



**Real Estate in Luxembourg: What you should know, what's new?
(Part 2)
13 October 2016**



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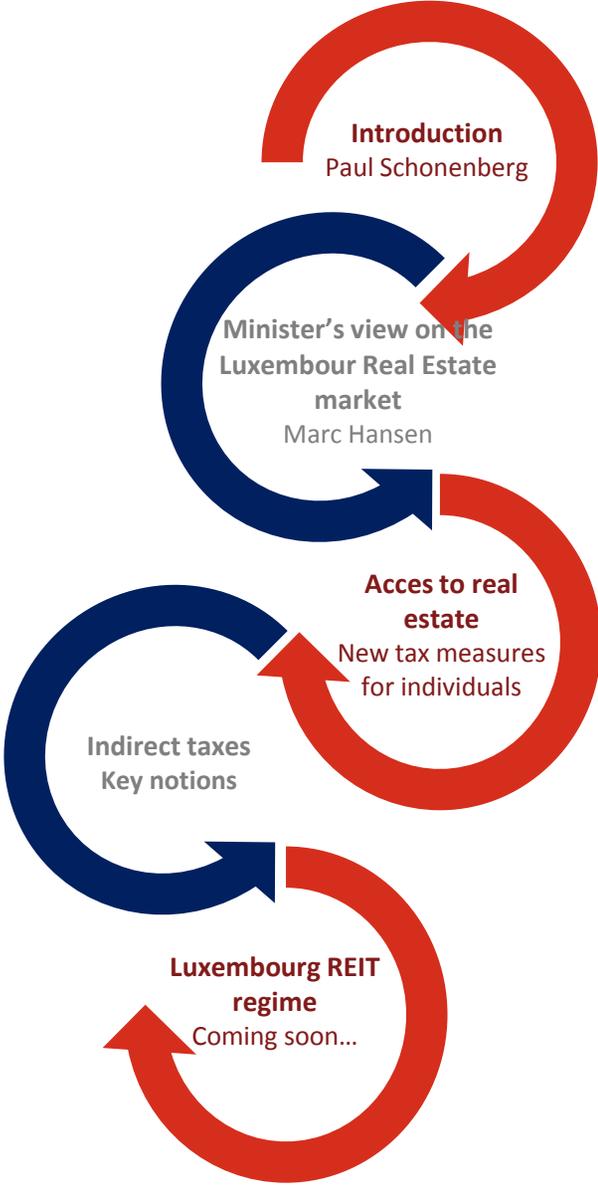
Moderator:



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Agenda:



Access to real estate : the tax side

Home saving schemes - “Contrat d'épargne-logement”

- Home-savings schemes are contracts linked to a loan agreement to finance the acquisition/construction/transformation of a main residence in Luxembourg.
- Contributions paid on such contracts are tax deductible up to a certain amount **per year** and **per member of the household**:

Current deductible amount:
672 EUR



Reform 2017:

- *Up to 40 years-old*: EUR 1,344
- *Over 40 years-old*: EUR 672



Access to real estate : the tax side

Mortgage interest related to the main residence

- Current amount of deductible mortgage interest:



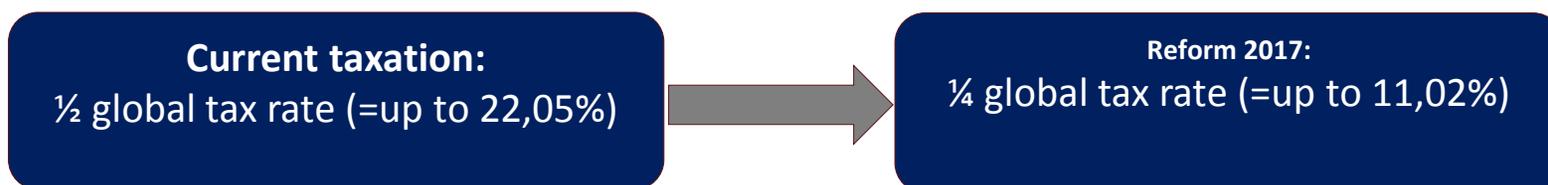
- Reform 2017 - deductible mortgage interest:



