBITDA or EUR 3,000,000 threshold is not met;
- For the non-deductible interest on the other hand, exceeding the 30% EBITDA or EUR 3,000,000 threshold.

Finally, some exceptions should be taken into account. There is no interest deductibility limitation in the following situations:

- For interest linked to loan agreements signed before 17 June 2016, provided that their T&Cs would not be significantly amended after that date (duration, interest rate, etc.);
- For the financial corporations: financing companies (back-to-back activity), insurance / reinsurance companies, banks, ManCos / Alternative Investment Funds (exemption based on the company's activity);
- For the companies part of an accounting consolidation, provided that their equity ratio would be at least equal to the equity ratio of the consolidated group.

An interest deduction can also be rejected in the context of anti-hybrid rules implemented via the transposition of the directives ATAD 1 and ATAD 2, in case of double deduction (in the payer's jurisdiction and in the beneficiary's jurisdiction) or of deduction (in the payer's jurisdiction) without inclusion (in the beneficiary's jurisdiction).

CREDITS SET OFF AGAINST CIT LIABILITY

Tax relief for investments;

- tax relief for the acquisition of software;
- tax relief for recruiting unemployed people;
- withholding taxes.

TAX CREDIT FOR INVESTMENTS

Tax relief for investments takes the form of a tax credit for investments in depreciable tangible assets booked in the balance sheet of a Luxembourg company other than buildings, farm stock and mineral or fossil deposits. The investment tax credit would be granted when in relation to eligible assets implemented within the territory of the European Economic Area provided that such investments are recorded in the balance sheet of a Luxembourg establishment.

This means that intangible investments goods, such as software, are not included (a special tax credit is available for software). The following goods acquired during the investment year are excluded from this tax relief:

- goods depreciable over a period of less than 3 years;
- used goods and goods acquired against payment by block transmission of an undertaking or part of an undertaking;
- passenger cars other than those used for commercial transport or rented out.

The tax credit for investment is broken down into two separate parts:

- tax credit for additional investment: **13%** of the additional acquisition value of the investments made in the course of the financial year;
- tax credit for global investment: **8%** for that part of the acquisition value of investments in the course of the year not exceeding EUR 150,000 and **2%** for that part of the investment exceeding EUR 150,000.

TAX RELIEF FOR THE ACQUISITION OF SOFTWARE

As its name suggests, this tax relief provides for a tax credit in case of acquisition of software. This regime can however not be combined with the tax relief for investments or with the draft new IP regime.

The tax relief for the acquisition of software is broken down into two separate parts:

- 8% rate for the part of the investment not exceeding EUR 150,000; and,
- 2% rate for the part of the investment exceeding EUR 150,000.

The tax relief can however not exceed 10% of the taxes due during the year when the software was acquired.

TAX RELIEF FOR RECRUITING UNEMPLOYED PEOPLE

Tax relief for recruiting unemployed persons takes the form of a tax credit of 15% of the amount of their gross pay for a period of 36 months starting with the month of their recruitment.

WITHHOLDING TAXES

Most taxes withheld at source constitute a down-payment on the income tax of the beneficiary, except for certain taxes withheld on interest in respect of individuals. Withholding taxes on bank interest paid to individuals are withheld by the paying agent while the other withholding taxes are withheld by the debtor.

Dividends paid by a Luxembourg company to a parent company resident in the Grand Duchy, another member state, or a state with which the Grand Duchy has concluded a tax agreement and whose taxation is comparable to that applied in the Grand Duchy (at least 8.5%), are exempt from withholding tax provided that the subsidiary has been held (or that the parent company undertakes to hold it) for at least 10% or for an acquisition price of EUR 1,200,000 for 12 continuous months. However, the exemption is submitted to additional anti-abuse requirements.

SALARIES, WAGES, PENSIONS AND ANNUITIES

Tax on these is withheld in accordance with the provisions of articles 136 to 145 of the law on income tax.

DIVIDENDS

- **15%** of the gross dividend;
- 17.65% of the net dividend.

These rates apply to resident taxpayers. For non-resident taxpayers, certain agreements to prevent double taxation may provide for lower rates. Under the scheme governing parent companies and subsidiaries, withholding at source is waived.

WITHHOLDING TAX ON INTEREST PAID TO RESIDENT INDIVIDUALS

A tax of 20% is to be withheld by the paying agent on certain interest paid to individuals who are resident for tax purposes in Luxembourg. In principle this withholding tax is a discharging tax.

DIRECTORS' FEES

- **20%** of the gross amount;
- 25% of the net amount.

