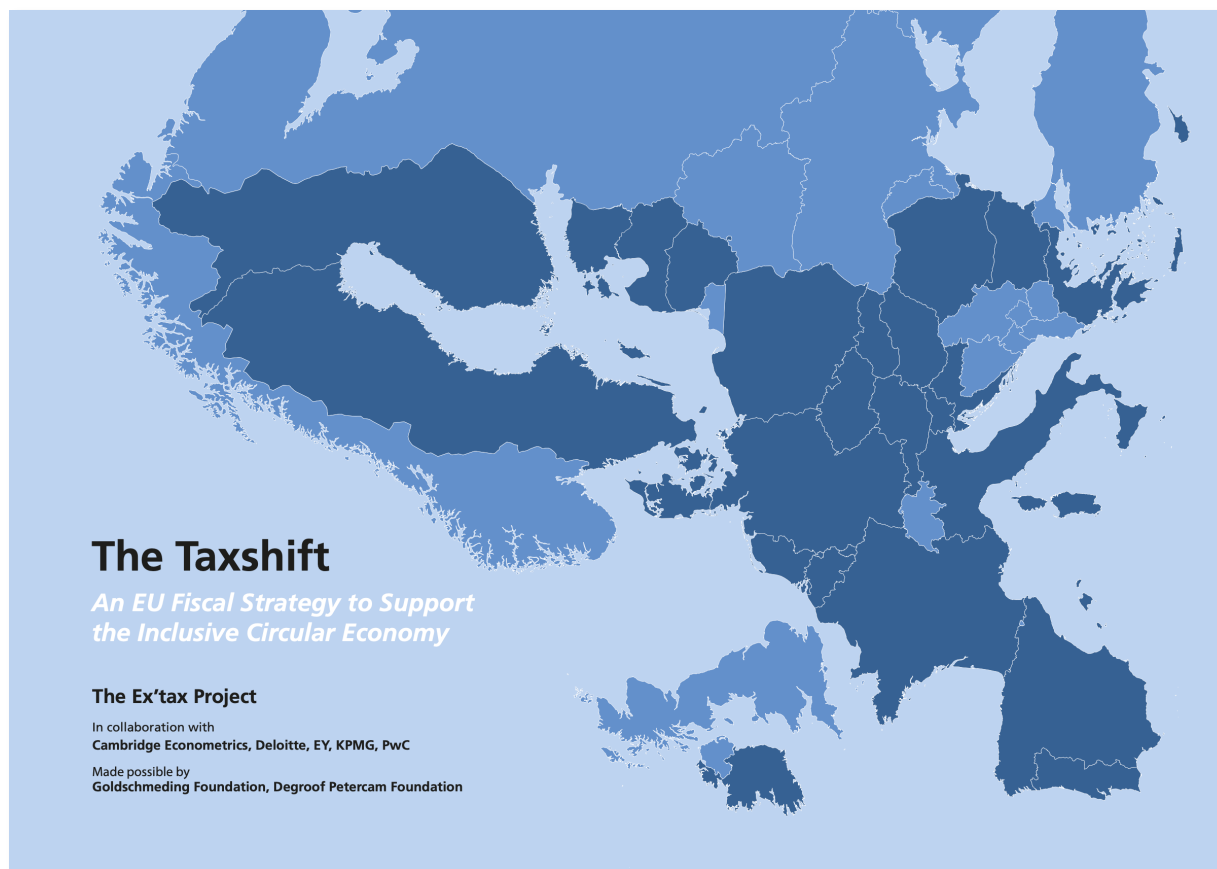




Luxembourg and the Taxshift

Country case study results

Extended case study by The Ex'tax Project Foundation in collaboration with Cambridge Econometrics and the Sustainable Development Committee of Luxembourg (*Conseil Supérieur pour un Développement Durable*)