Access to real estate : the tax side

Disposal of real estate more than 2 years after acquisition

- On 14 June 2016, the Parliament adopted the bill of law providing favourable tax treatment on capital gains arising from the sale of real estate/fields other than the main residence
- This favourable tax treatment is a temporary measure applying to the disposal of qualifying real estate from **1 July 2016 to 31 December 2017** more than 2 years after acquisition:



Access to real estate: additional measures

- **Residence occupied by the owner (main residence):** the deemed rental income of a property occupied by the owner should be abolished.
- **Encouraging rentals to approved social organisations:** income arising from the rental of housing to approved social organisations (e.g. Agence Immobilière Sociale) should benefit from a 50% exemption.



Access to and sale of real estate: the legal side

Nothing new, really, so just two reminders of practical points that are often misconceived.

Reminder 1:

- The so called “*compromis*” (sales agreement under private seal) is not a “pre-contract”, but a binding sales agreement, generally under a condition precedent. It is not recommended to sign any contract related to real estate without the assistance of a lawyer.

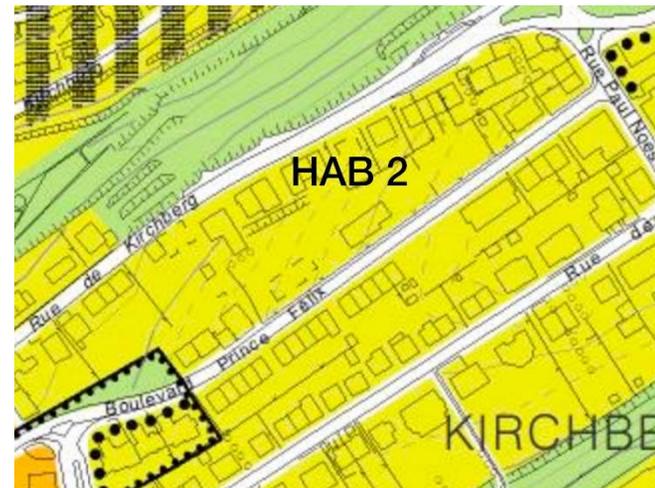
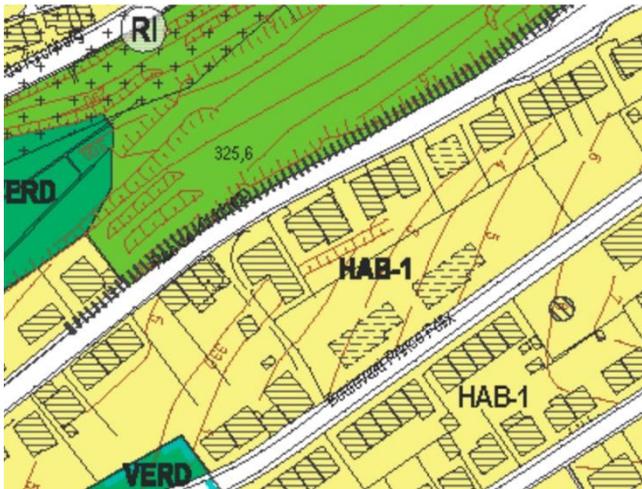
Reminder 2:

- If you buy a property that is yet to be built, and if it is a residential property or located in a mixed building, the specific provisions for sales before completion (*vente en état futur d'achèvement*, VEFA) apply.
- In such case, the sale is executed by notarial deed only; a *compromis* would not be valid
- The notarial deed can only be executed when the building permit, the register of division (*cadastre vertical*) and the rules of co-ownership (*règlement de copropriété*) have been approved.
- Prior to the notarial deed, no other agreement is possible save a reservation agreement (*contrat de réservation*), which terms are strictly circumscribed by the law.
- At the execution of the notarial deed, the buyer will only pay the portion of the price corresponding to the land, and the existing construction.
- During construction, the seller may not claim any amounts in excess of the timetable in the notarial deed, which in principle corresponds to the progress of the construction works.
- Most of the provisions dealing with the VEFA are of public order and may not be altered by contractual agreements.



PAG – what's new?

