CLIFFORD CHANCE

BUDGET 2021 LAW INTRODUCES NEW TAX MEASURES

The 2021 Budget Bill[1], as deposited by the Luxembourg government on 14 October 2020, proposes, among others, to introduce new tax measures impacting individual taxation, taxation of real estate, the fiscal unity regime, Value Added Tax ("**VAT**") and sustainability measures.

TAXATION OF REAL ESTATE

Real Estate Withholding Tax ("WHT)

The Budget Bill proposes a new non-deductible 20% WHT to be charged as from 1 January 2021 for certain types of Luxembourg real estate SIFs, RAIFs and Part II UCIs.[2] The new provision would target all rental and capital gains income from Luxembourg-based real estate held by SIFs, RAIFs and Part II UCIs (or through tax transparent entities such as FCP). Income from foreign real estate assets would remain out of scope from the 20% WHT.

Concerned taxpayers would need to declare their taxable income by 31 May 2022 and pay the tax by 10 June 2022. This applies also to taxpayers in scope of the provision but without any Luxembourg based real estate. The Budget Bill foresees a fine of up to EUR 10,000 for failing to satisfy the reporting requirements.

Restrictions on SPFs

In addition, Luxembourg SPFs (*société de gestion de patrimoine familial*) would no longer be allowed to hold or acquire real estate through transparent vehicles (i.e. partnership or FCP), applicable as of 1 July 2021.

Registration duty

The Budget Bill further aims to align the transfer tax treatment of asset deals and share deals (i.e. where real estate is contributed to a company whose shares are sold). As of 1 January 2021 the aggregated transfer tax would increase to 3.4% (from 1.1% - including 0,5 % registration fees increased by 2/10ths plus a 0.5% transcription tax). For real estate located in Luxembourg city, a 0.3% city surtax is to be added.

[1] Available in French at: https://www.chd.lu/wps/PA_RoleDesAffaires/FTSByteServingServletImpl?path=85D13F955F91FD856AAF8E92F87487FC3FAABAE9116DC25E9D14C6AB62C929005C56E0FC07A9E23BA6A5EF245A561EC0$DCAC34510A118AF16565DA7EBA4AE49E

[2] Refer to Finance Alert for further details: https://www.cliffordchance.com/client-portal/alerters/alerter-finance/2020/10/2021-budget-bill--new-real-estate-tax-for-certain-sifs--raifs-an.html

Depreciation rate applicable to real estate and VAT

Furthermore, the Budget Bill reduces the accelerated depreciation rate on real estate investments in rental properties to 4% (from 6%), applicable to real estate acquired or where the construction is completed after 01 January 2021. The time frame to use such accelerated depreciation rate is further reduced to 5 years.

For renovation work relating to sustainable energy measures on buildings older than 10 years (instead of 20 years) a super-reduced Value Added Tax ("**VAT**") rate would apply.

TAX CONSOLIDATION REGIME

Following the decision of the European Court of Justice (14 May 2020, C-749/18), concluding that the Luxembourg tax unity regime was not compliant with the EU freedom of establishment, the Budget Bill grants in the fiscal years 2020-2022 the possibility to switch from a vertical tax unity to a horizontal tax unity without triggering a retroactive cancellation of the existing tax unity (i.e. consequently without retroactive taxation).

The change is subject to certain conditions, such as (i) the integrating parent will become a subsidiary of the new fiscal unity group, (ii) a joint request by all members of the groups must be filed by the end of the relevant fiscal year, (iii) the new fiscal unity group must be larger than the dissolved fiscal unity, (iv) a dissolution of the new fiscal unity must be avoided for a period of five years.

VAT

Acknowledging Council decision 2019/2210 (19 December 2019), the VAT threshold for small enterprises would be increased (i.e. taxable persons with an annual turnover of up to EUR 35,000 are exempt from VAT).

SUSTAINABILITY

The Budget Bill introduces a CO2-tax which would lead to an increase in diesel and fuel prices (tax of approximately EUR 0.05/liter).

Furthermore, investment funds engaged with 5% of their assets under management in sustainable projects would benefit from a reduced subscription tax of 0.04% (instead of 0.05% - which can be gradually reduced down to 0.03%/0.02%/0.01% where qualifying investments reach 20%/35%/50%). Such investments would need to meet certain EU criteria.

INDIVIDUAL TAXATION

Tax Card

To digitalise the administrative process, tax cards will no longer be submitted in physical form as of 2022 but filed via a dedicated online system.

Inpatriate Regime

The Budget Bill aims at formalising the current inpatriate regime (Circular n°95/2 dated 27 January 2014) by amending Article 115 of the Luxembourg Income Tax Law ("LITL").

Inpatriates can benefit from an allowance that would be exempt at 50% from taxation (an amount of maximum 30% of the annual remuneration). This allowance would be equal to premium paid to the inpatriate compensating difference in living cost (and consequently inpatriate hiring expenses would be tax deductible business costs at the level of the employer). Amongst others, the regime would be open for annual remuneration of EUR 100,000 (instead of EUR 50,000) and the applicable period would be extended to 9 years.

Stock Options and Warrant Plans

Circular 104/2 dated 29 November 2017 concerning stock options and warrant plans would be repealed as of 1 January 2021. The regime would be replaced by a participative premium paid to employees. Such employees would benefit from a 50% tax exemption (to the extent certain conditions are met) and the premium would be considered as a tax deductible operating expense at the level of the employer (as foreseen by the amendment of Article 46 LITL).

By amending Article 95 LITL, the Budget Bill introduces the qualification as salaried income for such participative premium. The following conditions would need to be satisfied in order for the employee to benefit from the new regime:

Employee related conditions:

- the beneficiary must be an employee and receive an income from salaried occupation;
- the premium would not exceed 25% of the ordinary remuneration in the relevant fiscal year in which the premium is granted (based on the deemed gross salary, exclusive of the premium);
- the employee must be an affiliate of the Luxembourg (or another EU) social security system.

Employer related conditions:

- the employer generates income qualifying as commercial profit, agricultural profit or profit from a liberal activity;
- the employer keeps regular accounting (particularly in the year in which the premium is paid and in the previous year);
- A maximum of 5% of the profit in the preceding fiscal year can be allocated to the premium granted in a given fiscal year (i.e. 2020 for a premium allocated in 2021);
- The employer provides a list of nominated employees for such participative premium to the tax authorities (i.e. bureau d'imposition RTS, competent WHT office) in the relevant fiscal year (based on the parliamentary works, this should be communicated at the moment the premium is settled).

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