www.taxbites.be

Reprinted from *Tax Notes Int'l*, March 19, 2007, p. 1055

taxanalysts tax notes international

(C) Tax Analysts 2007. All rights reserved. Tax Analysts does not claim copyright in any public domain or third party content.

# News Analysis: Belgium Uses Tax Treaties to Attract Investment

*by Marc Quaghebeur*

Belgium uses its tax treaty network to enhance the country's position as an attractive location for holding and group financing companies.

In his March 2 meeting with Russian President Vladimir Putin, Belgian Prime Minister Guy Verhofstadt seems to have pulled off a similar feat to that of Finance Minister Didier Reynders during Reynders's January 2006 visit with U.S. President George W. Bush. Renegotiating the Belgium-U.S. income tax treaty was not on the list of items agreed upon by Belgian and U.S. diplomats in January, but Bush reacted to renegotiating the U.S. tax treaty by quipping, "If that means we both pay less tax, that's great." And on November 27, 2006, Belgium and the United States signed a new income tax treaty.

And now, after meeting with Putin at his Novo-Ogaryovo residence, Verhofstadt announced that Belgium and Russia would soon start negotiations on a new double tax treaty.

## Belgium-U.S. Tax Treaty

Verhofstadt expressed his hope that Belgium's negotiations with Russia would be as speedy as those with the United States. Negotiations with the United States proceeded quickly, and Belgium obtained a zero rate withholding tax on dividends, but at a cost. U.S.-source dividends will be exempt from U.S. withholding tax if the beneficial owner is a Belgian resident company owning directly or indirectly at least 80 percent of the voting power in the company paying the dividends for 12 months before the dividend attribution. An extensive limitation on benefits test must be satisfied.

Under the new treaty, Belgian-source dividends will be exempt from Belgian withholding tax if the beneficial owner is a U.S. resident company that owns directly at least 10 percent of the capital. The participation must have been held for 12 months before the dividend attribution.

The Belgian government on March 1 adopted a draft bill to ratify the new U.S. tax treaty. In light of the upcoming federal Parliament elections, which will be held on June 10, it is unlikely that the treaty will be ratified soon. Moreover, the bill may have a bumpy ride through Parliament because Reynders has made significant concessions in the treaty.

Although President Bush agreed to renegotiate the Belgian double tax treaty, the U.S. Treasury was not keen to do so. The U.S. Treasury previously terminated discussions regarding a new treaty because the Belgian negotiators were refusing to budge on Belgian bank secrecy rules. U.S. Treasury policy is to agree to a zero rate withholding tax on dividends only if the tax treaty includes limitation on benefits and information exchange provisions that meet the highest standards and if the overall balance of the agreement is appropriate. (For testimony of U.S. Treasury Deputy International Tax Counsel Patricia Brown on U.S. treaties, see *2006 WTD 23-7* or *Doc 2006-2092*.)

Under Belgian law, Belgian banks cannot give information about their clients to the tax authorities. However, fiscal bank secrecy is being eroded by new money laundering rules, and the Belgian Parliament in 2006 adopted a law providing that banks could no longer invoke the privilege in dealings with tax collectors.

The U.S. Treasury insisted that new provisions be included in paragraphs 5, 6, 7, and 8 of article 25 of the new treaty, which will require Belgium to change its tax legislation. The Belgian tax authorities would then have the power to ask for the disclosure of tax information and to conduct investigations and hearings beyond the applicable statute of limitations under Belgian domestic tax law. If a

www.taxbites.be



(C) Tax Analysts 2007. All rights reserved. Tax Analysts does not claim copyright in any public domain or third party content.

person refuses to give information requested by the United States, Belgium would have the power to bring appropriate enforcement proceedings.

Given that the standard applicable statute of limitations for investigating tax returns is three years, and five years for tax fraud, ratifying the double tax convention will require a substantial change in Belgian tax procedures.

Under article 10(12) of the new convention, the benefit of the zero withholding tax rate will automatically end after six years unless the U.S. Senate is satisfied that Belgium has complied with its obligations under article 25. Moreover, the United States has reserved the right to withdraw the benefit of the zero rate for Belgian parent companies if Belgium's actions regarding articles 24 and 25 materially alter the balance of the benefits of the convention.