- What is the PAG : *Plan d'aménagement général* = General development plan; One per Commune
- New proposition in the Commune of Luxembourg now available
- Protection of the “single family houses”
- Example:



Zoning and planning

WHY IS THIS ZONING AND PLANNING SO IMPORTANT?

It is material for the question if and what can be built on a specific plot, and the permitted use.

If you acquire an existing property, it will usually not affect current use and operation of the property, to the extent that current use is in line with the applicable laws and regulations (which is sometimes not the case!).

However, planning of public projects can entail expropriation for public utility projects.

Reconstruction of a building , whether willfully demolished or destroyed by accidental cause will be subject to the actual regulations; no right to identical reconstruction as authorized by the old building permit.

So prior to the acquisition of any property you should verify its specific situation!



Zoning and planning On a National Level

LAND USE PLANNING AND THE “PLANS SECTORIELS”

Aim: To govern sustainable spatial development on a **national** level (“top down”) by *Plans Directeurs Sectoriels* and *Plans d’Occupation du Sol*.

Consequence: Direct and material impact on territorial organization and land use of the communes.

Principle provided for by the Law of 30 July 2013 on Land Use Planning.



Zoning and planning On a National Level

LAND USE PLANNING AND THE “PLANS SECTORIELS”

Four areas

Plan directeur sectoriel “**Transports**”.

Plan directeur sectoriel “**Logement**”.

Plan directeur sectoriel “**Paysages**”.

Plan directeur sectoriel “**Zones d’activités économiques**”.



Zoning and planning On a National Level

LAND USE PLANNING AND THE “PLANS SECTORIELS”

2014: FIRST TRY - NOT VIABLE - A SUMMARY

Fierce opposition from municipalities and professionals because of numerous legal and practical issues.

Ordinance of 17 September 2014 by the president of the administrative tribunal : suspension of building permit because of serious doubts on the legality of the transitional measures as provided for by the grand-ducal regulations for the *plans sectoriels*.

Beginning of November 2014 a new Director-General of the Department of Spatial Planning and Development of the Ministry of Sustainable Development and Infrastructure was appointed.

18 November 2014: Formal opposition by the Council of State: serious constitutional issues: expropriation; communal autonomy; lack of legal basis.

As a consequence, they were eventually withdrawn by decision of the Government of 28 November 2014.



Zoning and planning On a National Level

LAND USE PLANNING AND THE “PLANS SECTORIELS”

February 2016: The Government announced that

The new plans sectoriels would go into procedure in the autumn of 2016, with more input by the communes by way of 5 regional conferences.

The consultation procedure should be completed end of 2016.

The a new law on land use should be ready in the spring of 2017.



Zoning and planning On a National Level

LAND USE PLANNING AND THE “PLANS SECTORIELS”

January 2016: Amendment of draft bill n° 6694, to amend Law of 30 July 2013 on Land Use Planning, pending a more fundamental reform.

April 2016: In its formal opinion on the draft bill, the Chamber of Trades (Chambre des Métiers) is still worried about the possible impact of the things to come on the acquired rights of the project owners (*porteurs de projets d'urbanisme*).

June 2016: Opinion by the Council of State: voices concerns as it deems that the amendments will not suffice to deal with the issues it has previously raised, and criticizes that this draft bill would entail the adoption of procedures governing instruments of land use under the old law while a new law is being elaborated; CoS suggests adopting the new law first rather than working with a provisional solution.



Zoning and planning On a National Level

LAND USE PLANNING AND THE “PLANS SECTORIELS”

27 September 2016: New Draft Bill 7065

- Fundamental reform of the legislation on land use by abrogation and replacement of the law of 2013.
- Government accepts opinion by the Council of State and drops Draft Bill 6694.
- The implementation of the *Plans Sectoriels* is thus delayed.
- The laws of 19 July 2014 on municipal land management and urban development, 15 March 1979 on expropriation and 16 August 1967 on road planning will be amended.



Zoning and planning On a National Level

LAND USE PLANNING AND THE “PLANS SECTORIELS”

27 September 2016: New Draft Bill 7065

Key points:

- Indemnification of deprivations of rights out proportion with the public utility.
- No general standstill during implementation, but specific and provisional easements (*servitudes*).
- Suppressing the distinction between binding provisions and recommendations.
- Simplification of procedures.



