

Human Resource Services

Luxembourg income taxes 2008: guide for individuals

Income Tax

Resident vs. Non-resident

Luxembourg tax liability applies to Luxembourg residents on their worldwide income and to Luxembourg non-residents on their Luxembourg source income.

Resident taxpayer

An individual taxpayer qualifies as a resident of Luxembourg provided that he has his tax domicile or usual abode in Luxembourg. Nationality is irrelevant in order to determine tax residence. The tax domicile is defined as a permanent place of residence that the individual actually uses and that he intends to maintain. Individual taxpayers who do not have their tax domicile in Luxembourg will qualify as residents of Luxembourg if they have a usual abode in Luxembourg. Such a usual abode is deemed to exist after a continuous presence in Luxembourg of 6 months (short absences being disregarded). The underlying 6-month presence can overlap two calendar years.
Tax residence applies as from the first day of presence.

Non-resident taxpayer

An individual taxpayer qualifies as a non-resident of Luxembourg where he has neither his tax domicile nor his usual abode in Luxembourg.

Income subject to taxes

Income subject to tax notably includes professional, investment and real estate income, and capital gains. The categories of income, after deduction of related expenses, are aggregated in order to determine the "net" total income. Said "net" income is then reduced by various deductions so as to determine the taxable income. Non-resident taxpayers are in principle not entitled to the whole range of deductions available to Luxembourg resident taxpayers. Non-residents taxable in Luxembourg on more than 90% of their worldwide professional source income can opt to be treated as if they were Luxembourg residents. Concerning Belgian residents, the option regime can be applied as soon as a threshold of 50% of the professional income is reached. The tax benefit of the option regime has to be considered on a case-by-case basis.

Tax year

In Luxembourg, the tax year corresponds to the calendar year.

Income tax rates

Income tax rates are progressive. They vary from 0% up to 38%. A 2.5% surcharge for unemployment fund applies so that the marginal income tax rate amounts to 38.95%.

Filing jointly

Married taxpayers file jointly (with specific conditions to be met for non-residents). Civil partners living together for a full tax year can elect (under certain conditions for non-residents) to file jointly.

Tax classes

Luxembourg income tax liability is based on the individual's personal situation (e.g. family status). For the latter purpose, individuals are granted a tax class. Three tax classes have been defined: tax class 2 (the most advantageous), tax class 1.a (intermediate), and tax class 1 (the least advantageous).

	Residents	Non-residents
Tax class 2	Married taxpayers (even if wedding or divorce during the calendar year)	Same as residents if not living apart and taxable in Luxembourg on more than 50% of their household's total professional income
	Widowed persons for the 3 years following the year in which they became widowed	Same as residents[1]
	Divorced or separated individuals for the 3 years following the year of divorce or separation	Same as residents[1]
	Civil partners who live together for a full tax year and elect to file jointly.	Same as residents if the Luxembourg professional income derived by either partner exceeds 90% of his/her professional income in Luxembourg over the tax year.
Tax class 1.a	Widowed persons not included in tax class 2	Same as residents[1]
	Individuals aged at least 65 on January 1	Same as residents[1]
	Single parents	Same as residents[1]
		Married taxpayers not living apart and taxable in Luxembourg on 50% or less of their household's total professional income
Tax class 1	Taxpayers not included in tax classes 2 or 1.a	Same as residents[1]

Tax liability depending on tax class	Yearly net taxable income			
	EUR 25,000	EUR 50,000	EUR 100,000	EUR 150,000
Tax class 1	EUR 2,316	EUR 11,146	EUR 30,621	EUR 50,096
Tax class 1.a[2]	EUR 716	EUR 9,917	EUR 29,392	EUR 48,867
Tax class 2[2]	EUR 372	EUR 4,633	EUR 22,293	EUR 41,768

Employment income

Taxable employment income generally includes all benefits in cash or in kind received within the context of an employment activity. The taxable value of benefits in kind is in principle assessed at the fair market value (i.e. costs that the employee would have incurred should he have acquired the benefit himself).

Luxembourg Income Tax Law, however, provides for a lump sum valuation method or exemptions for certain benefits in kind:

