Belgium

Branch Reporter
Steven Claes*

Summary and conclusions

Belgium has no generally applicable controlled foreign company (CFC) legislation. The Belgian tax regime nevertheless contains multiple general and specific provisions that allow the Belgian tax authorities to counter tax planning techniques through which Belgian corporate taxpayers attempt to route passive income to foreign low-tax jurisdictions.

While these provisions do not always exclusively apply to intra-group transactions, nor solely target the sheltering of passive income in foreign low-tax jurisdictions, most of them do counteract or neutralize the benefits of using foreign low-tax jurisdictions, entities or regimes. Some provisions are applicable only to passive income whereas others are applicable irrespective of the nature of the activity conducted or the income generated abroad.

Some of these provisions are rather complex and leave room for debate as to their exact scope and application. They have to be applied within the limits and boundaries of the Belgian Constitution, EU principles and applicable tax treaties.

1. Introduction

1.1. Scope

The object of this contribution is to analyse and describe whether and how Belgium approaches and possibly counters tax planning techniques through which Belgian corporate taxpayers attempt to route passive income to foreign low-tax jurisdictions. In this context, passive income is mainly to be understood as interest, dividends, royalties and capital gains, where it is allocated to a low-taxed company or branch within the group. It could also cover the remuneration for rather passive "activities" conducted by such a company or branch, i.e. management fees and (re-)insurance premiums. Passive income is typically derived from highly mobile assets which can be "easily transferred" within a group of companies. The concept of "a group of companies" should not be limited to parent–subsidiary (first tier) or

* Tax Partner Ernst & Young Belgium

head office–branch type relations, but should include all relations between entities in a broadly defined corporate grouping.

1.2. General regime

Belgian companies are, in principle, taxed on their net worldwide income, but with relief under certain conditions to avoid double taxation on domestic or foreign source income. They are allowed to deduct from their profit expenses incurred in order to obtain or safeguard taxable income. For example, interest and royalty payments are under certain conditions tax deductible, irrespective, in principle, of whether the recipient is a Belgian or foreign tax resident. Under certain conditions the Belgian withholding tax on these payments is reduced or brought down to nil.

The fiscal autonomy of business entities having separate legal personality, with respect to their shareholders or owners, is generally accepted in Belgian income tax law. As a matter of principle, the Belgian tax authorities (TA) have to respect the existence of a validly incorporated domestic or foreign company (FC). As a consequence, profits of subsidiaries will only be taxed in the hands of the Belgian parent company upon distribution of these profits in the form of a dividend.[1]

Therefore, a Belgian company will generally benefit from a deferral of taxation on the profits realized by its Belgian or foreign subsidiary. The Belgian parent company may, additionally, be eligible for a 95 per cent deduction for dividends received or a 100 per cent exemption on capital gains realized on shares, irrespective of their source. In other words, the tax deferral may become a permanent exemption.

Profits realized through a foreign permanent establishment (PE) will, in principle, be fully taxed at the level of the Belgian company. There is no domestic relief although the taxes paid abroad are deductible from the Belgian tax base. Income tax treaties concluded by Belgium will, however, generally provide for an exemption of PE profits. The majority of these treaties do not make the exemption dependent on an effective or minimum foreign tax, nor is there a switch-over to a credit regime.

Despite the fact that such a regime might indeed tempt Belgian companies to route passive income to foreign subsidiaries or branches located in low-tax jurisdictions, Belgium has no generally applicable CFC legislation.[2] The Minister of Finance has explicitly stated that he was not eager to introduce CFC rules due to the complexity of such a regime.[3] Furthermore, as a matter of policy[4] the Belgian government argues that CFC legislation is not compatible with the OECD model[5] and considers certain consequences of it in breach of the EU freedom of establishment.[6] Interesting as well is that the Minister of Finance and the Ruling

1 Brussels, 4 June 1974, *JDF*, 1975, 82.
2 The Parliamentary Commission for Fraud was very much in favour of introducing a CFC regime (DOC 52 0034/004, 268–269).
3 Question No. 109, 10 February 1986, *Bull.Bel.*, 1986, 1600.
4 The fact that e.g. the former Belgian coordination centres and more recently the NID regime might be hit by foreign CFC measures most likely explains this view.
5 Com.OECD Model, art. 1§27.4; art. 7§66 and art. 10§68.1.
6 Concl. Advocate General in C-298/05, 6 December 2007, *Columbus Container Services*, Nos. 59, 132 and 161.

