



The unbearable lightness of the expatriate tax regime

The media recently reported that the Court of Auditors had criticised Belgium's special tax regime for foreign executives. The news is not all as bad as it sounds.

The Court of Auditors is the Belgian State's auditor. It audits the accounts of the Government and reports to the Federal Parliament. At the end of February, it published a report on the "expatriate tax regime".

Admittedly, the term "expatriate" sometimes has a derogatory connotation. However, this is what the "special tax regime for foreign executives who are temporarily seconded to Belgium" has been called for the last twenty years and it is substantially shorter than its official name.

Everyone has heard of it, but what is this expatriate tax status? In short, it allows the Tax Authorities to treat foreign executives who are living and working in Belgium as if they were non-residents. It sounds contradictory but if foreign executives can demonstrate that they have kept the centre of their economic interests abroad, the Tax Authorities will give them a letter confirming that they are not to be taxed as Belgian residents.

How can you have your centre of your economic interests abroad if you have come to Belgium to live and work here? The Belgian Tax Authorities give you a couple of clues. Prove to us that your husband or wife and/or children are still living abroad, that you have a family home abroad, that your children are being educated abroad, that you have savings accounts and/or life insurance policies abroad, or that you continue to be liable to social security abroad, and we will give you expatriate tax status.

There is a double benefit to being considered as an expatriate for tax purposes.

First, as an expatriate, you are entitled to a number of tax-free allowances intended to cover the higher cost of coming to and living in Belgium. In the year of arrival in Belgium and in the year of departure, you are entitled to receive allowances to cover, among other things, moving costs, to cover the loss you made on the sale of the house you sold before you came to Belgium, the cost of furnishing your new home in Belgium.

More importantly, as an expatriate, you are entitled to a number of annual allowances to cover the fact that it is more expensive to live in Belgium than in your country of origin. Your employer can pay you a *cost of living allowance* (because you will, almost inevitably, make the mistake of shopping in the more expensive shops), a *housing allowance* (because rent is supposedly more expensive here, particularly if you have an accent), a *tax equalization allowance* (because Belgian tax is higher than in your country of origin) and a travel allowance to allow you to go home once a year.

These allowances are usually calculated by your employer's tax adviser and are based on criteria agreed with the tax man. However, there is a ceiling on these annual allowances, of € 11,250 per year or € 29,750 for employees working in a coordination centre or in a research lab. The employer can also reimburse the school fees for the expatriate's children without any limitation.

None of these allowances are taxable.

The second part of the tax benefit is that expatriates are deemed not to be resident in Belgium.



This means that they can only be taxed in Belgium on the earnings they receive for their work in Belgium. More particularly, this also means that they are not liable to tax in Belgium on any other income, such as the income from their investments or their earnings for work outside Belgium. For example, if they can prove that they spend 40% of their working time travelling outside Belgium, they will only pay tax in Belgium on 60% of their earnings. Many expatriates have discovered how much sense it makes to maximise their travelling abroad.

The Court of Auditors' report makes interesting reading. It highlights the fact that, if an employer wants to give his employee a net annual income of € 75,000, the gross cost for the employer of an expatriate with a 40 % travel allowance is € 148,453 instead of € 224,068.

It is not surprising that the expatriate tax status has proven very successful. The Court of Auditors calculated that, on average, an expatriate executive receives about half of his salary tax-free. The number of applications for expatriate tax status has doubled in the last six years, reaching a peak of 4.000 in 2000. Moreover, about half of the 40.000 non-resident individuals who are liable to Belgian income tax, are non-resident under the expatriate tax regime. All in all, the cost of the expatriate tax regime in uncollected income taxes for the Belgian State is about € 1,140 million per year.

It is hardly a surprise that the Court of Auditors, therefore, has serious reservations about the tax regime.

The Belgian expatriate tax regime is an outsider in Europe. Whereas other countries only give their expatriates a reduced tax rate or a tax exemption for certain allowances, Belgium gives them full tax exemption for all foreign source income. This can only encourage executives to travel outside Belgium. The Court of Auditors finds this inconsistent with the aim of the expatriate tax regime. The idea was to attract foreign investments to Belgium and to make it attractive for highly paid executives to come and work *in* Belgium.

More importantly, the Belgian tax regime is the only one that does not set any effective cap on the potential tax benefits available to foreign executives, apart from the € 11,250 ceiling for annual allowances. The Court of Auditors found some extreme cases where foreign executives were almost totally exempt from tax without any limitation in time.

The Court of Auditors discovered that the department within the Ministry of Finance that examines the initial applications for non-resident status is seriously understaffed. . With such limited resources the department can only carry out a brief check to see whether expatriates have maintained the centre of their economic interests abroad. The department cannot really check that the foreign executive really intends to stay in Belgium for a short time only, which is precisely the presumption on which the expatriate tax regime is based. Moreover, there is hardly any exchange of information between Belgian and other national tax authorities. This means that foreign tax authorities are often not aware that they might have the authority to tax income which is not taxable in Belgium, under the double taxation treaties they have concluded with Belgium.

The Court of Auditors considers that the limited number of effective tax audits carried out by the Belgian authorities gives expatriates the impression that they are not controlled. It feels that the ease with which foreign executives can claim the exemption for foreign travel is an ideal breeding ground for fraud.

Finally, and in line with numerous authors over the last twenty years, the Court of Auditors questions the legality of a special tax regime that was introduced in 1983 by way of an



Administrative Note from the Tax Authorities. It is true that the Belgian courts have hardly ever questioned the validity of the Administrative Note, but this may change when the Court of Arbitration renders a decision in a case currently pending before it. In this case, a Belgian executive claims that he was being discriminated against, as he was not entitled to the tax exemption for school fees available to foreign executives.

In its report, the Court of Auditors has made some recommendations for changes to the present system. The present tax advantages should be capped and limited in time and the percentage of the travel exclusion should be limited. Structurally, tax audits should be organized more effectively and information should be exchanged with foreign tax authorities.

The report can be found at http://www.courdescomptes.be/pdf/2003/fevrier_2003_cadres_etrangers.pdf

In his response to the report, the Minister of Finance, Didier Reynders, did not appear overeager to change the current system. The Minister does not propose any structural changes. He expresses the belief that the new system of tax rulings and the reform of the tax administration that his administration has devised should solve the problems. He insists that one must not forget that a small economy has to make its tax regime competitive and attractive for foreign companies. It is true that he is currently trying to sell Belgium to multinational companies as a place to invest in Europe and the expatriate tax regime is one of his trump cards.

A bad idea, of course, a couple of months before a general election.

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