Zoning and planning On a National Level

LAND USE PLANNING AND THE “PLANS SECTORIELS”

New Focus announced in 2014

- Reduce the use of surfaces from 2 hectares to 1 hectare per day.
- Mobilize unused land (plots).
- Densify the urban fabric.
- Build higher.
- But: keep quality of the habitat.



Zoning and planning On a National Level

LAND USE PLANNING AND THE “PLANS SECTORIELS”

“Important changes” in particular for the *Plan Sectoriel Logement*:

- Limitation to the designation of sites for major projects.
- More flexible approach with respect to the allocation of the potential for growth of housing and with respect to density.



Zoning and planning On a National Level

LAND USE PLANNING AND THE “PLANS SECTORIELS”

Risks and Chances

- Renaissance of certain easements and limitations on construction in certain areas.
- More square meters on certain plots?
- Indications for a more pragmatic and legalistic approach.
- But still a great uncertainty with respect to the new rules and regulations and their practical impact.
- New law considered to be urgent; timeline uncertain.



Zoning and planning On a National Level

THE « LOI OMNIBUS » - DRAFT BILL N°6704

Aims at the simplification of administrative procedures, in particular with respect to the adoption of General Development Plans (*Plans d'Aménagement Général*, PAG) and Partial Development Plans (*Plans d'Aménagement Particulier*, PAP) by the communes.

Objective: to render these procedures more efficient, shorten the timelines and reduce costs.



Zoning and planning On a National Level

THE « LOI OMNIBUS » - DRAFT BILL N°6704

Latest news: Splitting of Bill in two parts

Two series of amendments proposed:

- **20 November 2015, by Parliament; and**
- **4 January 2016, by Government.**

The latter is limited to the redress of legal and practical issues created by the Law of 22 October 2008 (« *pacte logement* ») with respect to the contractual freedom/flexibility regarding agreements on surface rights (*droits de superficie*), in particular with respect to non-residential buildings.



Zoning and planning On a National Level

THE “LOI OMNIBUS” - DRAFT BILL N°6704

Latest news: Splitting of Bill in two parts

15 July 2016: Second additional opinion by the Council of State

- Limited to the parliamentary amendments.
- More time needed to advise on the legal issues related to surface rights.
- Suggestion to split the Draft Bill so that the remainder of the Bill is not delayed.

September 2016: Government decides to split Draft Bill 6704

Vote: Still this year?



Zoning and planning On a Communal Level

New General Development Plans (*Plans d'Aménagement Général*, PAG)

- For every commune, new PAG's must be submitted to the municipal council until 8 August 2018 (Amendment of article 108 of the law of 19 July 2004 on communal planning and urban development by the Law of 14 June 2015).
- According to the initial law in 2004, this should have been achieved within 6 years, i.e. until 8 August 2010.
- > Not an easy exercise.



Zoning and planning On a Communal Level

New General Development Plans (*Plans d'Aménagement Général*, PAG)

The PAG of the City of Luxembourg

- The City of Luxembourg is currently in the process of adopting a new PAG.
- Draft of the new PAG released on 20 June 2016.
- Interested parties could file their complaints within 30 days.
- City administration will summon and hear those who have filed complaints.
- Process still deemed to last several months.
- Complaint is a prerequisite for judicial recourse against PAG (and the PAP).



Zoning and planning On a Communal Level

New General Development Plans (*Plans d'Aménagement Général*, PAG)

The PAG of the City of Luxembourg

- Not yet in force; may still be amended.
- However: any project that is not already authorised that does not match the provisions of the new PAG will not be authorized.
- From a practical standpoint, projects currently will need to be in line with the existing or old PAG, as well as with the new draft PAG.



Zoning and planning On a Communal Level

New General Development Plans (*Plans d'Aménagement Général*, PAG)

The PAG of the City of Luxembourg

For existing quarters, the new PAG has to be seen in connection with the specific provisions in the new Special Development Plans, PAP "*Quartiers Existants*".

- More information on <https://pag.vdl.lu/>.
- For new developments, new PAP's will have to be approved.