Commission (RC) in certain instances have accommodated taxpayers in helping to satisfy the subject to tax requirements imposed by the country of a parent company, in its CFC legislation or dividend exemption regime, by allowing that a portion of the notional interest deduction (NID) at the level of the Belgian subsidiary is waived[7] and the required level of effective taxation in Belgium is attained. But then again, it is remarkable that the TA consider article 344, §2 ITC, which to a certain extent can have similar consequences as a CFC regime (see below), not contrary to the treaties Belgium has concluded.[8]

1.3. Anti-abuse

The Belgian tax regime nevertheless contains multiple (general and specific) provisions that allow the Belgian TA to counter under certain conditions (international) tax planning transactions and structures which are set up with the aim of reducing or avoiding Belgian income tax.

While these provisions do not always exclusively apply to intra-group transactions, nor solely target the sheltering of passive income in foreign low-tax jurisdictions, most of them do counteract or neutralize the benefits of using foreign low-tax jurisdictions, entities or regimes. Some provisions are applicable only to passive income whereas others are applicable irrespective of the nature of the activity conducted or the income generated abroad.

On the other hand, and despite the fact that Belgium, in principle, does not conclude treaties with commonly named "tax havens",[9] it has increasingly been concluding such treaties with low- or favourable-tax jurisdictions.[10] The Belgian legislator seems to have a rather ambiguous policy whereby it on the one hand discourages or makes it less attractive for Belgian companies to use foreign low-tax jurisdictions or low-taxed entities,[11] whereas on the other hand it concludes treaties with low-tax jurisdictions and enacts tax incentives, like the NID, to attract foreign investment and to promote Belgium as a "base" or even "intermediary" country.

The general view of the TA is that treaties do not prevent them from applying the domestic anti-abuse provisions.[12] As a consequence of the principle that a treaty overrides domestic law, this view is only correct if the provisions of the treaty in question confer such a right or do not limit or prevent the application of the domestic anti-abuse provision.

7 Questions Nos. 15064, 15065 and 15066, 17 April 2007, Chamber Commission Finance, Com 1278, 17–18; Decisions Nos. 700,306; 700,329; 700,444; 800,280; 800,202; 900,234; 900,472; and 2011,495.

8 Com.Conv., No. 9/8.

9 Only in two instances is the term "tax haven" legally defined or is reference made to a definition (Law of 24 December 2002 and art. 307, §1 ITC).

10 Report from the Parliamentary Commission on fraud, DOC 52 0034/004, 216. Examples of existing treaties: UAE (1996) and Hong Kong (2003). Examples of pending treaties: Barbados, Isle of Man and Macao.

11 See also circular letter Ci.RH. 421/580.456, 14 November 2006 which recommends that the TA perform a TP audit in case of payments to (e.g. royalties, management fees) or the use of tax havens which do not add any economic value.

12 Com.Conv., No. 28/17.

2. General anti-avoidance rules (GAARs) and measures

2.1. Disregarding or restating the intervention of a foreign entity

The Belgian TA cannot disregard the existence of a validly incorporated (foreign) entity, even if that entity is set up with the aim of avoiding Belgian (income) tax. Furthermore, as a consequence of the general applicable principle of the "freedom to choose the least taxed route", taxpayers are free to use entities to set up tax efficient structures or transactions provided that they accept and respect all (legal) consequences of their structures/transactions.[13]

This is true even if the form of their structures/transactions is not the most usual one and even if – at least until recently – they were entered into with the sole purpose of reducing the tax burden. Under certain conditions, however, the intervention of such a (foreign) entity or its involvement can nevertheless be disregarded or restated on the basis of the "sham" or "tax abuse doctrines".

