GSLTR

Global Sports Law & Taxation Reports

Contents

NOLOT

9·4

DECEMBER 2018

Does new case law on a "subject-to-tax clause" in double tax treaties provide opportunities for Belgian sportspersons?

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Introduction

The Belgian Court of Cassation has ruled on 25 January 2018 on the application of art. 23, § 1, a ("methods for elimination of double taxation") of the Belgian-Dutch double tax treaty in the case of a professional cyclist.

The Court has confirmed that the provision does not grant Belgium the right to levy taxes on income in relation to which the taxing rights are allocated to The Netherlands, but which was not effectively taxed in The Netherlands under domestic tax law.

Furthermore, the judgement addressed the method of calculating the portion of the sportsperson's fixed salary which is attributable to activities performed outside of the home state under art. 17[2].

Facts

A professional cyclist – Belgian tax resident – was training and participating in races both in Belgium and abroad. His employment agreement with the cycling team entitled him to a fixed annual salary.

According to the cyclist, his fixed salary was to be allocated to the relevant sports activities performed in the respective performance states outside Belgium using a time-proportionate method, this in line with art. 17 of the relevant double tax treaties. Under this method, the income is allocated to the performances abroad by using a fraction, where the numerator generally consists of the actual number of days in which the sportsperson was present to perform activities in the given state, and the denominator is the total number of working days. The Belgian tax authorities, however, did not agree with the specifics of the taxpayer's calculation.

In calculating the total number of working days, the cyclist had only taken into account the performance days, i.e. race days and team training camps. The Belgian tax authorities, however, also took into consideration the individual training days and set the total number of working days at 220 working days per year. As a result, the portion of the fixed salary attributable to performances abroad was reduced.

The impact can be illustrated by a simplified example. A cyclist – Belgian resident – participates in races and team training camps for a period of 100 days per year, of which 45 days are performed in Belgium and 55 days are performed abroad. The remaining 120 days during which the cyclist performed individual training activities in Belgium (assuming 220 working days per year), are not included in the calculation base. Hence, 55% (55/100) of the income would be allocated to activities abroad and is taxable in the respective performance countries (assuming application of art. 17 of the respective treaties) and 45% (45/100) remains taxable in Belgium. According to the tax administration, however, only 25% (55/220) is attributable to activities abroad, and 75% (165/220) remains taxable in Belgium.

Furthermore, specifically in relation to the portion of the salary attributable to performances in The Netherlands, the Belgian tax authorities refused to allow an exemption (based on art. 17, § 1 and art. 23, § 1, a of the Belgian-Dutch double tax treaty) as the taxpayer was not effectively taxed in The Netherlands.
In their decisions preceding the judgement of the Court of Cassation, the lower courts of Bruges and Ghent (on appeal) agreed that only race days and team training camps (and not individual training days) were to be taken into account in allocating the income to the respective performance states.

With respect to the exemption of the relevant portion of the income derived from the activities performed in The Netherlands, the Court of Appeal in Ghent ruled that arti. 17, § 1 and art. 23, § 1, a of the Belgian-Dutch double tax treaty do not require evidence of an effective taxation in The Netherlands, contrary to the point of view of the Belgian tax administration.

Court of cassation

Art. 17 of the OECD Model Tax Convention

The tax authorities argued that individual training days are, in the same way as team training sessions, necessary in order to be able to compete in a successful manner. These individual training days should thus have been taken into

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2 Cass. 25 January 2018, website www.cass.be (accessed 3 December 2018).

consideration in determining the portion of the fixed salary which is connected to the performances outside Belgium.

The Court of Cassation, however, did not agree with the position of the tax authorities, and ruled that individual training days performed in Belgium can be aimed at preparing for both races in Belgium as well as races abroad. Therefore, it is appropriate to take into account only the team training days and race days and not the individual training days in calculating the portion of the salary attributable to a state abroad.

Elimination of double taxation under Belgian-Dutch treaty

Also, according to the tax authorities, the lower Court (Court of Appeal in Ghent) had violated art. 17, § 1 and art. 23, § 1, a of the Belgian-Dutch double tax treaty by judging that these articles do not require evidence that the relevant portion of the income attributable to the activities in The Netherlands had been effectively taxed there.