Zoning and planning On a Communal Level

New General Development Plans (*Plans d'Aménagement Général*, PAG)

The PAG of the City of Luxembourg – Issues

- Many properties affected by a change in classification and/or new or increased restrictions and easements.
- In a nutshell, in existing quarters, and with some exceptions, size and use of buildings, as well as the number of separate lodgings in a building will be subject to further restrictions, while new developments will be possible that may permit a much higher density.



Zoning and planning On a Communal Level

New General Development Plans (*Plans d'Aménagement Général*, PAG)

The PAG of the City of Luxembourg – Issues

- A considerable part of the communal territory is now classified in protected areas with additional restrictions.
- The protection as such appears to make sense in many cases.
- However, it is argued that the (new or increased) restrictions are too general, too far-reaching, lack flexibility and in many or even most cases go beyond what is needed to protect what is worthy of protection.



Zoning and planning On a Communal Level

New General Development Plans (*Plans d'Aménagement Général*, PAG)

The PAG of the City of Luxembourg – Issues

- Certain owners lose 25% or more of their constructible floorspace
- On the other side, the City refers to the “big picture” and argues that the new PAG will permit a 30% increase of lodgings and allow the City to grow to a population of up to 190.000.
- It should be assessed on a case by case basis whether the proposed regulations provide sufficient objective criteria for justifying the restrictions proposed in some areas.
- It is to be expected that there will be more controversial discussions, and eventually lawsuits.

To be continued.



Zoning and planning

- **Amendment of Land Use Plan (*Plan d'Occupation du Sol*, POS) for Luxembourg Airport.**
- Draft deposited by the Government on 4 July 2016.
- Affects properties in the City of Luxembourg, Niederanven, Sandweiler and Schuttrange.
- Shall amend the POS of 17 May 2006.
- Complaints could be filed until 17 August 2016.
- Aim: to adapt the POS to the results of a Strategic Environmental Assessment to reduce impact on environment.
- Further details:

http://www.dat.public.lu/actualites/2016/07/Depot-a-la-maison-communale-de-la-Ville-de-Luxembourg-du-projet-de-modification-du-plan-d_occupation-du-sol- POS - -Aeroport-et-environs-et-de-la-EES-y-afferente_04_07_2016/index.html



Indirect taxes - Key notions

Transfers and sales of immovable properties

Transaction	VAT treatment	Registration duties
Sale of an existing building	VAT exempt	7% / 10%*
Sale of an existing building with a VAT option	17%	
Sale under a forward sale contract (“vente à tempérament”)	VAT exempt for the part already built and the land	7% / 10%* on the part already built and the land
	17% / 3%** (VAT due upon settlement of the last payment – no official guidance in Luxembourg)	N/A
Sale in future state of completion (“VEFA”)	VAT exempt for the part already built and the land	7% / 10%* on the part already built and the land
	17% / 3%** for the part to be built	N/A
Sale of a building newly built and used as the main residence	VAT exempt but possibility to get a VAT refund**	7% / 10%* - tax credit possible

**If the building is located in Luxembourg city, a municipal surcharge of 3% is due except for single family houses. Further, a special registration duty rate is generally foreseen for purchases with a view to resell the property.*

***See slides on the application of the super-reduced VAT rate*



Indirect taxes - Key notions

Transfers and sales of immovable properties

Transaction	VAT treatment	Registration duties
Transfer of a building through a share deal/merger	VAT exempt	N/A
Contribution of a building against shares	VAT exempt	0,6% (+ 0,3%*) + transcription right of 0,5%
Contribution of a building in return for payment	VAT exempt	6% (+ 3%*) + transcription right of 1%

**If the building is located in Luxembourg city*

Point of attention: The taxable basis for registration duties includes VAT (if applicable). Conversely, the taxable basis for VAT does not include registration duties.



Indirect taxes - Key notions

Renting out of immovable properties

Transaction	VAT treatment	Registration duties
Renting out of a building (parking space included if the parking space is part of the whole)	VAT exempt	0,6% on the total amount of rents
Renting out of a building with a VAT option	17% (if a valid VAT option has been obtained with the VAT Authorities – see conditions in the slide concerning the VAT option)	Fixed registration duty of EUR 12
Renting out of specific immovable properties such as hotel rooms, safes or parking spaces	17% (3% for hotel rooms)	N / A

Points of attention:

- The taxable basis for registration duties includes VAT (if applicable). Conversely, the taxable basis for VAT does not include registration duties.
- The draft bill for the 2017 tax reform foresees a change in the rules for registration of rental agreements: these would no longer be mandatorily registered and consequently be subject to registration duties only if voluntarily presented to the registration formality.