2.1.1. Sham

Sham is a fraudulent technique consisting of disguising a transaction/operation by another transaction/operation with the final aim of reducing the tax burden. Typically, parties do not accept or respect all the legal consequences of the transaction/operation presented to the TA. Instead, there is an internal (secret) transaction/operation which modifies any or all of the legal consequences of the apparent one. As a consequence, the TA may disregard the sham act or transaction and levy taxes on the real act or transaction.

The Belgian courts are rather reluctant, however, to "pierce the corporate veil" of the (foreign) company on the basis of the sham doctrine. Most cases where sham has been proved to exist concerned a substantial misuse or denial of the separate legal existence of the company by its shareholders or other parties.[14] In these cases the TA were able to prove and convince the courts that the (legal) intervention of a company was a sham and therefore had to be disregarded. From several facts it appeared that the company was nothing more than a mere "nominee" or that in reality other parties (in lieu of the company) had entered into the transaction(s).[15]

2.1.2. Tax avoidance

In order to combat aggressive tax avoidance techniques and schemes, the Belgian legislator introduced in 1993 the general "anti-abuse" provision of article 344, §1

13 Brussels, 12 May 1992, *TRV*, 1992, 433, note S. Van Crombrugge.

14 L. De Broe, *International Tax Planning and Prevention of Abuse*, IBFD, 2008, 71–72.

15 Cass., 26 January 1965, *Pas.*, 1965, I, 515; Brussels, 9 June 1992, *TRV*, 1993, 475 (confirmed by Cass., 3 June 1993, *FJF*, No. 93/178); Brussels, 9 March 1995, *Fisc.Koerier*, No. 95/279; Brussels, 16 February 1996, *AFT*, 1996, No. 8,263; Ghent, 16 March 1999, *Fisc.*, No. 705, 11; Tr. Namur, 27 March 2002, *Fisc.Koerier*, 2002/323; Ghent, 10 September 2002, *Fisc.*, No. 870, 9; Contra Ghent, 26 November 1982, *FJF*, No. 83/48, 77; Ghent, 4 May 2007, *FJF*, No. 2008/7; 11 September 2007, *Fisc.*, 2007, No. 1095, 11; 6 May 2008, *TFR*, 2008, No. 352, 1071; and 21 May 2008, *Fisc.Int.*, No. 297, 1-4, note B. Springael.

ITC (also GAAR). The anti-abuse provision applied in principle to all kinds of "tax avoidance" and was not limited to only domestic transactions. The TA had to prove the existence of tax avoidance whereas the taxpayer could escape the application of this provision by proving that he also had a legitimate (i.e. non-fiscal) commercial purpose for executing the transaction.

Belgian jurisprudence has shown, however, that this provision has had a rather limited scope of application. It allowed the TA to disregard only the legal characterization applied by the parties to a transaction, but not the transaction(s) as such.[16] The TA had to replace the parties' legal characterization with another legal characterization which had similar legal consequences.[17] It is therefore generally accepted and confirmed by the Minister of Finance and the TA that on the basis of this provision, the existence as such of a (foreign) company could not be challenged, nor the fact that such a company had transferred its seat or an activity abroad.[18] This did not, however, mean that the legal acts in which a company participated or intervened could never be recharacterized. The TA, with the blessing of the courts, succeeded in doing so a few times – in rather extreme cases[19] – by disregarding the tax consequences of consecutive intermediate transactions and replacing them with a single transaction that would have had the same result (the so-called step-by-step approach).[20]

With the aim of providing the TA with a more effective tool to combat tax avoidance, the Belgian legislator recently enacted a modified GAAR. As from 2012[21] the TA can in case of proven "tax abuse" disregard not only the legal characterization of a transaction, but also the transaction itself. The TA have no obligation to replace the transaction with another transaction, but can simply disregard it. If tax abuse is proven to exist, the TA may recharacterize the transaction to bring it in line with the objectives of the tax laws. The TA may determine the taxable base and the amount of tax as if the tax abuse never occurred.

