

Recent developments in Belgium: May 2009 – March 2010

ECJ in the cases *Belgische Staat v. KBC Bank NV and Beleggen, Risicokapitaal, Beheer NV v. Belgische Staat* (C-439/07 and C-499/07)

On 4 June 2009, the ECJ gave its judgment in the joined cases *Belgische Staat v. KBC Bank NV and Beleggen, Risicokapitaal, Beheer NV v. Belgische Staat*. Both cases challenge the Belgian participation exemption and the failure to exempt dividends in the scenario where the Belgian parent company has no or insufficient taxable profits. On 12 February 2009, the European Court of Justice already ruled that the Belgian participation exemption conflicts with article 4(1) of EC Parent-Subsidiary Directive where it fails to exempt dividends in *EU situations* (Cobelfret judgment, C-138/07). In the cases *Belgische Staat v. KBC Bank NV and Beleggen, Risicokapitaal, Beheer NV v. Belgische Staat* the ECJ was requested to judge on dividends received in *domestic situations* and dividends received from *third countries*. The ECJ considered that when Belgian income tax law refers to community law for internal situations, it is for the national judge to decide on the exact scope of the reference to community law. The ECJ additionally considered that where under national law, dividends from a company established in a third country are treated less favorably than dividends in domestic situations, the national court must decide, while taking into account the (domestic) legislation and facts, whether the freedom of capital (art. 56 EC Treaty) applies and where appropriate precludes such different treatment.

On 29 June 2009 the Belgian Ministry of Finance published a circular letter to bring the Belgian participation exemption in line with the above mentioned judgments. In the circular letter an extended application of the Cobelfret judgment to domestic situations is confirmed. The application to dividends from third countries remain however unclear.

Preliminary ruling requested from ECJ regarding conditions for exemption of income from foreign investments from supplementary municipal tax

On 26 June 2009, the Court of Appeal Antwerp requested a preliminary ruling from the European Court of Justice in the case of *G.A. Dijkman and M.A. Dijkman-Lavaleije v. Belgische Staat* (C-233/09). Under Belgian tax law, income from foreign investments is exempt from supplementary municipal tax if received through a Belgian intermediary (art. 465 BITC). No such requirement applies for domestic investments (art. 465 BITC). The national court asked whether this requirement and distinction is compatible with the free movement of capital.

ECJ in the case of *Jacques Damseaux v. État Belge* (C-128/08)

The European Court of Justice decided on 16 July 2009, in the case of *Jacques Damseaux v. État Belge* that juridical double taxation in respect of dividends is not incompatible with the free movement of capital. The ECJ observed that as far as no general criteria for the

attribution of areas of competence between EU Member States are laid down in EC law, the free movement of capital does not preclude provisions of a double tax treaty, under which dividends distributed by a company established in one Member State to a shareholder residing in another Member State, are subject to tax in both Member States, where the Member State in which the shareholder resides is not obliged to prevent the juridical double taxation.

New guidelines on functional currency for Belgian intra group finance companies (CAS 2009/10)

In Belgium, a derogation to keep accounts in a currency other than EUR is an important tool to manage foreign exchange risks. The Belgian Commission for Accounting Standards recently published, specifically for finance companies, a flexible set of guidelines to obtain such derogation and to make it easier to manage foreign exchange risks in doing business outside the EUR currency zone. These new guidelines are certainly of importance for multinationals that centralize their finance activities in Belgium to take benefit of the notional interest deduction.

Court of Appeal rejects the application of the Velasquez Doctrine in a non-EU context

According to the Belgian "sequence-rules" (determining the order of loss compensation) Belgian losses or carried forward losses of a Belgian resident company with a permanent establishment in a treaty country are to be deducted from the profit realized by the permanent establishment (approved by the Belgian Supreme Court in the "Velasquez-case" on 29 June 1984 and in practice referred to as "the Velasquez-doctrine").

Joint application of these Belgian sequence rules and double tax treaty rules may unfortunately lead to double taxation in Belgium. However, with reference to ECJ case law ("Amid", C-141/99) the Belgian tax authorities currently accept that Belgian losses or Belgian carried forward losses should no longer be set off against PE exempt profits. However, in practice, it remained uncertain whether a same approach would be accepted in a non EU context. After all, application of ECJ case law (more specifically the Amid case), is in principle restricted to the European Union.

Recent Belgian case law however shows that also in a non EU context good arguments exist to counter the double taxation resulting from the joint application of the "Velasquez doctrine" and treaty rules. More specifically, on 17 September 2009, the Brussels Court of Appeal decided that, for tax purposes, a Belgian resident company, bearing tax losses in Belgium, and having a permanent establishment located outside the European Union, may not be treated equally to a Belgian company making profits in Belgium and also having a PE located outside the European Union.

OECD standards re administrative assistance – exchange of information

Belgium recently signed several agreements, or protocols to existing treaties, on exchange of information; this to implement the internationally agreed tax standards. Agreements are signed, amongst others, with Australia, Denmark, France, Isle of Man, Luxembourg, Monaco, the Netherlands, San Marino, Seychelles, Singapore, United Kingdom, Finland, Norway etc.

Circular letter on Belgian – Emirates double tax treaty, giving raise to tax opportunities

On 5 October 2009, The Belgian tax authorities published a circular letter regarding the application of the Belgium – Emirates (UAE) double tax treaty.

Before, it was unlikely that the Belgian tax authorities would exempt profits realized by a Belgian company which are attributable to a UAE permanent establishment. This was mainly driven by the fact that in most cases UAE profits are not effectively taxed in the UAE.