Directors' fees ("tantièmes") are not deductible for tax purposes. The withholding at source of 20% constitutes a definitive taxation for non-resident taxpayers if their professional income in the Grand Duchy of Luxembourg exclusively comprises directors' fees whose annual gross amount does not exceed **EUR 100,000**.

PRACTICE OF AN INDEPENDENT ACTIVITY OF A LITERARY OR ARTISTIC NATURE OR A PROFESSIONAL SPORT ACTIVITY BY NON-RESIDENT TAXPAYERS

- 10% of the gross amount;
- 11.11% of the net amount.

These amounts withheld are only applicable to income allocated to non-resident taxpayers if the activity is or was carried out or exploited in the Grand Duchy of Luxembourg.

SCHEME APPLICABLE TO PARENT COMPANIES AND SUBSIDIARIES

Dividends received and capital gains achieved by a fully taxable resident company because of its participations are exempt if:

- the participation represents at least **10%** of the capital or the acquisition price is at least **EUR 1,200,000** for dividends or **EUR 6,000,000** for capital gains;
- the participation is maintained for at least 12 months or the company undertakes to maintain the participation for at least **12 months**;
- the participation is directly held in a fully taxable joint-stock company or through a “transparent” company.

If the participation is in a joint stock company not resident in the Grand Duchy of Luxembourg and not resident in a member state of the European Union, taxation comparable to that applied in the Grand Duchy (at least 8.5%) is required in the country of residence.

Participations that are exempt under the scheme for parent companies and subsidiaries are also exempt from net wealth tax.

The exemption is submitted to additional anti-abuse requirements.

SCHEME FOR INTELLECTUAL PROPERTY RIGHTS

The derogatory tax regime in force since 1st January 2018 provides for an **80%** exemption for CIT and MBT purposes of net eligible income related to eligible intellectual property (“IP”) rights. Those same assets are also exempt for net wealth tax.

Eligible IP rights consist of rights having been constituted, developed or improved after 31 December 2007 in the framework of research and development activities and notably include protected inventions (patents, utility models, etc.) and software protected by copyright. However, brands, designs or models as well as domain names are excluded.

Are considered as eligible income, royalties, capital gains on the disposal of IP rights, IP income embedded in the sale price and judicial indemnities. Also, net eligible income should in principle be determined for each eligible asset on an individual basis.

Eligible expenses must be directly related to the constitution, the development or the improvement of eligible IP rights and should, in principle, be carried on by the taxpayer himself.

They may however also be carried on by a permanent establishment of the taxpayer located in the EEA (under conditions) or be paid by the taxpayer to a third-party undertaking or to an affiliated undertaking (in the sense of article 56 I.T.L.), provided that said affiliated undertaking transfers the amounts received to a third-party undertaking without realizing a profit margin. Acquisition costs of the IP right itself or of the right to use said right, interests and financing costs, real estate costs as well as other costs not directly linked to an eligible asset are thus considered as non-eligible expenses.

Due to the provisions of the BEPS action plan, the exemption is nevertheless only available after the application of a ratio i.e., development costs directly related to the IP right (i.e. eligible expenses) / total costs, which is used as a substance indicator for the activity carried out in the country.

As a reminder, the previous tax regime regarding certain IP rights was repealed as of 1st July 2016 for CIT and MBT purposes and as of 1st January 2017 for net wealth tax purposes. However, IP rights acquired or developed before 1st July 2016 still benefit (under conditions) from a grandfathering period of 5 years expiring on 30th June 2021 (1st January 2021 for net wealth tax).

In all cases, both regimes are not cumulative and taxpayers eligible to both regimes should irrevocably opt for one of them.

INTERNATIONAL TAX

The Grand Duchy of Luxembourg has concluded many agreements to prevent double taxation, more particularly with all the member states of the European Union, most of the member countries of OECD and a number of other countries.

Luxembourg has also transposed the tax measures linked to ATAD 1 and ATAD 2 directives regarding (among others): anti-abuse rules (GAAR), Controlled Foreign Companies (CFC rules) and anti-hybrid instruments rules.

NET WEALTH TAX (NWT)

NWT is a tax calculated on the basis of the unitary value of the company which in theory corresponds to the net wealth of the company after making certain specific adjustments, particularly for property and participations. The decreasing rates applied to the unitary value is:

- **0.5%** on the part of the net wealth that is lower or equal to EUR 500,000,000;
- **0.05%** on the part of the net wealth that is higher than EUR 500,000,000.

The capital companies which are liable to NWT can obtain a reduction of the tax. In this regard, they have to create a legal reserve amounting to 5 times the requested reduction and to maintain it 5 years in the balance sheet.