Executive summary

Full report available at: www.ex-tax.com/reports/eu-country-results-2023

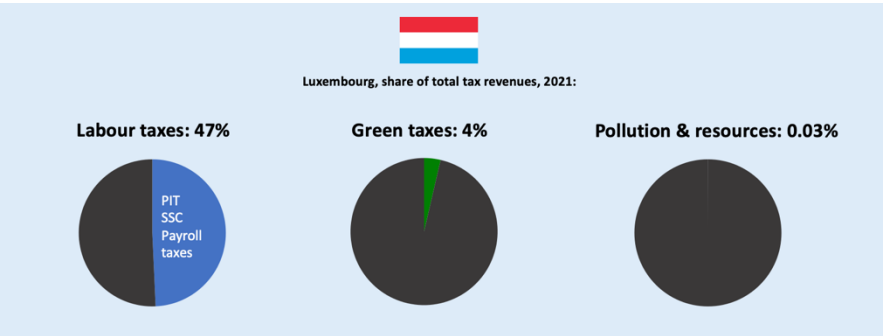
The European Green Deal includes a commitment to shift the tax burden from labour to pollution and resource use. The 2022 study titled *‘The Taxshift. An EU fiscal strategy to support the inclusive circular economy’*¹ presents a roadmap for such a rebalancing of the tax mix, both at national levels and in an EU context. For each of the 27 Member States Cambridge Econometrics has modelled the impacts of a set of example taxshift measures that could shift the tax burden from labour to resource use and pollution.

This document provides information on the scenario and its key impacts in the case of Luxembourg, as reviewed and adjusted based on consultations with the Sustainable Development Committee of Luxembourg (*Conseil Supérieur pour un Développement Durable*) and on additional national statistics provided by STATEC with regard to the Luxembourgish context of frontier work.

Fiscal structure Luxembourg

Among EU Member States, Luxembourg has the second lowest share of environmental taxes, at 1.4% of GDP. And while green taxes provide only 3.8% of total tax revenues, labour taxes provide 47.3% of total tax revenues. A mere 0.03% of tax revenues are based on resource use and pollution. This means that the Polluter Pays Principle is not consistently applied (see Figure 1).

Figure 1: Tax structure Luxembourg



The scenario and its impacts

The scenario under review (see Figure 2) is broad-based and includes 20 measures, each with their own dynamics and impacts. Some of the measures increase costs for business sectors and consumers, as pollution and resource use are priced at increasing rates. Other measures reduce labour taxes, which lowers costs for employers and enhances spending power, especially for the lowest two income quintiles. The net results of these two forces prove to have a positive impact on the economy, society and the environment. In the

scenario, GDP levels in the Luxembourg in 2025 are 0.5% higher and employment levels are 1.4% higher than business as usual. At the same time, CO2 emissions have fallen by 11.6% (see Figure 3).

Figure 2: Tax shift scenario Luxembourg

(€ million, in 2025, difference to baseline, E3ME)

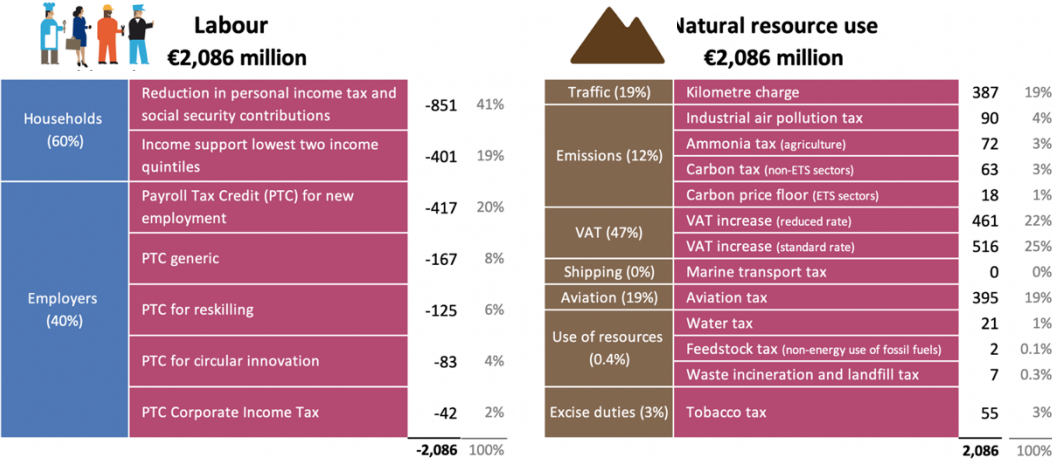
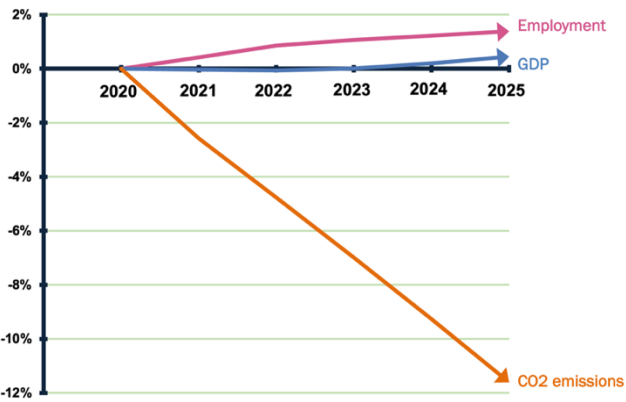


