The Belgian Supreme Court decides that old stock option plans are tax-exempt

In 1999 Belgian adopted a new tax regime for options granted under an employee stock option plan (ESOP) ; the old tax regime had proven entirely inadequate.

It was only in 1984 that the Belgian Parliament introduced legislation to tax the fringe benefit obtained by an employee under an ESOP (art 45 Act of 27 December 1984). In fact this legislation did not as such introduce a tax on the fringe benefit relating to a stock option ; it stated that capital gains realised by a beneficiary under an ESOP would be tax-exempt under certain strict conditions. The new text stated that if stock options had been granted in accordance with these conditions, and where they qualified as a taxable fringe benefit, the beneficiary would not be taxed on the capital gain which he realised at the time he exercised the option.

However, the fact that the tax law added a qualification ('where these options are a taxable fringe benefit') gave tax lawyers an opportunity which they grabbed with both hands.

They argued that the capital gain as such was not a taxable fringe benefit under the tax legislation as it stood then. The taxable event should have been the transaction whereby the employer granted the option to the employee, and under the legislation then, this transaction was not liable to tax. Moreover, they said, once the option had been granted, it fell into the individual's private estate and capital gains made on one's private estate cannot be taxed.

As the conditions for the exemption were rather rigid, very few companies set up stock option plans, which complied with these conditions. They relied upon the advice given by their tax lawyers, and did not declare a fringe benefit for their employees when an option was given.

Following the rally on the stock markets, and the resurgence of stock option plans, the Government introduced new legislation in 1999. It completely changed its approach. Under the new tax regime, the tax would be levied on the value of the stock option when it was granted and a favourable valuation would be used, in particular if the beneficiary would refrain from exercising his option for at least three years.

When it commented the 1999 legislation, the Conseil d'Etat clarified that the new legislation made a correct application of the law and that the old legislation disregarded the common rules of tax law.

However, this did not solve the problem of the old stock option plans. Did the employee have to pay tax on the capital gain realised once he exercised his option ?

The Tax Authorities assumed they did and many employees found themselves in a position where they had to challenge a tax claim. At first, the courts seemed to confirm that the capital gains were not subject to tax. The Court of Appeal of Antwerp decided on 23 October 2001 that it was not because the law introduced a provision exempting the gains from stock options, that one could conclude, a contrario, that the gains were taxable in the first place.

The Court of Appeal in Brussels decided otherwise: it stated that the Parliament had deemed the capital gain to be a taxable fringe benefit when it adopted the 1984 legislation, that the employee's exercising the option revealed the capital gain and that this was the taxable event, and that this taxable fringe benefit was only exempted if the conditions of art 45 of the Act of 27

December 1984 were met (see Brussels, 2 May 2001 and 7 June 2002, also Antwerp 19 February 2002 and Court of First Instance Brussels 14 March 2002).

On 16 January 2003, the Belgian Supreme Court, the *Cour de Cassation*, handed down a decision that overruled the decision of the Court of Appeal of Brussels of 2 May 2001. It looked at the abstracts of the Parliament's discussions and found that the Parliament had not intended to decide whether the gain resulting from the exercise of the option was or was not taxable, and that it only defined the conditions under which this gain would be exempted.

The Supreme Court stated that in order to determine whether the employee receives a taxable fringe benefit, one should place oneself at the time the option was granted. The Cour de Cassation also confirmed that the capital gains which an employee may realize when he exercises his option, are the result of the variations of the value of the shares, and not of the work he has done for an employer. As such they could not be liable to tax. This decision is not entirely unexpected. On 4 February 2002, the Cour de Cassation had already taken the same decision for the application of the social security.

This decision has the benefit of being clear; it does not leave the courts of appeal much choice but to decide in favour of the taxpayer. However, it does not indicate how the value of the benefit must be calculated, but in general this does not matter anymore, as most (old) options have been granted more than five years ago, so that the Tax Authorities are time barred from claiming back tax.

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