However, the amount of the reserve is subject to two limits:

- the reserve is limited to 5 times the amount of the CIT of the previous year (employment fund contribution included and before application of the tax credits);
- the normal NWT reduced through the creation of a five-year reserve cannot be lower than the reduced minimum NWT.

NWT is not deductible from taxable profits.

MINIMUM NET WEALTH TAX

Minimum NWT of **EUR 4,815** (taking into account the employment fund contribution) applies for:

- companies resident in Luxembourg;
- therein the amount of financial assets, shares, intercompany receivables and cash at bank exceeds **90%** of the total of the Luxembourg balance sheet and an amount of **EUR 350,000**.

Generally speaking, with a view to greater clarity, the law expressly specifies the relevant accounts of the Standard Chart of Accounts, namely accounts 23, 41, 50 and 51, to which reference is to be made for the purposes of calculating the 90% ratio and the EUR 350,000 criterion.

However, if companies to which the minimum NWT figure of EUR 4,815 applies are principally "Soparfis" (sociétés de participations financières = companies carrying on the business of managing participating interests), a different minimum NWT tax amount is applied to entities which are not covered by the first tax.

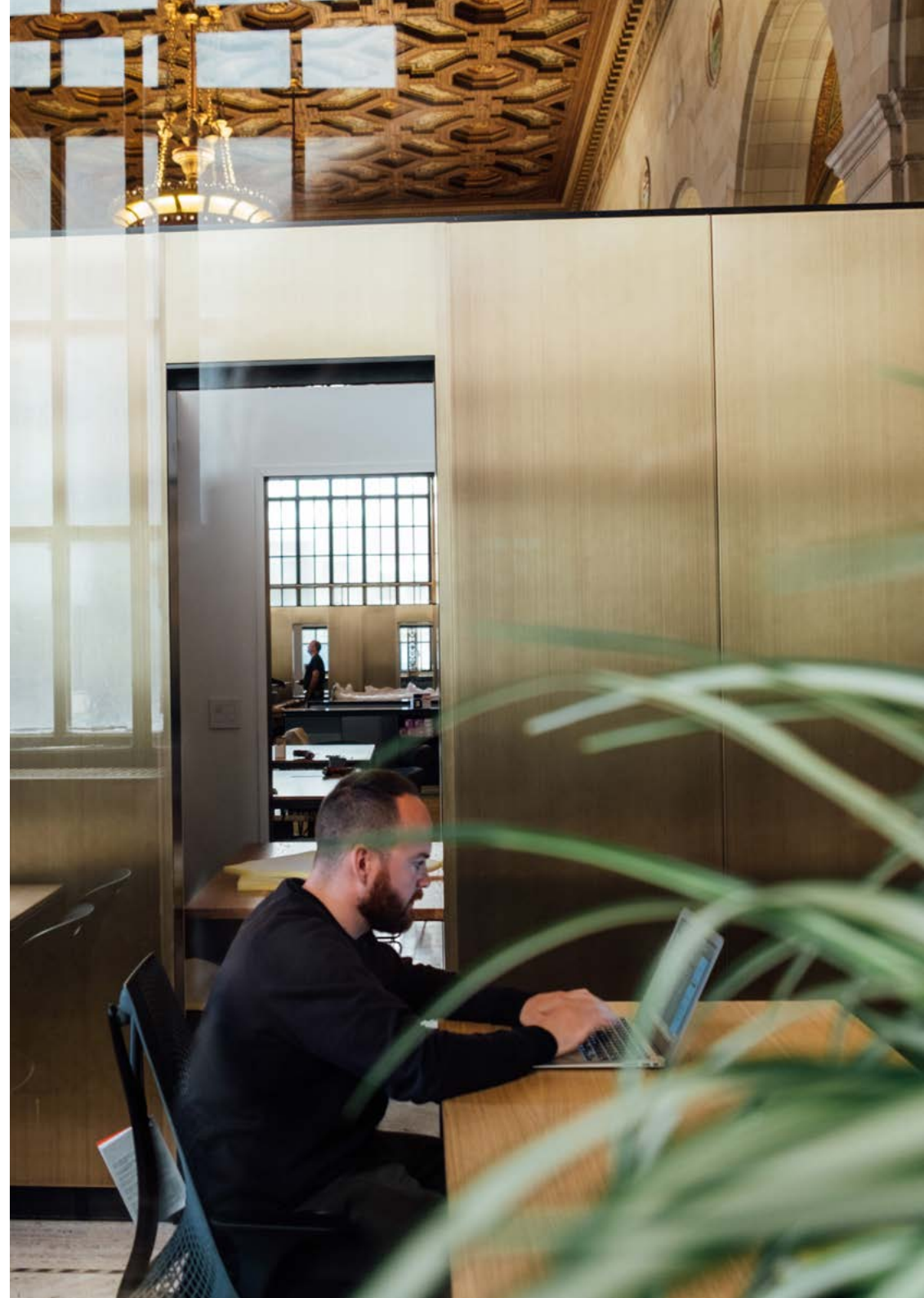
Thus, a commercial company will also pay a minimum NWT amount referable to its total balance sheet figure, as follows:

