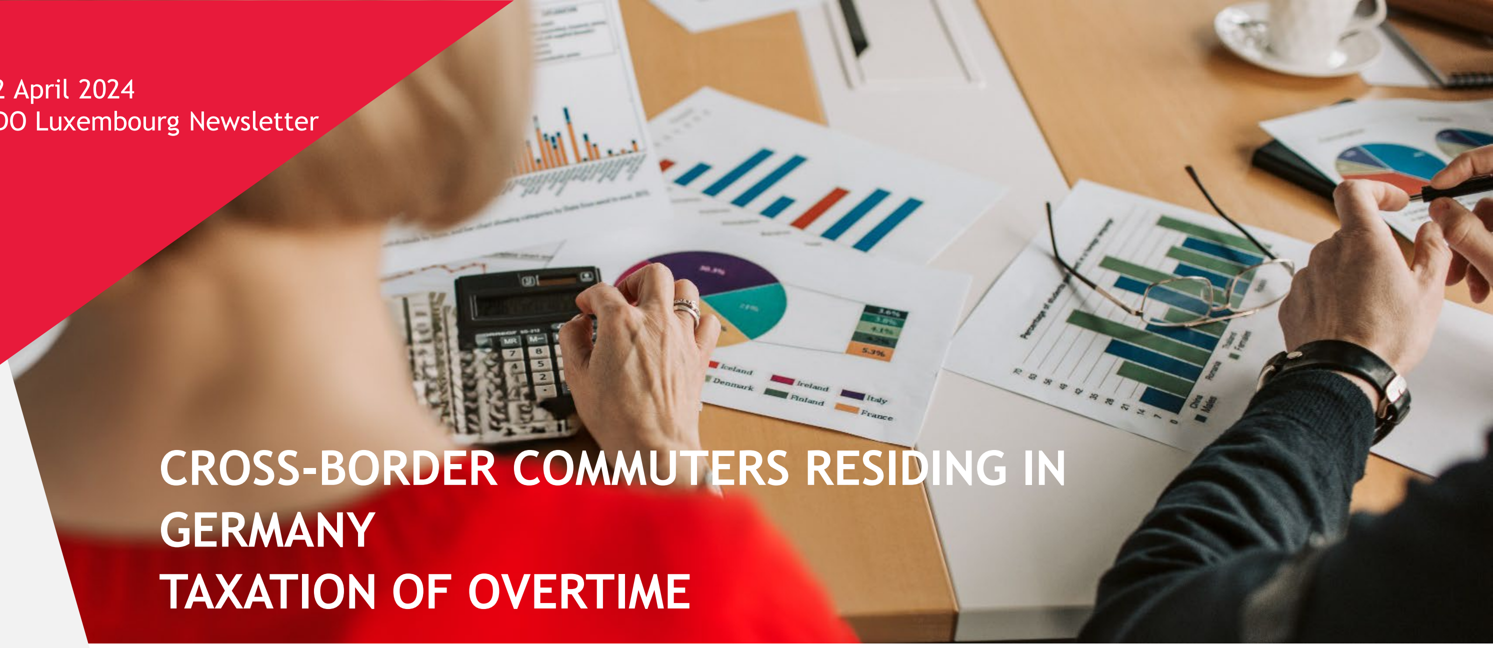
12 April 2024
BDO Luxembourg Newsletter



CROSS-BORDER COMMUTERS RESIDING IN GERMANY TAXATION OF OVERTIME

The Luxembourg and German tax authorities signed an amicable agreement on 11 January 2024. The purpose of the agreement is the interpretation and application of the Convention for the Avoidance of Double Taxation and the Prevention of Tax Evasion with Respect to Taxes on Income and on Capital (hereinafter referred to as the "Convention")[1] signed between the two countries on 23 April 2012.

It follows from this amicable agreement that Germany will henceforth tax all wages paid by Luxembourg employers for overtime worked by cross-border workers residing in Germany, even if the overtime was worked in Luxembourg and the base remuneration of the German cross-border workers is fully taxable in Luxembourg (which is the case if an employee has worked exclusively in Luxembourg or if an employee has worked less than 35 days outside Luxembourg).

On the face of it, the taxation of all overtime in Germany appears to be contrary to the method of taxation provided for in the Convention, which provides that wages to be taxed in Luxembourg are exempt from income tax in Germany.

However, the Convention also provides that Germany may tax income or parts of income[2] that would normally be taxable only in Luxembourg and exempt in Germany, if in fact the Grand Duchy does not levy income tax on such income, or parts of income.

Currently, Luxembourg tax legislation provides that wages paid by a Luxembourg employer for overtime are fully exempt from Luxembourg income tax. Therefore, as long as Luxembourg exempts wages paid for overtime from Luxembourg income tax, overtime paid to employees resident in Germany will be taxable in Germany.