- **Luncheon vouchers**
  The taxable benefit per voucher is equal to EUR 2.80 for a voucher value of EUR 8.40 maximum. The taxable basis is reduced to the extent that the employee participates in the related cost.
- **Company car**
  The taxable fringe benefit generated by the private use of a company car is equal to the private mileage multiplied by the kilometre cost of the car. A logbook indicating private mileage is to be held by the employee. For practical reasons, a lump sum evaluation is authorised. Based on the latter evaluation method, the monthly taxable fringe benefit corresponds to 1.5% of the listed price of the new vehicle (options and VAT included).
- **Free accommodation**
  The taxable fringe benefit amounts to the monthly rent and other rental charges paid by the employer. A reduction of taxable monthly rent to 75% is applied, subject to certain conditions (the reduction does not apply to the other rental charges).
- **Interest free (reduced) rate loan by the employer – Interest subsidy by the employer**
  A loan granted by the employer at an interest rate lower than 3.75% (rate applicable in 2008) generates a taxable fringe benefit. The taxable benefit corresponds to the difference between this 3.75% rate and the discounted interest rate. Interest subsidy by the employer applies where the employer provides financial support in respect of the interest charges related to a loan that his employee took out with a third entity. The interest subsidy by the employer generates a taxable fringe benefit in the hands of the employee.
  The above benefits are tax-exempt up to EUR 3,000 for mortgage loans for the acquisition of the main residence and up to EUR 500 for other personal loans. These tax-exempt amounts are doubled for married taxpayers file jointly and single taxpayers with dependent children.
- **Occupational pension schemes**
  Employer's contributions to a qualifying occupational pension scheme are subject to a flat tax rate of 20% to be borne by the employer[3]. Benefits received are tax-exempt.
- **Specific income tax exemptions**
  - Gifts by the employer based on the employee's seniority with the company. The said exemption varies between EUR 1,120 and EUR 4,500.
  - Overtime pay and extra pay for working nights, Sundays or on public holidays.
  - Severance pay (conditions).

[1] If they derive professional income taxable in Luxembourg.
[2] A tax bonus of EUR 922.50 per year and per dependent child is granted to (most) taxpayers by the "Caisse Nationale des Prestations Familiales".
[3] An additional tax of 0.9% assessed on the same basis has to be paid by the employer.

Deductible items

Professional expenses
Professional expenses related to the acquisition of employment income are tax deductible. A yearly lump sum deduction of EUR 540 is available. The said deduction can be replaced by effective expenses incurred (evidence is then required). Commuting expenses are deductible based on the distance between the employee's home and work place. On a yearly basis, the minimum deduction available amounts to EUR 396 and the maximum deduction to EUR 2,970.

Special expenses
1. **Mandatory social security contributions**
   Mandatory social security contributions paid to the Luxembourg social security scheme and contributions paid to a foreign State scheme further to a social security treaty application.
2. **Gifts (*)**
   Gifts made to a qualifying institution are tax deductible if total yearly gifts amount at least to EUR 120. Tax deductibility is limited to EUR 500,000 and 10% of the total net income.
3. **Voluntary contributions to an occupational pension scheme**
   Employee's voluntary contributions to an occupational pension scheme set up by the employer are tax deductible up to EUR 1,200 (yearly ceiling).
4. **Lump sum deduction**
   A yearly lump sum deduction of EUR 480 is available for employees (deduction is doubled for married taxpayers file jointly who both derive employment income).

The said lump sum deduction can be replaced by the following actual deductions:

	Yearly limit
Alimony paid to a divorced spouse (*)	EUR 21,600
Interest payments[4] (*)	EUR 672
Insurance premiums[4] (*) life, death, disability, accident, sickness, civil liability	EUR 672
Contributions to home ownership savings plan[4] (*)	EUR 672
Private old-age pension scheme[5] (*)	from EUR 1,500 up to EUR 3,200
Single death insurance premium related to a mortgage loan[6] (*)	EUR 3,000

Extraordinary charges (*)
Extraordinary charges are tax deductible provided that they exceed a percentage of the taxpayer's taxable income. The said percentage will vary based on the taxpayer's taxable income and his tax class. Alternatively, costs for child care, for household employees, and home assistance for the disabled are also deductible. The deduction is subject to a cap of EUR 3,600 on a yearly basis.

Single parent deduction
Single parents with dependent children may claim a yearly tax deduction amounting to EUR 1,920.

Education and maintenance costs – Non-dependent children
Education and maintenance costs paid for children who do not qualify as dependent can be tax deductible up to EUR 3,480 per year and per child.

Compensatory deduction for employees
Employees are entitled to a EUR 600 tax deduction on a yearly basis (applicable to each married spouse deriving a taxable salaried income).

Extra-professional deduction
Married taxpayers are entitled to a EUR 4,500 tax deduction on a yearly basis provided that they are file jointly and both derive professional income taxable in Luxembourg.

Dividend and interest income

A 15% withholding tax applies on Luxembourg domestic dividends (this withholding tax is not in full discharge). For final taxation, dividend income is subject to progressive income tax rates. A 50% tax exemption can be obtained on dividend income paid by a fully taxable company resident in a European Union Member State or a State that has concluded a tax treaty with Luxembourg.

Interest paid or attributed to Luxembourg resident individuals by a paying agent located in Luxembourg is subject to a 10% withholding tax which is in full discharge in the hands of the taxpayer. Interest payments which do not fall within the scope of the 10% withholding tax (e.g. income received from a UCIT, interest paid by a foreign paying agent,...) continue to be subject to a final taxation according to progressive income tax rates. A total lump-sum deduction of EUR 1,500 (doubled for married taxpayers taxable jointly) applies on total dividend and interest income (subject to final taxation) received during the tax year.