According to the Minister of Finance the principle of the "freedom to choose the least taxed route" remains applicable unless the taxpayer has committed a qualifying tax abuse.[22]

The TA have to prove the existence of such a "tax abuse", a concept which is explicitly defined in the ITC, as discussed below. The TA, however, do not have to prove that the transaction was done only or solely for tax avoidance reasons. Ultimately, the taxpayer can avoid the application of the GAAR if he demonstrates that he did not have the intention of abusing the law, i.e. that he had legitimate motives, other than tax motives, that justify the transaction. These non-tax motives cannot be marginal compared to the possible tax motives.[23] In other words, if the

16 Parl. Doc., Senate, 1992–93, 762-1, 3.

17 Cass., 4 November 2005, *FJF*, No. 2006/21 and 22 November 2007, *FJF*, No. 2008/140.

18 Circ. No. Ci.D.19/453.895 (6 December 1993), No. 17; Q&A, Senate, No. 1-66, 1997–98, 3406–3407.

19 Being close to sham.

20 Brussels, 5 February 2004, *FJF*, No. 2004/196; Antwerp, 31 March 2009, *FJF*, No. 2010/80; Cass.,10 June 2010, *FJF*, No. 2011/21. Tr. Antwerp, 4 January 2012, *Fisc.*, 2012, No. 1314, 1.

21 Art. 167 Programme Law (I) of 29 March 2012, Official Gazette, 6 April 2012, Ed. 3. The changes are applicable as from assessment year 2012, and on acts carried out during a taxable period closing at the earliest on the date of publication of the law modifying art. 344(1) ITC.

22 DOC 53 2081/016, 38.

23 According to the explanatory notes this will, however, be the case if the transaction is executed solely with the aim to obtain a tax benefit, if the non-tax motives brought up by the taxpayer are very

taxpayer has an "acceptable" business, economic, financial or other non-tax motive for his transaction, it should not come under the anti-abuse provision, even if the transaction is tax efficient.

Tax abuse is legally defined as the instance where a taxpayer accomplishes through an act or a series of acts a transaction with the view of avoiding a tax increasing provision or with the view of applying a tax decreasing provision in a manner contrary to the purpose of the provisions of the ITC or the decrees executing the ITC. It will be key to know what the "purpose" is of a certain tax provision and when a transaction frustrates such a purpose. In the reporter's view, it is not the use as such of a (low-taxed) FC or a PE to conduct a business outside Belgium that frustrates a tax provision, but rather the conditions under which they are used.

According to the explanatory notes to the law,[24] frustrating the purpose of the tax law must also be understood in light of the concept of a "wholly artificial construction". The latter is defined as an operation that does not pursue the economic objectives underlying the tax legislation, does not correspond to the economic reality, or does not occur at commercial or financial market conditions. The only aim of an artificial construction is to obtain tax benefits or avoid taxes.

The concept of artificial construction originates from case law established by the European Court of Justice (ECJ) regarding the abuse of the EU treaty freedoms. With respect to the use of a (foreign low-taxed) subsidiary the ECJ is of the view that the fact that a company is formed in another Member State for the sole purpose of benefiting from a more favourable legislation (i.e. tax regime) does not necessarily constitute an abuse (of the treaty).[25] However, the existence of a domestic anti-abuse provision may be justified, that restricts treaty freedoms provided it aims at preventing the use of "wholly artificial arrangements which do not reflect the economic reality and with a view to escaping the tax normally due".[26] There is no artificial construction, despite the existence of tax motives, if the incorporation of a company in another Member State reflects economic reality within the meaning of an actual establishment intended to carry on genuine economic activities and implying the existence and presence of premises, staff and equipment.