Indirect taxes - Key notions

VAT option

Why?

- VAT exempt transactions as the sale and the renting out of certain immovable properties do not allow input VAT recovery on expenses linked to these transactions for the seller/lessor.
- Transactions subject to VAT allow input VAT recovery on expenses linked to these transactions.
- A possibility to waive the VAT exemption is possible if the following formal and substantive conditions are met:

Formal conditions	Substantive conditions
Written declaration submitted to the VAT Authorities and approved by them	Seller / lessor and purchaser / tenant should be both taxable persons with a VAT registration number in Luxembourg
VAT is mentioned in the deed of sale / sale agreement / lease agreement / invoices	The property is mainly used by the purchaser / tenant for activities allowing input VAT recovery

Point of attention: The VAT option must be submitted and approved by the VAT Authorities before the application of VAT by the seller/the lessor on the sale/rental of the building and before registration.



Indirect taxes - Key notions

VAT option

COMMENTS ON SPECIFIC ISSUES REGARDING VAT OPTIONS:

Step-up clause in commercial and office lease agreements

It is common practice to include a clause in commercial and office lease agreements that provides that to the extent the VAT option is not granted or becomes obsolete at a later stage because the tenant does not fulfil the conditions for the option, the rent will be increased by an amount equivalent to the VAT on the rent at the rate then applicable.

No retroactivity of the VAT Option

Judgement of the European Court of Justice of 9 September 2004 in Case C-269/03, Administration de l'enregistrement et des domaines, État du grand-duché de Luxembourg / Vermietungsgesellschaft Objekt Kirchberg SARL:

The provisions of European Law do not preclude a Member State, which has exercised the power to allow taxpayers a right of option for taxation on leasing or letting transactions of immovable property, from adopting legislation which makes full deduction of the input VAT paid conditional upon *non-retroactive, prior approval* of the tax authorities.



Indirect taxes - Key notions

VAT option

COMMENTS ON SPECIFIC ISSUES REGARDING VAT OPTIONS:

Lease agreements vs. service agreements in business centers

This bears relevance for

- The validity of the agreements;
- The compliance with the law of 31 May 1999 on the domiciliation of companies;
- Compliance with the law of the 2 September 2011 on the access to commercial, craft and industrial activities, as well as certain liberal professions (business permit, *autorisation de commerce*).
- Recouping of Input VAT

On 16 December 2015 the Appellate Court of Luxembourg has rendered a decision by which it has declared null and void the agreement between a business center and its client, a company that had its registered office at the address of the business center.

The Court has analysed the contract and found (i) that certain of its provisions were incompatible with the essence of a lease agreement (ii) that the services provided by the business center were the predominant part of the agreement, and (iii) that the agreement was to be construed as a domiciliation agreement, for which the business center was not licensed.



Indirect taxes - Key notions

VAT option

COMMENTS ON SPECIFIC ISSUES REGARDING VAT OPTIONS:

Lease agreements vs. service agreements in business centers

Apart from the nullity of the agreement, such a situation could constitute a criminal offence under the law of 31 May 1999 on the domiciliation of companies, as well as under the law of the 2 September 2011 on business permits, and could lead to sanctions including the judicial winding up of the company.

This could also raise issues regarding the VAT treatment. On the one side, as long as a taxable person was in good faith the nullity of the agreement should not exclude the deduction of input VAT. On the other side, in the case of a services agreement, the provider will invoice VAT without having to opt in; while in the case of a lease agreement an opt-in will be required.

As this format of contract appears to be widely used in business centers, it is strongly advised to review any such agreement that one is a party to. As the case may be, a split between lease and services in separate agreements should be considered.



Indirect taxes - Recent trends and positions of the Luxembourg VAT authorities

Development costs

- The VAT Authorities recently refused in part the deduction of the VAT incurred on development costs (lump sum rejections) since they consider these costs as linked to the land although the property was let under a VAT option.