Figure 3: Key modelling results 2021-2025, Luxembourg

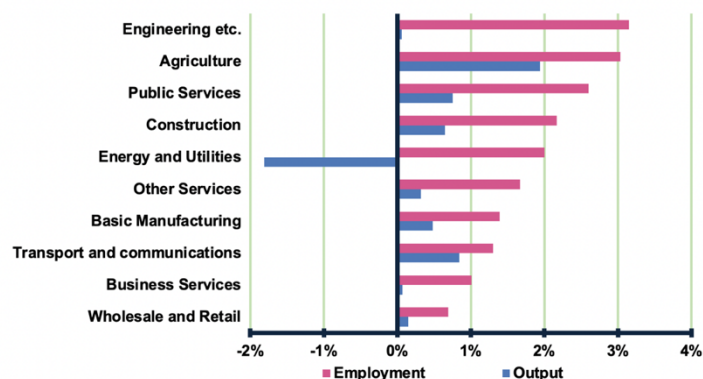
(Difference from baseline, E3ME)



In 2025, compared to baseline, the scenario increases output in all broad sectors except Energy and Utilities (-1.8%). This negative impact is more than compensated by increases in output in other sectors (see figure 4).

Figure 4: Sectoral employment and output in 2025, Luxembourg

(Difference from baseline, E3ME)



Over a five-year period, the scenario shifts a total of €7.3 billion in tax revenues (non-discounted) in Luxembourg. Key cumulative impacts over the 2021-2025 period are (compared to the baseline):

- Adding **€0.4 billion** to GDP
- Adding **23,500 person years of employment** (11,200 of which are likely to be filled by cross-border workers)
- Investing **€183 million** in infrastructure
- Saving **3.8 million tonnes** of carbon dioxide emissions
- Saving **€0.5 billion** on the energy import bill.

The taxshift scenario assumes a gradual introduction of policy measures from 2021 to 2025. By 2025, they are in full force, after which the measures are maintained. GDP and employment continue to increase after 2025 in the scenario, albeit at lower rates than the period between 2021 and 2025.

The results indicate that a budget-neutral taxshift is an effective strategy to align the tax system with the goals of green and inclusive economic growth. Sustainability is becoming a race to the top, with more and more countries and businesses committing to circularity and climate neutrality. Half of all greenhouse gas emissions are related to materials

management activities and the competitiveness of economies will increasingly depend on their resource efficiency. Companies that 'do more with less' will gain a competitive advantage in the current climate. A taxshift levels the playing field for inclusive and circular businesses.

Bridging the gap between national and EU policy

Taxation is, in principle, a national competence: many steps must be taken at national level. However, far-reaching changes could create differences between Member States that have an impact on the Single Market, especially in the case of an open economy such as Luxembourg. Therefore, coordination within the EU is key.

At a national level, all Member States can start gradually implementing the first tax policy options: the low-hanging fruit. While they develop and implement unilateral steps, the preconditions could be created for the next, bigger steps. These should be taken together with neighbouring countries, in coalitions between Member States as well as jointly with the EU27. The proverb 'if you want to go fast, go alone. If you want to go far, go together' applies here.

Based on their national priorities, all Member States could draw up a roadmap prioritising suitable policy options as well as a timeline. Depending on the speed at which the revenue-generating measures are introduced, financial room for tax reductions would develop. The Taxshift report provides several tools to support country-specific scenario planning, including a 'Toolkit' and a roadmap for the Netherlands as an example.

Recommendations for country-specific scenario planning

The taxshift scenario in this study was designed in an EU context. As a next step, the general principle could be taken, and adapted to national circumstances. For Luxembourg, a country-specific scenario and roadmap could be drawn to map suitable policy options and to allow for a macro-economic modelling exercise by the designated national research agencies.

A country-specific scenario will be able to target country-specific challenges. Measures could be designed to resolve specific socio-economic challenges, such as rising income inequality, high housing costs, construction sector labour shortages and labour market opportunities for older workers.

The taxshift offers a unique opportunity to develop consistent, step-by-step tax policies that align financial incentives with Luxembourg's commitments to sustainability and inclusive growth.

¹ The Ex'tax Project (et al.) (June 2022), The Taxshift. An EU fiscal strategy to support the inclusive circular economy. <https://ex-tax.com/taxshift/>