By publication of the above mentioned circular letter, the Belgian tax authorities clearly changed its reasoning and confirmed that for Belgian companies, UAE profits attributable to a permanent establishment, are exempt in Belgium even if no taxes are paid in the UAE.

For Belgian and international tax practice this gives rise to tax opportunities. Since by using a Belgian company, where in line with the at arm's length principle as much as possible profits are allocated to a UAE permanent establishment, double non taxation may be realized. Important remark however is that Belgian tax authorities, likely will pay an increased attention to profit allocations towards UAE permanent establishments.

European Commission requests Belgium to amend its discriminatory legislation to benefit from the reduced dividend withholding tax rate

On 8 October 2009, Belgium is requested by the European Commission to amend its conditions for the entitlement to the reduced dividend withholding tax rate of 15%.

Under Belgian legislation, share dividends/bearer shares that have, since their issue, been held in an open deposit with a Belgian bank subject to the control authority for the Belgian financial sector as well as share dividends or dematerialised shares held in securities accounts in Belgium, give entitlement to a reduced withholding tax rate of 15% (art. 269, lid 3, b BITC). However, dividends on bearer shares or dematerialised shares held under similar arrangements (open deposit or held in securities accounts) with a financial institution established in another EEA country are currently subject to a rate of 25%.

In addition, dividends distributed by Belgian investment companies are subject to a withholding tax of 15%, while dividends distributed by equivalent investment companies in other EEA countries currently are subject to a withholding tax of 25%.

European Commission requests Belgium to abolish the "fixed financial asset" condition for the Belgian dividend participation exemption

In addition to the above, Belgium is also requested by the European Commission to amend its conditions for the application of the Parent-Subsidiary directive; more specifically the dividend participation exemption (request of 20 November 2009). Besides the Directive condition, where a parent company should own at least 10% of the capital of a subsidiary established in another Member State, Belgium requires that the shareholding qualifies as a "fixed financial asset". Since such additional condition is not contained in the Directive, Belgium has been requested by the Commission to abolish it.

ECJ in the case of *Société de Gestion Industrielle (SGI) v. Belgian State* (Case C-311/08)

On 21 January 2010, the European Court of Justice confirmed the Advocate General's opinion in the case of *Société de Gestion Industrielle (SGI) v. Belgian State* (Case C-311/08) and decided that the Belgian anti-abuse provision regarding abnormal or gratuitous benefits (art. 26 BITC) is not incompatible with the freedom of establishment.

Changes to the Belgian dividend participation exemption

Up to 31 December 2009 Belgium applied the dividend participation exemption, where dividend income is exempt up to 95%, under the following conditions (to be simultaneously met):

- the Belgian company shareholder has to hold a minimum participation of at least 10% or a participation with an acquisition value of at least 1.2 million EUR (minimum holding requirement);
- the participation has to qualify under Belgian accounting law as a fixed financial asset (see in this respect the reasoned opinion of the European Commission, as mentioned above),
- the Belgian company shareholder must have or have had full legal ownership of the participation for an uninterrupted period of at least one year, and
- the subsidiary distributing the dividend must comply with the qualitative taxation rules.

Credit institutions, insurance companies and quoted companies benefited from the participation exemption even if the above mentioned minimum holding requirement was not met. This exception was historically introduced in order to allow credit institutions, insurance companies and quoted companies, (which usually do not hold qualifying participations) to benefit from the dividend received deduction.

During the 2010 budget negotiations however, the Belgium government announced that the exception for credit institutions, insurance companies and quoted companies is no longer justified. The exception is consequently abolished as from assessment year 2010 (income tax year 2009).

Furthermore as from 1 January 2010, the minimum investment amount, for companies that do not have a 10% holding, is increased from 1.2 million EUR to 2.5 million EUR.

In income year 2010 consequently, all corporations (so not only credit institutions, insurance companies and quoted companies), must, in principle, hold a minimum participation of at least 10% or a participation with an acquisition value of at least 2.5 million EUR in order to benefit from the participation exemption.

The abolition of the above mentioned exception and the increase of the minimum investment amount may lead to adverse tax consequences for companies usually not holding substantial participations. Proper tax planning will be recommended since dividend income, for corporations not meeting the conditions, will be fully taxable. Furthermore practice has shown that, even if the minimum holding requirement is met, companies may still face difficulties to prove towards the Belgian tax authorities that the dividends received derive from shares that qualify as fixed financial assets (especially when it concerns participations beneath the 10% threshold). However, since the above-mentioned conditions are not applicable on dividend income distributed and received by Investment Companies (e.g. the Belgian Pricaf), the status of Investment Company can prevent taxation of the dividend (for 95%) and analysis of the fixed financial asset requirement.

Other newly introduced corporate income tax measures:

By Program Law of 23 December 2009, new fiscal measures are adopted and implemented into Belgian tax law. Most important corporate tax measures are:

- *Reporting obligation for payments to companies established in tax havens:*

As from 1 January 2010, direct or indirect payments to companies established in tax havens, where the total amount paid is equal or exceeds 100.000 EUR, are not deductible unless they are reported in the corporate income tax return *and* proof is provided that those payments are based on sound business reasons. In this context, tax havens are defined as:

- companies established in countries that do not respect the minimum OECD standard on transparency and information exchange; and
- companies established in a country with a nominal tax rate of less than 10%. By Royal Decree, a list of these countries will be published.

- *Notional interest deduction:*

Following the budget negotiations, the percentage for the notional interest deduction for assessment year 2011 and 2012 (income tax year 2010 and 2011) is capped at 3.8%. For small companies a rate of 4.3% applies.

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