TAX REFORM 2025

On 17 July last, Minister for Finance Gilles Roth announced a **comprehensive tax reform to enhance the purchasing power of employees and the competitiveness of Luxembourg.** A bill has already been submitted to Parliament (No. 8414). We hereby present the aspects of the reform related directly to salary management, with the first part dedicated to measures for reducing the tax burden on households and the second part focusing on proposed changes to strengthen the country's attractiveness.

1 | REDUCTION OF TAX BURDEN ON HOUSEHOLDS

- **New adjustment of the personal income tax scale**

After an initial adjustment of the tax scale by 4 index brackets on 1 January 2024, the bill provides for a new adjustment of **2.5 index brackets** this time. In concrete terms, this means a tax reduction for all employees!

- **Additional tax relief for tax class 1a**

First of all, the bill proposes **a significant adjustment of the tax rate for class 1a** to bring the tax burden of this class closer to that of class 2.

Similarly, in order to ease the burden on single-parent households in particular, the **single-parent tax credit** is to be increased as follows:

  - For an adjusted taxable income of the taxpayer less than €60,000, the single-parent tax credit amounts to **€3,504** (compared with the current €2,505);

  - For an adjusted taxable income between €60 000 and €105,000, the single-parent tax credit amounts to € [3 504 – (adjusted taxable income – 60 000) x 0.0612];

  - For an adjusted taxable income of the taxpayer exceeding €105,000, the single-parent tax credit amounts to **€750.**

By way of reminder, the single-parent tax credit is granted by the tax authorities upon the taxpayer's request and under certain conditions. Depending on the cases, it will be applicable directly on the payslip, otherwise, it will be taken into account in the tax return.

- **Tax-exempt unskilled minimum social wage**

In a social and solidarity-oriented fiscal policy, the bill aims to **eliminate the tax burden for the minimum unskilled social wage earners** through the minimum social wage tax credit (MSWTC). The amounts will be as follows:

For a gross monthly salary or, where applicable, a fictitious gross monthly salary of :
  - from €1,800 to €3,000, the MSWTC amounts to **€81** per month,
  - from €3,000 to €3,600, the MSWTC is €81 / 600 x [€3,600 - (notional) gross monthly salary] euros per month".

This will concern employees in class 1 since, in practice, those in classes 1a and 2 on the minimum unskilled social wage already do not pay tax at this time.

The bill goes even further by providing an overcompensation on 1 January 2025 so that the tax burden on a minimum unskilled social wage earner remains zero even if an additional index bracket were to fall in 2025.

2 | STRENGTHENING THE ATTRACTIVENESS OF LUXEMBOURG

- **Enhancement of the profit-sharing bonus scheme**

Governed by Article 115 (13a) of the Tax Code and introduced by a law on 19 December 2020, this bonus allows employers to pay employees a **profit-sharing bonus that is 50% tax-exempt** when the company has made profits. The bill proposes **two important changes:**

  - One of the conditions for paying this bonus is that it must not exceed 25% of the employee's gross annual remuneration (before incorporation of benefits in cash and in kind) during the year in which the bonus is allocated. The bill proposes to increase this ceiling to **30%.**

  - Furthermore, the total amount of profit-sharing bonuses that employers can allocate to their employees and on which they can apply the 50% exemption is currently limited to **5% of the company's positive operating profit from the previous fiscal year.** The bill proposes to increase this percentage by 2.5 points, thus rising from 5% to **7.5%.**

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- **Modernisation of the expatriate tax regime**

In order to make the Luxembourg ecosystem more competitive against the backdrop of strong international competition for skilled labour, Luxembourg has for many years applied a favourable tax regime for impatriate employees under certain conditions.

Up to now, this regime offered a range of different exemptions based on actual expenses and an impatriation bonus from which the employer could freely choose. The idea of the bill is to modernise the impatriate tax regime so as to **facilitate its practical implementation** and thus offer companies a **simpler and more attractive tool** to attract talent to their companies. The new model thus provides a **flat-rate system** characterised by:

  - **A tax exemption of 50% of the total gross annual remuneration,**

  - While capping the annual remuneration amount eligible for this exemption at **€400,000.**

It is also worth noting that:

  - To benefit from such a regime, employees must perform the activity for which they benefit from it for **at least 75% of the working time.** The other eligibility conditions remain unchanged.

  - The current regime will continue to apply to eligible employees in 2024, but they can opt for the new regime starting in 2025. However, such a choice will be irrevocable!

- **New bonus for employees under 30: "the young employee bonus."**

Following the introduction of the rental bonus on 1 June 2024, allowing the employer to pay a bonus to a young employee renting his or her primary residence, the government wishes to renew its support for young workers by creating a **young employee bonus** to help them start their professional life.

This new tax exemption measure will be an additional tool for employers to attract young talent to their companies! In practice, the employer will have the possibility of paying a **tax-exempt bonus of 75%** to their young employee. This bonus, the amount of which will vary depending on the employee's gross annual salary, can be paid **once off** within the first 5 years of the contract:

  - **€5,000** pour employees whose gross annual remuneration is ⩽ €50,000,

- **€3,750** for employees whose gross annual remuneration is between €50,001 and €75,000,
- **€2,500** for employees whose gross annual remuneration is between €75,001 and €100,000.

- **Introduction to a new overtime tax credit for cross-border employees**

The bill introduces an "overtime tax credit" to **account for the loss of income that cross-border employees** may suffer when their Luxembourg employer pays for overtime. In point of fact, if overtime is fully tax-exempt in Luxembourg, the country of residence can sometimes subject these hours to taxation, thereby depriving the cross-border employee of this exemption benefit. This decision likely follows the recent position of the German tax authorities to tax in Germany the overtime exempted in Luxembourg for their citizens. The government's clear aim is to **maintain Luxembourg's attractiveness** for cross-border workers.

The overtime tax-credit is set as follows:

- For overtime gross remuneration not reaching €1,200 per year, the overtime tax credit is not granted;
- For overtime gross remuneration between €1,200 and €4,000 per year, the overtime tax credit amounts to €[(gross remuneration – 1,200) x 25%] per year;
- For overtime gross remuneration exceeding 4,000€ per year, the overtime tax credit amounts to **€700** per year.

Cross-border employees will be able to benefit from it either upon request in case of an assessment-based taxation or within the framework of an annual statement.

The bill provides for **retroactive application as of 1 January 2024.**