On this point, the Court of Cassation first establishes that, based on art. 17, § 1 of the Belgian-Dutch treaty, the taxing rights relating to the portion of the income remunerating the Dutch activities are allocated to The Netherlands, and that Belgium has no taxing rights.

Subsequently, the Court of Cassation refers to art. 23, § 1, a pertaining to the elimination of double taxation, stipulating that, where a Belgian tax resident derives income which "is taxed" in The Netherlands, Belgium shall exempt such income with progression. The Court of Cassation concludes that this article does not grant Belgium the right to levy taxes with respect to income that was not "effectively taxed" in The Netherlands. In other words, according to the Court, this article does not entitle Belgium to taxing rights on income not effectively taxed. According to the Court, the argument according to which Belgium can levy taxes with respect to income that was not "effectively taxed" in The Netherlands, fails.

Analysis

Application of art. 17 of the OECD Model Tax Convention

In the case at hand, there was no dispute regarding the application of art. 17 of the OECD Model Tax Convention with respect to the fixed salary of the cyclist. Both lower courts had confirmed that the entire salary of the professional cyclist falls within the scope of art. 17 and not – not even partially – within the scope of art. 15.

This was not always the case in the past. In a Circular Letter of 27 April 2012[3], the Belgian tax authorities expressed their (often challenged) view that income, derived from training sessions or other preparatory activities in a contracting state, only falls within the scope of art. 17, provided that the activities "are directly linked to specific public performances" of the sportsperson in that state. Income derived from training activities, performed abroad before the start of the season and without a link to a specific sports event in that country, did not fall within the scope of art. 17, but within the scope of art. 15.

The Belgian tax authorities, however, have adjusted their position since the 2014 update of the OECD Commentary, which confirms the application of art. 17 in relation to the fixed salary of the employed sportsperson, also including the salary relating to training periods preceding the competition season.[4]

Allocation of income to activities abroad – calculation method

The horizontal allocation of the taxing rights under art. 17 to the respective performance states and calculation method did cause a discussion in the case at hand.

The historical position of the Belgian tax authorities has always been that, in determining the total number of working days, the number of days mentioned on the individual payslips are to be taken into account. This generally resulted in the tax authorities departing from an estimated number of total working days fixed at 220 days per year (estimated number of working days performed by a regular employee as mentioned on the taxslips) as the denominator of the fraction in the calculation method.

The authorities allowed for alternative calculation methods only if, by way of duly conclusive information, it was shown which part of the annual salary could be linked to specific races or training activities abroad. Also, the alternate allocation method was only accepted if based on "*bona fide grounds common in the relevant sports discipline and not purely driven by tax-inspired motives*".

In the case at hand, the lower courts had already dismissed the tax authorities' point of view, in line with recent case law. Important to stress is that the lower courts hereby focused on the provisions of the employment agreement, which clearly showed that the fixed salary was essentially connected with taking part in the races (and not the training). This method has thus now been also validated by the Court of Cassation.
The Court of Cassation's judgement again stresses the importance of the provisions of the employment agreement with a view to determining the level of taxable income of an international sportsperson in application of art. 17. In order to avoid issues with the Belgian tax authorities, the employment agreement should always clarify the specific activities (both in the country of residence and abroad) in consideration of which a sportsperson is remunerated.

It should be noted that this issue was also addressed in the 2014 update of the OECD commentary, as section 9.2 of the OECD Commentary update confirms that it is:

"[...] *appropriate, absent any indication that the remuneration*

3 Ci.AFZ/2012-0288.

4 Section 9.1.

or part thereof should be allocated differently, to allocate that salary or remuneration on the basis of the working days spent in each State in which the entertainer or sportsperson has been required, ***under his or her employment contract,*** *to perform these activities."* (Emphasis added).

Taxation condition in the Belgian-Dutch double tax treaty

Art. 23 § 1, a of the OECD Model Tax Convention stipulates that the state of residence must allow an exemption if the income "may be taxed" in the other state. According to this provision, the exemption applies irrespective of whether the income was effectively subject to tax in the source state or not. A number of Belgian double tax treaties, however, deviate from the OECD Model Tax Convention (amongst which the Belgian-Dutch double tax treaty) and stipulate that Belgium only is to exempt the income if it "is taxed" or "effectively taxed" in the other contracting state.