## Zero Rate for Dividends

While the signing of the new Belgium-U.S. income tax treaty was an important message to potential U.S. investors, a tax treaty is not required to enable investors to repatriate profits tax-free. Indeed, with effect from January 1, 2007, Belgium has extended the benefits of the EU parent-subsidiary directive[1] to parent companies established in a country that has signed a double taxation convention with Belgium. In accordance with the directive, parent companies established in one of the 27 EU member states[2] already enjoy an exemption from withholding tax on the payment or distribution of dividends from a Belgian company in which they hold a 15 percent direct participation.

To qualify for the withholding tax exemption, the parent company must be resident in a country with which Belgium has signed a double tax treaty and must have a corporate legal form analogous to one of the forms listed in the annex to the directive. Most corporate legal forms exist in one or more EU member states. The parent company must hold a direct participation of at least 15 percent[3] in the capital of the Belgian subsidiary for an uninterrupted period of 12 months.[4] The exemption also applies if the parent company undertakes to hold the participation for 12 months after the distribution of the dividend.

Similar measures already apply in Denmark, the Netherlands, and Spain. If they can claim the benefit of the directive, parent companies in treaty countries not only avoid the 15 percent, 10 percent, or 5 percent withholding tax under the applicable convention, but also the general limitation on benefits provisions that are in most double taxation conventions.

Under the specific limitation on benefits test, the parent company must be liable to corporate income tax and must not enjoy a tax regime that substantially departs from the ordinary tax regime. Moreover, the tax treaty (or other agreement) must provide for an adequate exchange of information for the proper application of domestic tax legislation in the contracting states. The government has said the only countries that would be excluded are some of the former Soviet Union republics — Kyrgyzstan, Moldova, Tajikistan, and Turkmenistan. Switzerland may not have an adequate double taxation convention, but a Swiss parent company would normally qualify for the zero rate by virtue of the agreement between the European Union and the Swiss Confederation of October 26, 2004, if it has held a participation of 25 percent of the capital of a Belgian company for at least two years without interruption.

## 10 Tax Rules

A combination of 10 tax rules makes Belgium an attractive location for holding companies and group financing companies.

### Capital Duty

Belgium does not charge a capital duty when a company is incorporated or when its share capital is increased.

### Zero Rate on Inbound Dividends

Belgium has implemented the EU parent-subsidiary directive so that tax is not withheld at

---

[1]Council Directive 90/435/EEC of July 23, 1990, on the common system of taxation applicable in the case of parent companies and subsidiaries of different member states (O.J., L 225, August 20, 1990, p. 6-9, as amended by Council Directive 2003/123/EC of December 22, 2003 (O.J. L 7, January 13, 2004, p. 41-44); see http://www.europa.eu/scadplus/leg/en/lvb/l26037.htm.

[2]The European Union includes Austria, Belgium, Bulgaria, Cyprus, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Latvia, Lithuania, Luxembourg, Malta, the Netherlands, Poland, Portugal, Romania, Slovakia, Slovenia, Spain, Sweden, and the United Kingdom.

[3]The minimum participation will be reduced to 10 percent on January 1, 2009, under Council Directive 2003/123/EC.

[4]The exemption requires that a certificate be delivered to the subsidiary which confirms that the parent company qualifies and has held the required minimum participation for at least one-year. Moreover, if the parent company has held the participation for less than a year, the Belgian subsidiary must retain the withholding tax until the end of the one-year period.

www.taxbites.be



(C) Tax Analysts 2007. All rights reserved. Tax Analysts does not claim copyright in any public domain or third party content.

source on dividends paid from an EU subsidiary in which the Belgian company holds a 15 percent participation (10 percent starting in 2009) for at least a year.

In 2006 Belgium signed, in addition to the tax treaty with the United States, double tax treaties with Macau and Singapore providing for a zero rate on dividends if the beneficial owner is a company resident in the other contracting state that is holding a 25 percent participation for at least 12 months.

### Zero Rate on Inbound Interest and Royalties

Belgium has also implemented the interest and royalty directive. Tax is not withheld at source on the payment of interest or royalties from related EU companies in which the Belgian company, or a related third EU company, holds a 15 percent participation (10 percent from 2009) for at least a year.

### VAT Group Treatment

On April 1, Belgium will allow a group of companies to be considered as a single VAT payer, so that transactions between group members remain exempt from VAT. This may result in significant VAT savings, particularly to VAT-exempt or mixed taxpayers — for example, banks, insurance companies, and real estate businesses.