Minimum net wealth tax (including the contribution to the employment fund)	Total closing balance sheet figure
EUR 535	≤ EUR 350,000
EUR 1,605	EUR 350,001 – EUR 2,000,000
EUR 5,350	EUR 2,000,001 – EUR 10,000,000
EUR 10,700	EUR 10,000,001 – EUR 15,000,000
EUR 16,050	EUR 15,000,001 – EUR 20,000,000
EUR 21,400	EUR 20,000,001 – EUR 30,000,000
EUR 32,100	> EUR 30,000,000

Securitization companies, SICARs, SEPCAVs and ASSEPs are exempt from NWT with the exception of the minimum NWT.

Please note that the assets whose income is taxable in another country in application of a Double Tax Treaty have to be deducted from the total balance sheet figure (i.e. income derived from a building situated in another country). The same applies for the total balance sheet to be considered in order to determine if the financial assets exceed the 90% and EUR 350,000 threshold.

The applicable minimum NWT may however be reduced by the amount of CIT of the previous year (employment fund contribution included and after application of potential tax credits).



THE MAIN INDIRECT TAXES AS AT 1ST JANUARY 2021

VAT

The VAT rates in the Grand Duchy of Luxembourg are:

- standard rate: **17%**;
- intermediate rate: **14%** (custody and management of securities, printed advertising material, heat not provided by heating network, cold, etc.);
- reduced rate: **8%** (gas, electricity, floriculture, hairdressing, etc.);
- super-reduced rate: **3%** (books, hotel accommodation, restaurants and non-alcoholic beverages, radio and television broadcasting services, etc.).

These VAT rates are among the lowest in Europe. In principle, the reverse charge in the scope of the VAT registered service receiver is the rule (B2B).

The right of deduction is particularly attractive as there is no specific limit on the entitlement to deduct VAT from operating expenses. VAT legislation also provides for a number of attractive special schemes.

Examples:

- exemption for the management of investment funds ("OPC");
- entitlement to opt for VAT to be applied to certain sales or rental agreements in respect of real estate theoretically exempt from VAT, resulting in the owner of the real estate being entitled to effect deductions;
- super-reduced rate of 3% for the renovation of accommodation to be used as a principal residence;
- super-reduced rate of 3% for the construction of accommodation to be used as a principal residence by its owner;
- super-reduced rate of 3% for radio and television broadcasting services;
- special scheme of taxation of the profit margin on certain goods;
- simplified regime for consignment stock / call of stocks.

Any person established in the Grand Duchy of Luxembourg starting a taxable activity must register for VAT if it is presumed that the annual turnover will exceed **EUR 35,000**. An entity subject to VAT established outside the Grand Duchy of Luxembourg must apply for direct registration for Luxembourgish VAT if it carries out operations within the Grand Duchy that are subject to Luxembourgish VAT for which the entity has to pay the tax, or "distance selling" operations for an annual amount in excess of EUR 100,000.

Entities subject to VAT that are not established in the European Union may be required to deposit a security or a bank guarantee to ensure payment of the tax.

Moreover, must register to VAT, any liable person established in Luxembourg who only realizes operations which do not grant the right to deduction as well as any non-liable company established in Luxembourg, whose intra-Community acquisitions do exceed an annual threshold of **EUR 10,000** during the previous civil year or during the civil year of the acquisition.

Finally, every person / company carrying out a VAT exempt activity (bank, insurance company) and being the service receiver of a foreign supplier must be registered to VAT. Indeed, in this case, VAT has to be self-assessed by the person / company.

TRANSFER TAX

A registration fee of EUR 75 is payable in respect of the following transactions involving Luxembourg companies:

- incorporation;
- transfer of registered seat (registered office or place of effective management) from another country to the Grand Duchy;
- amendment of the articles of association.

For the contribution to a company of immovable property located in the Grand Duchy, the following taxes are due:

- a transfer tax of 3,4% in case of contribution of an immovable property in exchange for shares
- a transfer tax of 7% in case of contribution of an immovable property not in exchange for shares (e.g. in exchange for cash).





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