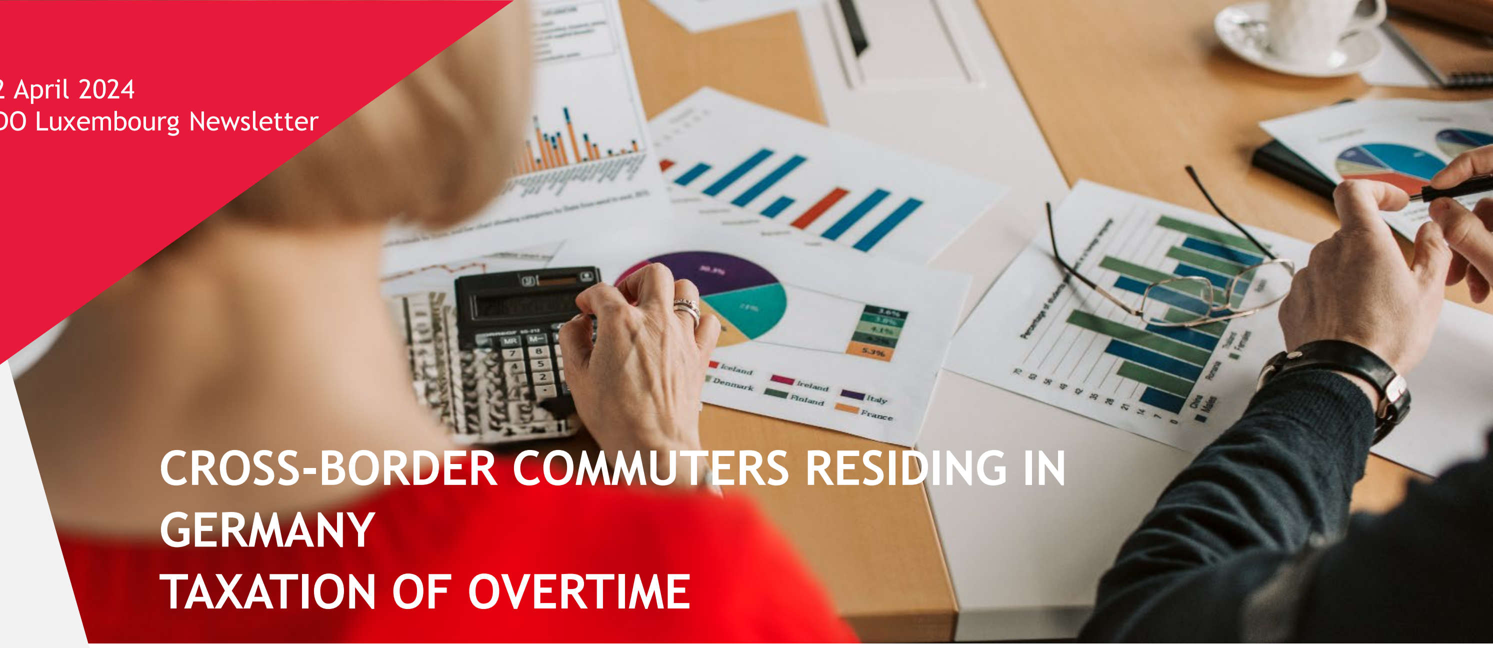
It should also be noted that the amicable agreement of 11 January 2024 specifies that, with the exception of the arrangements relating to the new provisions introduced into the Convention by the addendum of 6 July 2023, the arrangements agreed between the Luxembourg and German tax authorities are applicable to all taxations that are not yet final and to those that are the subject of an amicable procedure between the Luxembourg and German tax authorities.

This clarification provided by the agreement of 11 January 2024 suggests that the approach of the German tax authorities is not new and that the German tax authorities have tried to tax overtime paid by Luxembourg employers to employees resident in Germany already in the past.

The fact that the agreement of 11 January 2024 is also applicable, with a few exceptions, to taxations that are not yet final, raises the question of whether the German tax authorities will

[1] The amicable agreement is based on the Convention in the version resulting from the Amendment signed on 6 July 2023 between the Grand Duchy of Luxembourg and the Federal Republic of Germany and ratified by the Grand Duchy of Luxembourg on 22 December 2023. The exchange of instruments of ratification was published on 29 December 2023. The amicable agreement replaces the amicable agreement of 26 May 2011 on the taxation of cross-border workers' wages, the amicable agreement of 7 September 2011 on the taxation of compensation paid as a result of a dismissal and/or a redundancy plan, as well as unemployment benefits, and the amicable agreement of 7 September 2011 on the taxation of drivers, locomotive drivers and accompanying personnel.

[2] Clarification added to the Protocol of 23 April 2012 by the addendum to the Convention dated 6 July 2023: the expression "income" also includes parts of income.



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apply the new approach, consisting of taxing overtime paid by Luxembourg employers to employees resident in Germany, only to overtime hours paid from 2024 onwards, or also to overtime paid before the year 2024.

In view of the current German tax legislation, the German tax authorities could retrospectively tax all overtime wages received for tax years not yet time-barred. For an employee resident in Germany whose only income has been wages taxable in Luxembourg and who was therefore not required to file a tax return in Germany, this means that, until 31 December 2024, he could be taxed in Germany on all overtime hours he has received from a Luxembourg employer since 2016. In practice, however, it is not clear how many years the tax authorities will actually go back.