Capital gains on real estate

The capital gain on the sale of the taxpayer's main residence is tax-exempt. The capital gain on other real estate property:
- is subject to progressive income tax rates if disposal takes place within 2 years of acquisition;
- is subject to a reduced tax rate if disposal takes place more than 2 years after acquisition. The said reduced tax rate will not exceed 19.475%. A tax deduction of up to EUR 50,000 (doubled for married taxpayers and civil partners filing jointly) valid every ten years may be claimed on the capital gain. The said tax deduction may also be increased by EUR 75,000 for inherited property (heir of line).

(*) Tax deductible items for non-residents to the extent that they opt to be treated as Luxembourg tax residents.
[4] Increased by EUR 672 for jointly taxable married taxpayers and each dependent child.
[5] The tax deduction limit is determined based on age. The said deduction is doubled for married taxpayers taxable jointly who both took out a private pension insurance scheme.
[6] The said deduction can be increased based on the individual's personal situation (age, number of dependent children).

Under specific conditions, taxation of capital gains from the disposal of property can be deferred to the extent that it is used to fund the acquisition of a new property located in Luxembourg, which the owner intends to put up for rent.

Capital gains on shares

	Income tax regime
Short-term capital gains Shares are disposed of within 6 months of the acquisition date	Taxation based on Luxembourg progressive income tax rates (max. 38.95%) if total gain of the year amounts at least to EUR 500.
Long-term capital gains Shares are disposed of more than 6 months after the acquisition date	Capital gain is tax-exempt if the taxpayer does not hold a major shareholding (10%). Capital gain is taxed at a reduced tax rate (max. 19.475%) if the taxpayer holds a major shareholding (10%). A tax deduction of up to EUR 50,000 valid every ten years may be claimed on the capital gain (doubled for married taxpayers and civil partners filing jointly).

Directors' fees

Gross directors' fees, whether they are paid to a resident or a non-resident director, are subject to withholding tax at the rate of 20%. The 20% tax is used as a tax credit against final income tax liability assessed on the basis of an income tax return.
The 20% tax withheld is in full discharge in the hands of non-resident directors if (i) their gross directors' fees do not exceed EUR 100,000 and if (ii) they have no other Luxembourg source professional income. However, said directors may opt to file an income tax return. In the scope of an individual income tax return, tax is assessed pursuant to progressive income tax rates (max. 38.95%). For non-resident directors, the minimum rate is of 15.375% on net directors' fees. The opportunity to apply for the income tax return has to be considered on a case-by-case basis. Please note that directors' fees paid to non-resident directors by a billionaire holding company are tax-exempt.

Income tax return

In Luxembourg, not all taxpayers are subject to an income tax return filing obligation. Those who are must file their annual income tax return prior to March 31 of the year following the income tax year (extension is possible upon request). Should the taxpayer not be subject to a filing obligation, he may request a yearly calculation to the extent that certain conditions are met. The purpose of such a request is to obtain a refund of excessive payroll taxes (if any). The said request must be filed prior to December 31 of the year following the income year.

Please note that the aggregated elements to be taken into consideration in order to determine if a taxpayer is liable to file an income tax return or request for a yearly calculation are:
- His/her residence status;
- His/her tax class;
- His/her level of income;
- The nature of income;
- The number of days worked in Luxembourg.

Luxembourg social security contributions

Regular social security contributions

Regular Luxembourg social security contributions consist of an employer's and an employee's portion. Both are computed on a yearly gross remuneration capped at EUR 7,851.40 per month until the end of Februray 2008[7]. The following rates have been effective since January:

	Employee's portion	Employer's portion
Health		
• periodic remuneration	2.80%	2.80%
• non-periodic remuneration (e.g. bonus)	2.70%	2.70%
Pension	8%	8%
Accident	/	0.51% - 6%[8]
Health at work	/	0.10% - 0.11%[9]
TOTAL (periodic remuneration)	**10.80%**	**11.41% - 16.91%**

Mandatory social security contributions borne by the employee (employee's portion referred to above) are deductible for Luxembourg income tax purposes.

Dependency contribution

In addition to the above-mentioned regular social security contributions, employees are subject to a monthly contribution ("contribution dépendance") assessed on the gross remuneration decreased by EUR 4,808.94 per year for the year 2008.
This contribution amounts to 1.4%. Contrary to regular social security contributions, the dependency contribution is assessed on a basis that is not capped and it is not tax deductible.

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[7] EUR 8,047.66 per month as of March 2008.
[8] This rate varies depending on the sector of activity.
[9] Or EUR 40/year if the employer is registered to the ASTF.

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