The scope of the wording "is taxed" has often been discussed in Belgian case law (e.g. Court of Appeal of Antwerp 21 June 2011 and Court of Appeal of Mons 31 October 2015). In line with older jurisprudence of the Court of Cassation ("Sidro"-judgement of 12 September 1970), the Belgian tax authorities consider an item of income being "taxed" in the event that it was "subject to a tax regime" in the source state. Following the "Sidro"-case, a number of scholars, and even the tax authorities in their Circular of 6 April 2010, confirmed that an income can also be considered "subject to a tax regime" if a partner state's legislation explicitly provides for an exemption of that type of income under specific circumstances.

In the case at hand, the Court of Cassation did not make reference to its judgement in the "Sidro"-case, nor did it take a position on whether the income of the professional cyclist could be regarded as "made subject to a tax regime" in The Netherlands. It should be noted that The Netherlands grants an explicit exemption with respect to income of foreign artists and sportspersons. We, therefore, tend to conclude that also the income derived by the Belgian professional cyclist in relation to his activities in The Netherlands, but which remained explicitly exempt there, could be considered "subject to a tax regime" and is thus indeed to be exempt in Belgium in accordance with art. 23 § 1, a of the Belgian-Dutch double tax treaty.

The Court's judgement, however, does not provide an analysis of the matter in light of its 1970 case law. It is limited to a mere reference to the text of art. 23 § 1, a of the Belgian-Dutch double tax treaty, subsequently concluding that this treaty provision does not grant Belgium the right to levy taxes on income that was not effectively taxed in The Netherlands.

The Advocate-General's conclusion also offers few insights here. It focuses mainly on refuting one of the arguments raised by the tax authorities, whereby reference is made to the definition of "taxed" included in the Joint Belgian-Dutch Commentary on the treaty in the context of art. 21 of the double tax treaty. This Joint Commentary provides that "taxed" in the context of art. 21 is to be read as "effectively taxed". It is, however, clear that the rationale and methodology of art. 21 are entirely different to that of art. 23, entailing that the definition of "taxed" under one article cannot be extended to the other. This was also confirmed by the Advocate-General.

Finally, the Court of Cassation also neglected to make any reference to art. 3 § 2 of the Belgian-Dutch double tax treaty. This article provides that, as regards the application of the Convention by a contracting state, any term not defined therein shall, "*unless the context otherwise requires*", have the meaning under the domestic laws of that state. *The context* as mentioned includes the common purpose of the contracting states when signing the treaty (section 3.12 of the OECD Commentary). Analyzing the scope of the concept of "*is taxed*", applying the methodology as referred to in art. 3 § 2 and understanding whether an autonomous interpretation is in place, should have been the first step to be taken by the Court.

Conclusion

The Belgian Court of Cassation rendered a noteworthy judgement regarding the application of the provision on elimination of double taxation in the Belgian-Dutch double tax treaty.

According to the Court, Belgium is to provide exemption in relation to the income of which the treaty grants The Netherlands with the taxing rights, regardless of whether the income is effectively taxed in The Netherlands. The judgement, however, unfortunately lacks profound considerations and analysis of this longstanding issue.

The impact of this judgement cannot be underestimated. Belgian tax resident sportspersons and entertainers may find themselves being able to claim a treaty exemption in Belgium in relation to the portion of their income derived from the activities performed abroad, without the requirement of being effectively taxed in that concerned state. This is not only relevant for Belgian sportspersons or entertainers performing activities in The Netherlands, but also for those active in the other contracting states with whom Belgium has concluded a treaty providing a similar wording (e.g. Hong Kong). It should be noted, however, that the Belgian tax authorities meanwhile issued a circular[5] opposing the judgement and confirming their historical position on the matter. Discussions with the tax authorities on the matter are thus still very likely to be settled in court.

As to the allocation of a Belgian sportsperson's income to his activities performed abroad, the judgement does provide answers on how to calculate the exempt portion of the income. Assuming this corresponds with the wording of the employment agreement, only the competition days (and team training days) are to be taken into account, regardless of the individual training days spent in Belgium. This can be very beneficial for Belgian tax resident sportspersons mainly competing abroad.

5 2018/C/94 of 20 July 2018.