



GES NewsFlash

Luxembourg — Local and international developments in personal taxation and social security

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Fiscal dispute regarding German commuters working in Luxembourg coming to an end?

After several months of hot-tempered discussions between the German and Luxembourg tax authorities, on 26 May 2011, the Finance Ministers of their respective countries finally came to an agreement about the German cross-border commuters working in Luxembourg.

The consensus on the tax treatment of wages for commuters was set up through a mutual agreement to the agreement of 23 August 1958 between the Grand Duchy of Luxembourg and the Federal Republic of Germany for the avoidance of double taxation. The mutual agreement is in force as of 27 May 2011 and is applicable to all cases that had not already been finally assessed before that date.

The memorandum of agreement between Germany and Luxembourg permits a tax buffer of up to 19 working days per calendar year for cases where the employee works in the country of residence (Germany) or in a third country, provided that the salary income is subject to taxation in the country of activity (Luxembourg). Salary income pertaining to work days that total no more than 19 are tax exempt in the country of residence (Germany). However, if the employee works 20 working days or more during the calendar year in the country of residence (Germany) or in a third country, the taxation of salary income pertaining to these working days falls back to the country of residence (Germany).

The distribution of wages between the country of residence (Germany) and the country of activity (Luxembourg), for taxation purposes, will be based on the "agreed working days" according to the labour contract. This means that vacation days, weekend days (or alternative rest days), and public holidays are not taken into account for the computation of the pro rata of income taxable in each state.

Payments with respect to maternity leave and sick leave (the so-called “unproductive” days that have made it difficult to find a consensus) are taxed in the state of activity (Luxembourg). Consequently, these types of salary income are tax exempt in the state of residence (Germany).

However, unpaid sick days will reduce the agreed working days.

The following additional rules for calculating the agreed working days and the division ratio are set by the agreement:

- Working time spent in a third country should be taxed in the country of residence (Germany).
- Overtime must be considered separately.
- Work on a nonagreed working day with a compensation holiday (i.e., without payment of a separate cash amount) should be taken into account to compute the agreed working days.
- Lump-sum payments (such as anniversary payment for jubilees) for no more than 10 years’ previous active service are proportionately attributable to the activity in the state of residence (Germany) and in the state of activity (Luxembourg) using the above principles. Note that the reason of payment will be relevant, if the lump-sum payments are pensions or pension claims, the taxation right will fall back to the country of residence (Germany).
- Holiday allowances and payments for unused vacation days are included in the division ratio; for holiday payments that are related to vacation days of a previous year, the division ratio of the year concerned is applicable.
- If effective working days differ from agreed working days because the employee transferred vacation days from one year to another, the agreed working days used to compute the division ratio must be increased/reduced accordingly, unless the number of transferred holidays is no more than 10.

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Deloitte’s view

The agreement puts an end to a long-lasting period of uncertainty for German residents working in Luxembourg and is good news in this respect. The division ratio, the calculation of the agreed working days, and the calculation of the Luxembourg wage tax will likely raise questions for which it could be helpful for the Luxembourg tax authorities to issue guidelines in the near future. The guidelines currently available on the taxation of professional drivers (in the mutual agreement between the Grand Duchy of Luxembourg and the Federal Republic of Germany on the tax

treatment of wages for professional drivers dated 1 March 2005 and the circular letter LG –Conv. DI n°51 of the Luxembourg tax authorities dated 18 April 2005) can be a useful reference in this respect. We will keep you informed of any developments in this area.

People to contact

If you have any questions concerning the issues in this GES NewsFlash, please contact one of the tax professionals at our Deloitte offices as follows:

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