New Luxembourg government proposes tax reforms to attract business

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The newly composed Luxembourg government on 2 December 2013 published its coalition programme, including components of a fiscal policy intended to re-balance public finances through structural reforms.

The programme proposes to achieve the re-balancing by reviewing public expenses, supporting economic growth and reforming the tax system, but claims stability as a key principle of its tax policy. It would increase Luxembourg's VAT but keep it the lowest among EU members and not increase any other taxes. The programme is intended to attract new businesses and corporate headquarters to Luxembourg and to allow entrepreneurs to develop economic activities.

The government also proposed to strengthen Luxembourg's international role by extending its corporate governance and substance rules, developing comprehensive transfer pricing legislation in line with international standards and developing a uniform procedure for tax clearances. Some business tax provisions, such as the so-called participation exemption, the rules for intellectual property and the rules on functional currencies, would be amended to improve Luxembourg's appeal as the global or regional headquarters of multinational companies. Smaller companies would also be encouraged to invest in Luxembourg through other mechanisms intended to achieve sustainable economic growth.

The programme claims it would improve social justice by reviewing the tax laws for individuals, including personal allowances and the new government has announced it will not reintroduce the net wealth tax. It anticipates permitting spouses to elect to be taxed separately, which currently is not allowed.

Reinforcing tax revenues

The government's fiscal policy favours increasing tax revenues by improving economic growth, reinforcing tax collection, modernising the General Tax Law and reforming criminal tax laws. However, it considers tax increases other than the increased VAT rates – which it argues are unavoidable – to be measures of last resort.

The program suggests extending the direct and indirect tax self-assessment system to individuals and businesses. It would apply existing penalties for late filing and payment more systematically and commits the government to fighting tax fraud.

VAT rates would be increased to compensate for the anticipated diminishment of the tax base from e-commerce. However, the government committed to keeping the standard rate – currently 15% – the lowest within the EU.

International role

The new government hopes to develop Luxembourg as a prime location for business headquarters. A first step would be to reinforce the material and operational presence of companies and highly skilled workers in Luxembourg by extending current governance and substance rules.

To provide more transparency, coherency and certainty, the government would also develop comprehensive transfer pricing legislation in line with international standards. It would also expand Luxembourg's network of tax treaties.

The programme does not support a European financial transaction tax (FTT) as currently proposed. However, it supports a worldwide FTT, which would not discourage financial activities within the EU.

The new government plans to continue the former government's policy on information exchange, including participating in the work done within the European Union and the OECD, but it would expand automatic information exchange only in ways that ensure the stability and competitiveness of the financial sector.

Business taxation

To develop Luxembourg as a headquarters for multinational companies, the program proposes to modernise the participation exemption regime, amend the tax rules for intellectual property income and formalise the use of functional currencies.

Achieving sustainable economic development and growth includes sustaining small and medium-sized enterprises, so the programme would introduce deferred profits taxation through a special reserve for investment.

To strengthen the capitalisation of companies with shareholders equity, the government would introduce the concept of notional interest, allowing some companies to deduct a deemed interest expense that would be calculated on the amount of their capital.

Funds

The new government hopes to make Luxembourg the leading hub for alternative investment funds in Europe and to attract private equity funds. It would not increase subscription taxes for specialised investment funds (SIFs), including private equity, real estate and hedge funds setup as SIFs and undertakings for collective investment in transferable securities and would maintain the tax rules for *sociétés d'investissement en capital à risque* (SICARs).

Because the carried interest regime would apply to all new funds launched in Luxembourg, the government said it will become more efficient.

Tax advisers

To enhance professionalism and the reputations of the financial centre and of tax professionals, the government plans to introduce regulations on the authorisation and supervision of tax advisers.