### Belgian Holding Company Regime

Belgium does not have a specific holding company regime, but the general corporate income tax system provides for a 95 percent exemption for dividends received from qualifying participations and a full exemption for capital gains on participations. The Belgian holding company must have a participation of either 5 percent of the nominal share capital of the subsidiary, or an acquisition value of €1.2 million or more. For the dividend exemption, the subsidiary must meet a "subject-to-tax" condition.

Belgium has lenient thin capitalization rules and no controlled foreign corporation rules.

### Minimizing Corporate Income Tax Liability

All Belgian or foreign companies can benefit from the risk capital deduction (notional interest deduction), regardless of their activities, if their profits are subject to the Belgian ordinary corporate income tax regime. The deduction is 3.781 percent of the company's equity (that is, the company's share capital and retained earnings, with some exceptions to avoid double dipping). (For prior coverage, see *Tax Notes Int'l*, June 20, 2005, p. 1035.)

The risk capital deduction can be combined with other tax exemptions such as the tax exemption for staff assigned full time in Belgium: to scientific research or the development of the technological potential of the company; or to the head of the export or "total quality management" department. The exemption is €25,570 if the person recruited is a highly qualified researcher assigned to scientific research. Corporate income tax payers are also entitled to a tax exemption of 150 percent of the funds that they invest in the production of Belgian audiovisual work; the investment is limited to one-third of their taxable profits before tax, and further limited to €750,000. The tax exemption can be carried forward indefinitely.

### Advance Rulings

Belgium has made its ruling practice more efficient, business-minded, and proactive; the advance rulings delivered by the Ruling Committee provide greater certainty in tax matters. (For prior coverage, see *Tax Notes Int'l*, Jan. 8, 2007, p. 53.) The Ruling Committee can provide rulings within three months of an application for an advance ruling.

### Extensive Tax Treaty Network

Belgium has a tax treaty network covering the major economies as well as most emerging economies, totaling 87 states, including: Argentina, Australia, Brazil, Canada, the People's Republic of China, Egypt, India, Indonesia, Israel, the Republic of Korea, Kuwait, Malaysia, Mexico, Pakistan, Russia, Singapore, South Africa, Thailand, Turkey, Ukraine, the United States, Venezuela, and Vietnam.

Belgium prides itself on having the first comprehensive double tax treaty with Hong Kong, which allows Belgium to position itself as a gateway for the repatriation of profits from the Far East. The tax treaty exempts dividends from withholding tax if the beneficial owner is a company resident in the other contracting state holding a participation of 25 percent for at least 12 months. Dividends from a Hong Kong subsidiary are not liable to withholding tax in Hong Kong,[5] and they qualify for the dividend exemption under the Belgian holding company regime. Alternatively, a Belgian company that has a permanent establishment can repatriate its profits tax-free, even if the majority of the profit consists of offshore income (including royalties and interest) that is tax-exempt in Hong Kong. (For prior coverage, see *Tax Notes Int'l*, Apr. 8, 2005, p. 201.)

### Zero Rate for Outbound Dividends

As explained above, dividends paid to a parent company in an EU member state or in a treaty partner state are exempt from withholding tax if the parent company holds a direct participation of at least 15 percent (10 percent in 2009).

---

[5]Hong Kong does not have a dividend withholding tax.

www.taxbites.be



(C) Tax Analysts 2007. All rights reserved. Tax Analysts does not claim copyright in any public domain or third party content.

### Zero Rate for Outbound Interest and Royalties

In accordance with the interest and royalty directive, tax is not withheld on the payment of interest or royalties to related EU companies. Under double tax treaties, Belgium generally reduces to 10 percent or 15 percent the interest paid. As for royalties, they are exempt if paid to Iceland, Liechtenstein, Norway, South Africa, Switzerland, some former Soviet Union republics under the Soviet Union tax treaty, and the United States.

Generally, Belgium exempts interest on loans paid to foreign entities by Belgian group financing companies. These are Belgian companies or permanent establishments that exclusively, or mainly, provide financial services to the exclusive benefit of group companies. They must be financed exclusively by legal entities outside Belgium (with the exclusion of individuals), and they are not allowed to hold shares for more than 10 percent of their net assets.◆

♦ *Marc Quaghebeur, partner, Vandendijk & Partners, Brussels*