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Luxembourg Tax Reforms Intend to Boost Corporate Competitiveness

- ***ATOZ Tax Advisers' Petya Dimitrova explains new tax measures***
- ***Government must monitor changes for long-term fiscal impact***

Luxembourg has introduced pivotal tax reforms aimed at reshaping its fiscal landscape and responding to global economic challenges, rising regional competition for talent and investment, and inflation-driven cost pressures.

The reforms are also important in the context of growing insecurity in neighboring jurisdictions and in the UK, where businesses and investors are increasingly uncertain about the tax environment.

The newly adopted measures include reductions in corporate taxes, enhanced personal income tax relief, and targeted incentives for attracting and retaining talent. Together, these changes underline Luxembourg's commitment to fostering growth and resilience in a competitive environment.

By balancing corporate tax cuts, targeted incentives for talent, and relief measures for residents, the government is positioning Luxembourg to remain competitive on the global stage.

Revamped tax incentives for high earners and young professionals, adjustments to personal income tax brackets, and clarified corporate tax rules are also part of the 2025 tax package.

Corporate Tax Overhaul

Luxembourg has reduced its corporate income tax rate from 17% to 16%, resulting in a decrease in the aggregate tax rate in Luxembourg City from 24.94% to 23.87%. This aligns the country with average corporate tax rates across the OECD, ensuring Luxembourg remains an attractive destination for multinational enterprises.

The coalition government has signaled its intention to further reduce the corporate tax rate up to an expected overall 5% depending on budgetary constraints, reinforcing the country's commitment to maintaining an attractive and stable fiscal framework.

An equity escape clause under the interest limitation rule is an important addition. This clause, applicable from Jan. 1, 2024, allows single-entity groups to fully deduct borrowing costs without limitation if they meet specific conditions. This rule is expected to target some securitization structures in Luxembourg.

Another change is the introduction of optionality in the participation exemption regime. This will allow eligible companies more flexibility when structuring their holdings to benefit from tax exemptions on dividends and capital gains, and is designed to enhance Luxembourg's attractiveness as a holding company jurisdiction.

Luxembourg has adjusted its minimum net wealth tax to ensure distribution of tax liabilities among corporations in accordance with the recent case law of the Luxembourg Constitutional Court in this respect.

The new rules refine the thresholds and calculations, ensuring that businesses contribute appropriately based on their financial position. These changes aim to balance Luxembourg's competitive tax environment with the need for sustainable public revenues.

Additionally, the new tax measures clarify the alphabet shares redemption system, ensuring clearer tax treatment for redemptions of the different share classes. This aims to improve transparency and provide greater certainty for companies that are structuring capital distributions.

Attracting, Retaining Talent

Luxembourg has simplified its impatriate tax system to make relocation more attractive for highly skilled workers. Starting in 2025, eligible employees who move to Luxembourg can benefit from a 50% tax exemption on their annual gross salary up to 400,000 euros ($415,000). The exemption is valid for up to nine fiscal years, provided the eligibility criteria are met.

This measure significantly reduces the tax burden on impatriates, making Luxembourg a competitive option for global talent.

The government also changed its profit-sharing bonus regime. Employers can now allocate up to 30% of an employee's annual gross salary as a tax-exempt bonus, up from the previous 25%. The maximum amount an employer can allocate to this bonus has risen to 7.5% of the previous year's profit, up from 5%. These changes encourage companies to share profits while providing additional tax savings for employees.

Young professionals can take advantage of a new partial tax exemption on bonuses. Workers under 30 who begin their first permanent job with a Luxembourg employer now can claim a 75% tax exemption on bonuses for five years.

Individual Tax Relief

To address the impact of inflation and improve residents' purchasing power, Luxembourg has again adjusted its personal income tax scale by 2.5 index brackets in addition to the four index brackets adjustments already effective from Jan. 1, 2024. This change, effective from 2025, is designed to offset the effects of automatic salary indexation and prevent individuals from being pushed into higher tax brackets due to inflation-driven wage increases.

Additional measures include expanded tax credits for single parents, minimum wage earners, and citizens aged 64 and older. These adjustments aim to provide greater financial relief to vulnerable groups, ensuring a more equitable distribution of benefits.

Collectively, the personal income tax adjustments and increased tax credits are set to enhance disposable incomes, boosting domestic consumption and supporting economic growth.

Luxembourg's 2024 tax reforms are expected to yield both short- and long-term benefits and foster a business-friendly environment intended attract further investment. However, the government will need to monitor the fiscal impact of these changes to ensure that public finances remain sustainable in the long run.

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