The EU Commission does, however, admit that it is not altogether certain how those criteria may apply in respect of intra-group financial services and holding companies, the activities of which generally do not require significant physical presence.[27]

The Minister of Finance has stated that although the new anti-abuse provision should not be applied to the mere "holding" of a company, the incorporation of foreign companies that have no real economic activities (i.e. letter box or shell companies) can, however, be validly targeted by the new provision. With reference

cont.

general and not specifically related to the transaction concerned (e.g. related to all transactions of the same kind) or if the non-tax motives are specific but unsubstantial in the sense that a reasonable person would not have carried out the transaction based on these non-tax motives (Doc. 53 2081/001, 114–115).

24 DOC 53 2081/001, 114.

25 C-167/01, 30 September 2003 (*Inspire Art*).

26 C-196/04, 12 September 2006 (*Cadbury Schweppes*).

27 COM/2007/785.

to ECJ case law the TA have confirmed this view by stating that a letter box or fronting company can be an artificial construction.[28]

The question of whether the foreign (interposed) entity has sufficient economic substance is, however, not always relevant in appreciating whether a transaction is to be considered as an artificial construction. With respect to transfer pricing and thin capitalization rules the ECJ has decided several times[29] that the specific anti-abuse provision was not contrary to the EU freedom of establishment where it aimed at imposing arm's length conditions in intra-group transactions. In many of these cases, the main consideration for the ECJ has been that Member States are legitimately entitled to prevent groups of companies from arbitrarily shifting taxable base to other Member States and that such concerns amount to a justification for the restriction that an anti-abuse rule imposes on the right of establishment. The ECJ did restrict the application of such rules to the excessive or "non-arm's length" part of the transactions involved.[30] In such a case, it is not relevant whether the provision targets only transactions with foreign persons or also applies to persons that have sufficient economic substance. In other words, a transaction may also be "artificial" if it does not meet the "at arm's length" standard.

It remains to be seen how this new article 344, §1 ITC will be interpreted and applied by the TA and Belgian courts, but from the above it appears that it should not be applicable to a Belgian company that owns, directly or indirectly, or is involved in arm's length transactions with a low-taxed foreign group company even where the latter is conducting a rather passive activity like group financing or licensing. If the latter company is effectively established in its country of residence and employs sufficient people and means to conduct such business,[31] it cannot be considered a "wholly artificial arrangement". Moreover, one can conclude that a transaction predominantly set up for tax reasons is not a tainted artificial construction provided real and genuine economic activities are involved. This seems true even if the FC has its residence and activity outside the EU since the explanatory notes in referring to the concept of "artificial construction" do not limit its application only to EU territory.

Finally, the question can be raised on how this GAAR relates to specific anti-abuse provisions in the ITC. It is clear that this GAAR in principle can be applied to a transaction that is specifically set up with the aim of avoiding the application of a specific anti-abuse provision. But it remains unclear whether a transaction that is not a sham and respects all specific anti-abuse provisions can still be attacked under the GAAR.

According to the explanatory notes, the TA will in the first instance rely on the specific anti-abuse measures and only turn to the GAAR as a "last resort" if no satisfactory solution can be reached.[32] This "rule of priority" seems to be a matter

[28] Ci.RH.81/616, 4 May 2012.

[29] C-524/04, 13 March 2007 (*Thin Cap GLO* §§18–91); C-231/05, 18 July 2007 (*Oy AA* §§58–76).

[30] C-524/04, 13 March 2007, §83.

[31] The TA have confirmed this to a certain extent with respect to the NID, stating that a company centralizing the group financing and treasury activities cannot be considered an "artificial construction" (Ci.RH.840/592,613, 3 April 2008).

[32] DOC 53 2081/001, 113 and 2081/016, 70 and 79; Ci.RH.81/616,207, 4 May 2012. Also the old 344, §1 ITC was considered a means of last resort (Question No. 451, 8 July 2011, *Q&A*, Chamber, 2010–11, No. 037, 53).

of policy, but does not follow from the wording of the law. It also remains an open question as to what the TA mean by no "satisfactory" solution.