The agreement of 11 January 2024 unfortunately does not contain any answers to this question and it is to be hoped that the German authorities will soon provide clarifications on this subject before imposing fines on employees for non-declaration of overtime on the basis of the information received from the Luxembourg tax authorities through the automatic exchange of information.

Alternatively, employees resident in Germany who have worked overtime in Luxembourg since 2016 should contact a German tax advisor in order to assess the extent to which they should retrospectively declare their overtime to the German tax authorities on their own initiative in order to avoid possible penalties.

Finally, it remains to be emphasised that, following the agreement of 11 January 2024, other parts of wages paid by Luxembourg employers to employees resident in Germany that are partially exempt from income tax in Luxembourg should not be covered by the new approach of the German tax authorities. This is the case, in particular, for supplements for night, Sunday and public holiday work, as well as for remuneration which has been reduced by deductions for obtaining costs.

However, it remains unclear how the German tax authorities will treat other income or parts of income that are fully exempt in Luxembourg, such as severance pay provided for in the labor law or that is agreed in a collective agreement.

Other arrangements covered by the amicable agreement of 11 January 2024 concern:

- The breakdown between Luxembourg and Germany of:
  - salaries paid to employees resident in Germany if they carry out their salaried activity both in Luxembourg and abroad;
  - salaries of drivers, locomotive drivers and accompanying personnel active in international transport;
  - compensation paid following a dismissal and/or redundancy plan;
  - unemployment benefits and other benefits paid by Luxembourg institutions to employees or insured persons resident in Germany;
  - the salaries of civil servants and public employees resident in Germany if they carry out their salaried activity both in Luxembourg and abroad;
- Determination of the 34-day non-taxation threshold.

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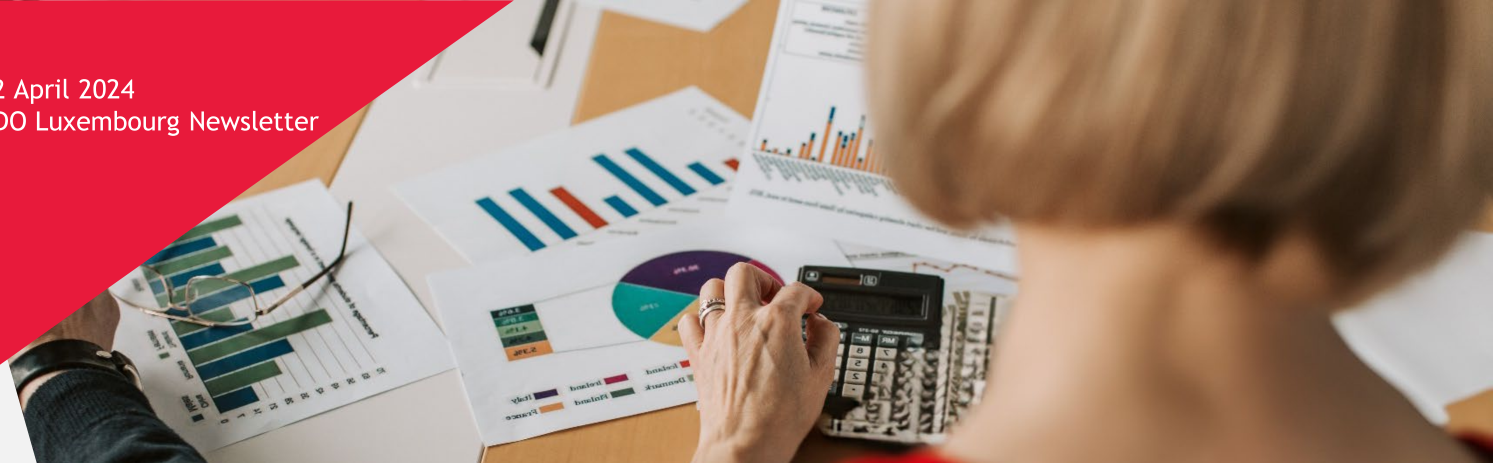

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INTERESTED?

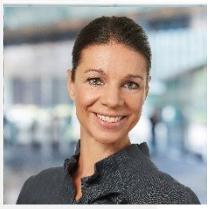
Get in touch with:

Paul Leyder
Partner
+352 45 123 734
paul.leyder@bdo.lu

Patricia Dupuis
Manager
+352 45 123 358
patricia.dupuis@bdo.lu

Ralf Gilch
Manager
+352 45 123 557
ralf.gilch@bdo.lu

Laura de Stefanis
Manager
+352 45 123 579
laura.destefanis@bdo.lu



Christiane Anger
Partner
+49 89 76906 526
christiane.anger@bdo.de

Pia Schreiegg
Consultant
+49 59 76906 517
pia.schreiegg@bdo.de

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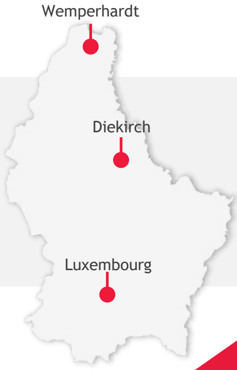

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