Free rental periods

- VAT Authorities challenged the VAT deduction right of property companies granting free rental periods to their tenants.

Transfer of Going Concern (TOGC) relief

- The VAT Authorities do not accept to treat the sale/contribution of leased premises as a TOGC, contrary to a number of EU Member States like Germany, UK, etc. A VAT option (if possible) is needed to avoid VAT adjustments on construction / renovation / acquisition costs and VAT pre-financing.



Indirect taxes - Application of the super-reduced VAT rate on construction and renovation works

Application of the super-reduced VAT rate on construction and renovation works

- Application of the super-reduced VAT rate of 3% instead of 17%.
- Super-reduced VAT rate directly applied by the supplier or via a formal reimbursement request submitted by the acquirer to the VAT Authorities (office 12).
- Application of the super-reduced rate of 3% limited to certain costs (list given by the Luxembourg VAT law and guidelines of the VAT Authorities) incurred for the construction or the renovation of a building used as the main residence by the landlord or by the tenant.

Application of the super-reduced VAT rate on acquisition of buildings newly built

- Acquisition of buildings newly built are VAT exempt. As a consequence, developers are not entitled to recover VAT incurred on costs linked to these transactions. Such a VAT cost is likely to impact the price of the new building.
- The VAT Authorities accept to reimburse 14% of the potential hidden VAT which may have been applied by the developer / seller.



Indirect taxes - Application of the super-reduced VAT rate on construction and renovation works

Application of the super-reduced VAT rate on acquisition of new buildings (cont'd)

- VAT reimbursable = price of the building (land excluded) - 20%* ÷ 1,17** x 14%***
 - *Lump sum corresponding to architect / engineer costs and the margin realized by the developer (if amounts are available for these costs, the VAT Authorities use these amounts instead of the lump sum method)*
 - **Hidden VAT (17% on price of the building (land excluded) - 20%*)*
 - ***Difference between 17% and 3%*
- The reimbursement is limited to EUR 50,000 (i.e. taxable basis of EUR 357.142,86) and is subject to strict conditions:
 - The construction of the building must have been finalized maximum two years before the reimbursement request;
 - The deed of sale shall mention the price of the land and the price of the construction (with no indication of VAT);
 - The building must be used as the main residence;
 - The VAT refund request shall be done on a specific reimbursement form.



Luxembourg Real Estate Investment Trust (LREIT) - under discussion

❑ Objectives

- Use of the **“LREIT” brand**.
- **Cross-border Real Estate and infrastructure investments.**
- Open to **various distribution channels.**
- **Neutral flow-through tax regime.**
- **Robust framework** from a legal and regulatory perspective, adopting minimum criteria which are common to other REIT regimes.
- **International acceptability** (equivalence).



Luxembourg Real Estate Investment Trust (LREIT) - under discussion

❑ Legal and regulated aspects

- Legal form: either corporate entity (SA, S.à r.l, SCA) or partnership (SNC, SCS, SCSp).
- Capital requirements: no specific requirements.
- Listing requirements: no specific requirements.
- Regulated: In principle yes (e.g. AIFMD/Prospectus directive).
- Diversification: No risk diversification rules.
- Compartments: optional.
- Multi-currency: optional.
- Lux GAAP/IFRS: optional.
- Maximum leverage: (e.g., 65% Debt to Portfolio Value).



Luxembourg Real Estate Investment Trust (LREIT) - under discussion

❑ Legal and regulated aspects

- Investors restriction: Professional and retail investors.
- Investing activities/qualifying assets: investments in direct and indirect or local Real Estate and; infrastructure assets; debt financing the assets; single property possible; assets under development subject to specific conditions.
- Distribution requirements: compulsory yearly distribution of at least 75% of the income from the qualifying assets (interim dividends possible).



Luxembourg Real Estate Investment Trust (LREIT) - under discussion

Taxation

- Fully taxable entity.
- NWT liability.
- No withholding tax on distribution except on income derived from Luxembourg Real Estate asset.
- Treaty/directive benefit.
- Substance.
- BEPS...



Q&A

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