Global Rewards Update
Luxembourg - New Tax Regime for Stock Options/Warrants

Key Points to Know

- Clarifications on required grant notifications required for certain award types have been issued by the Luxembourg tax authority, including penalties for failure to comply with the notification requirements.
- Effective January 2018, the taxable basis for irrevocable options (i.e., options that are fully vested at grant) increased from 17.5% to 30%.
- Conditional awards, such as stock options or restricted stock unit awards subject to vesting conditions, are not impacted by the Circular.

Background

On November 29, 2017, the Director of the Luxembourg Tax Authorities issued a revised Circular 104/2 (hereafter "the Circular") which introduced several revisions for option and warrant plans in Luxembourg, including:

i. Clarification on required grant notifications, including penalties for non-compliance

ii. Change in calculation of taxable basis for irrevocable options

Grant Notification Requirements

Grant Notification Timing

The Circular states that a "grant notification" must be provided to Luxembourg Tax Authorities in a "timely" manner following grant of option/warrant plans *taxable at grant* (i.e., irrevocable options and eligible warrant plans), and should include the estimated yearly gross salary of the beneficiary, excluding the options/warrants.

The Circular does not specify what is considered "timely" for purposes of the grant notification, though it is expected that Luxembourg Tax Authorities will consider a grant notification to be "timely" provided that it is made within the 4-5 days following the grant of date.

Further, the Circular eliminates the requirement to provide notification two months prior to the grant of options / warrants, as defined under Circular 104/2bis dated December 28, 2015.

Note that conditional options (i.e., options subject to vesting conditions) are not impacted by the Circular, and remain subject to tax / tax reporting at the point of exercise.

Impact of Failure to File Grant Notification

In the event an employer fails to comply with the grant notification requirements, the Luxembourg Tax Authorities reserve the right to subject the full value of the shares underlying the option/warrant at grant to tax, without the application of the lump sum valuation percentage (as discussed below) or any other potential discounts.

Change in Taxable Basis at Grant

Option/warrant plans *taxable at grant* (i.e., irrevocable options and eligible warrant plans) are subject to tax and reporting at the time of grant, based on a percentage of the value of the shares underlying the option/warrant at grant.

For example, if an employee was granted 10 options over shares with a value of EUR 10 each, the gross benefit-in-kind at grant would be equal to EUR 100.

Historically, the taxable benefit at grant was equal to 17.5% of this gross benefit-in-kind, or EUR 17.50.

However, the circular increased the taxable basis to 30% of the gross benefit-in-kind, or EUR 30.00.

Options granted on or after January 1, 2018 will be subject to tax and reporting in accordance with the new basis. As noted above, failure to comply with the grant notification requirements may result in the Luxembourg Tax Authorities disallowing the application of the lump sum valuation percentage at grant. Using the example, this means that potentially the full EUR 100 gross benefit-in-kind would be subject to tax at grant.

Deloitte's view

For companies granting options/warrants subject to taxation at grant, it is important to ensure that proper procedures are in place to ensure that the Luxembourg entity is aware of the grant (assuming it is not the granting entity) and has a proper reporting structure in place as failure to comply with the requirements may have a significant impact on taxation of the awards.