VANDENBULKE
CORPORATE, FINANCE AND TAX LAWYERS

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LUXEMBOURG TAX REFORM COMES INTO PLAY

On 27 December 2016, the Tax Reform Law of 23 December 2016[1] was published along with a new transfer pricing circular on intragroup financial transactions. Our new tax update outlines the most relevant corporate tax measures for Luxembourg taxpayers in 2017.

Significant decrease in the corporate income tax rate

The corporate income tax rate will be reduced from 21% to 18% within the next two years. The decrease will lead to a maximum aggregate rate for corporate income tax, municipal business tax (Luxembourg City resident companies) and the contribution to the employment fund of 27.08% in 2017 and 26.01% in 2018.

Enlightenment about the use of carry forward losses

Although the preliminary proposals included a double restriction of (i) ten years and (ii) tax carry forward losses being offsetable only against 80% of the net taxable profits, the final bill sets out that losses generated during and after 2017 will be able to be carried forward for a maximum period of 17 years with no other particular limitation.

Additionally, the tax carry forward losses incurred during the previous fiscal years will be carried forward indefinitely by the taxpayer who suffered them.

New transfer pricing landscape

The Luxembourg tax authority issued a circular letter "L.I.R. n° 56/1 – 56bis/1" relating to the tax treatment of companies performing intra-group financing transactions (the "**New TP Circular**"). The New TP Circular, which is based on the article 56bis of the Luxembourg income tax act[2] repeals the two previous transfer pricing circular letters issued by the Luxembourg tax administration on 28 January 2011 and 8 April 2011.

The provisions of the New TP Circular letter bring a major degree of flexibility to the intra-group financing, in particular:

- The rule regarding the equity at risk of at least 1% of the principal amount of the loans, or EUR 2,000,000 has been removed;
- For simplification purposes also, if the remuneration earned by a Luxembourg company that acts as intermediary is not supported by a transfer pricing report, it is acceptable that the taxable result amounts to a minimum of 2% on the financed assets after taxes; and
- The substance requirements have been also further confirmed. In particular, the criteria of effective presence in Luxembourg requires that in order to bear the risk related to its financing activities, any Luxembourg company must have a majority of board members with the capacity to bind the Company resident in Luxembourg and also key decisions being taken in Luxembourg.

Increase in the minimum net wealth tax

A minimum net wealth tax charge was introduced as from 1 January 2016, which replaced the previous provision for the minimum corporate income tax for all corporate entities having their statutory seat or central administration in Luxembourg. This minimum tax applies

[1] *Law of 23 December 2016 implementing the tax reform of 2017.*
[2] *Amended law of 4 December 1967 relating to Income Tax Law.*

to companies dedicated to the holding and financing whose sum of fixed financial assets, intercompany loans, transferable securities and cash at bank (as reported in their commercial accounts presented in the standard Luxembourg form) exceeds both 90% of their total gross assets and EUR 350,000.

The minimum net wealth tax will increase in 2017 from EUR 3,210 to EUR 4,815.

Value added tax

New provisions have been introduced which render managers liable for the fulfillment of the VAT obligations, including the payment of the VAT due incurred by companies that they manage.

It is worth noting that the extension of liability to directors, receivers or right holders of VAT taxable persons that are in liquidation or bankruptcy have been finally relinquished from the scope of the above new measures.

Additional changes in the loop

Abolition of the ad valorem registration duty of 0.24% levied on the registration of a transfer of a claim i.e. deeds not subject to a registration obligation were nevertheless subject to registration duty when they were subsequently mentioned in, or attached to, deeds subject to the formality of registration; and

Corporate tax returns will no longer be filed by post but electronically.

Our comments

The new legislation is generally consistent with the bill on the implementation of the 2017 tax reform previously issued by the Luxembourg Government on 26 July 2016.

The new corporate tax package seeks to restore and upgrade the competitive tax framework in the country.

In principle, there is though still a significant path to excellence as some key proposals still remain under discussion such as the abolition of withholding tax on dividends and of net wealth tax, as well as an extension of the participation exemption regime.

We can however, beyond other advantages already into play, welcome such a significant reduction of corporate tax rate and the simplification of the new transfer pricing rules. This will partially relieve investors from heavy and costly transfer pricing arrangements when non substantial amounts are concerned.

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