

Luxembourg

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THE YEAR IN REVIEW

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by *Jurjan Wouda Kuipers and Xavier Picha*

Luxembourg's government announced several tax measures in 2010. If passed by the parliament, they will take effect January 1, 2011. Although they would mainly affect individual taxpayers, companies would also face a slightly higher overall tax rate. Some companies would have to pay a minimum annual tax of €1,575.

Throughout the year, however, Luxembourg has demonstrated its commitment to fostering an attractive investment climate. The government introduced guidance on Islamic finance arrangements and legislation further promoting Luxembourg as a platform for investment funds. Luxembourg also expanded its tax treaty network in 2010.

Proposed Corporate Tax Changes

Any Luxembourg company that does not require either a business license or the approval of a supervisory authority, and that owns financial assets (including participations, securities, and cash) exceeding 90 percent of its total assets, would be required to pay a minimum tax of €1,575 (corporate income and employment tax). The corporate unemployment fund contribution would be increased by 1 percent, increasing the overall tax rate for companies incorporated in Luxembourg City from 28.59 percent to 28.80 percent. The tax deductibility of large bonuses and "golden handshakes" will also be restricted. An increased special tax depreciation was introduced and will apply to some green investments, while an increased investment tax credit may be claimed for some eligible investments.

Proposed Individual Tax Changes

The highest individual income tax rate bracket will be increased by 1 percentage point to 39 percent. There will also be an increased contribution to the unemploy-

ment fund (of up to 6 percent) and a temporary crisis contribution of 0.8 percent. Deductions will be limited.

2010 Individual Taxation Changes

On July 26 the parliament approved a bill amending the tax laws to comply with the European Commission's request regarding the taxation of nonresident individuals. As of January 1, 2010, Luxembourg's progressive income tax rates apply equally to income realized by residents and nonresidents. The benefit for the first nontaxable income bracket is now also granted to nonresidents who derive at least 90 percent of their overall income from Luxembourg sources.

Self-Assessment Procedure

As of February 1, a self-assessment tax return procedure applies for Luxembourg resident companies. The tax authorities will raise tax assessments immediately on receipt of the tax return, based on the taxable profit reported. Once the initial assessment is issued, the tax authorities have five years to reassess or request more information based on a later detailed review of the return. (For prior coverage, see *Tax Notes Int'l*, Feb. 22, 2010, p. 651, *Doc 2010-3226*, or *2010 WTD 31-1*.)

Islamic Finance

The tax authorities issued a circular letter on January 12 outlining the tax treatment of Islamic financial instruments issued or held by Luxembourg entities. (For prior coverage, see *Tax Notes Int'l*, Jan. 25, 2010, p. 309, *Doc 2010-824*, or *2010 WTD 10-4*.)

Investment Funds

On August 11 a draft law was submitted to the parliament to implement the European Union's UCITS IV Directive; if enacted, the measure will take effect January 1, 2011. Exchange-traded funds would be exempt from the annual 0.5 percent subscription tax now imposed, while capital gains realized by nonresident investors in investment funds would also become fully exempt from Luxembourg income tax. Also, establishments for collective investment established outside Luxembourg but having their effective management center

or central administration located in Luxembourg would be exempt from Luxembourg corporate income tax, municipal business tax, and net worth tax. (See *Tax Notes Int'l*, Aug. 23, 2010, p. 586, *Doc 2010-17983*, or *2010 WTD 156-5*.)

Case Law

Losses incurred by a Luxembourg company can be carried forward indefinitely. However, it has long been unclear whether a Luxembourg company's losses generated from one activity can be offset against profits from another activity, if the other activity was initiated after a transfer of shares of the loss-making company to a third party. That was the topic of Luxembourg Administrative Court decisions on February 4 and July 15. (For prior coverage, see *Tax Notes Int'l*, Aug. 9, 2010, p. 433, *Doc 2010-17047*, or *2010 WTD 147-2*.) The tax authorities issued a circular on September 2 summarizing the court decisions and providing more guidance. It says the tax administration will not challenge the right to use losses carried forward by a Luxembourg company based solely on the fact that its shareholders have changed if its activities have continued or expanded. However, depending on the facts, the transaction can be challenged based on the abuse of law concept. The circular says that factors such as the termination of the activities that generated the losses, the absence of any valuable assets, and the transfer of shares closely following the termination of activities will all be considered.

Tax Treaties

To date, Luxembourg has concluded tax treaties with 60 countries, including five new treaties that became effective on January 1 (Azerbaijan, Georgia, India, United Arab Emirates, and Moldova). A new tax treaty with Panama was signed, and parliament approved treaties with Bahrain and Liechtenstein. Tax treaty negotiations with Lebanon, Pakistan, Serbia and Montenegro, Syria, and Uruguay are ongoing, and Luxembourg has initiated negotiations with the United Kingdom to amend the existing tax treaty.

Luxembourg is amending new and existing tax treaties to include the OECD standard clause on information exchange. New treaties with Armenia, Monaco, and Qatar that include the clause will become effective on January 1, 2011. Similar amendments to treaties with Austria, Denmark, Finland, Norway, Spain, and the United Kingdom will also become effective on the same date. Parliament has already approved protocols amending tax treaties with Belgium, France, Germany, Iceland, the Netherlands, Mexico, Switzerland, Turkey, and the United States. Amendments to existing treaties with Hong Kong, Japan, Portugal, and Sweden were also signed in 2010. ◆

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