2.2. Belgian residence or permanent establishment

Rather than challenging the intervention of the FC, the TA may challenge its status as a Belgian non-resident. This would lead to the income of the alleged FC being subject to tax in Belgium. The definition of a Belgian resident company is broad and, since Belgian corporate and tax law adhere to the real seat doctrine, it may include companies incorporated abroad which have their principal establishment or effective seat of management in Belgium. This entails a factual appreciation whereby substance prevails over mere form.[33] The TA have successfully upheld the Belgian residence of an FC in court, demonstrating that the FC was effectively managed in Belgium and therefore subject to corporate income tax in Belgium.[34] The RC has also decided that a lack of substance prevented it from confirming that the company incorporated abroad could also effectively be considered as a Belgian non-resident entity.[35]

Alternatively, the TA may argue that the FC has a Belgian establishment under domestic law or, in a treaty context, a PE in Belgium. The latter will be the case where the FC is considered to have a Belgian fixed place of business through which its activities are carried on, or has a qualifying agent in Belgium. Such risks will be of particular importance where significant support services are maintained from Belgium, or agreements are signed or negotiated in Belgium.

2.3. Business purpose for expenses

As a general rule, expenses incurred or borne by a Belgian company are only tax deductible if they are incurred with a view to acquiring or preserving taxable (business) income (article 49 ITC). The reality and the amount of the business expense has to be proved by the taxpayer. The criterion "incurred with a view to acquiring or preserving taxable income" means that the expense must be (necessarily) related to the functioning/activity of the enterprise (see also article 53(1) ITC) as defined in the company's by-laws.[36] Expenses are not deductible if they exceed the business needs in an unreasonable manner (article 53(10) ITC).

The TA can, consequently, reject these expenses if they are incurred for the benefit of other persons without receiving an adequate remuneration or if they remunerate services that have not effectively been delivered. Furthermore, the TA and the Supreme Court disallow the deduction of expenses that are solely incurred in order to reduce the income tax liability (such as cash drain operations).[37] Hence in order to be deductible, expenses should pass a business purpose

33 Brussels, 29 June 1982, *FJF*, No. 82/119.
34 Brussels, 9 April 1963, *Bull. Bel.*, 1993, No. 402, 2366; Liège, 9 November 1988, *Bull. Bel.*, No. 709, 2298.
35 Annual Report 2012 RC, DOC 53 22/13001, 34.
36 Cass., 19 June 2003, *FJF*, No. 2003/224.
37 Com.I.T. No. 192/29.

test which verifies whether the expense has or could have had a positive influence on the accounting profit (before tax) of the company.

In that sense article 49 ITC can be considered as a general anti-abuse provision regarding the deductibility of expenses.

3. Specific anti-avoidance rules (SAARs) and measures

3.1. Non-deductibility of certain payments

3.1.1. Interest, royalties and service fees

According to article 54 ITC interest, royalties and service fee payments are disallowed when they are paid directly or indirectly to a non-resident person or to a foreign establishment that fail a subject to tax test. An entity/establishment will fail the test when, in the country where it is established, it is not subject to income tax or with respect to such income is subject to a substantially more beneficial tax regime than the Belgian tax regime applicable to such income. It is of no relevance whether the payment is to a group company or not.

Such payments are disallowed unless the Belgian taxpayer shows that these expenses are related to "genuine (i.e. real existing) and proper" transactions and that the expenses do not exceed the normal limits,[38] i.e. that the expenses fall within the normal framework of business transactions, and meet an industrial, commercial or financial need and are at arm's length.[39] However, in order to trigger article 54 ITC, the TA nevertheless have to effectively demonstrate either that the foreign beneficiary is not subject to income tax or that the income is effectively subject to taxation which is substantially more beneficial than the Belgian tax regime applicable to the income.[40]

General statements by the TA supported by general publications "indicating" that a country is a "tax haven" are not sufficient.[41] The mere appearance on a blacklist of countries whose tax regime is deemed to be substantially more beneficial is not sufficient either.[42]

There are no detailed guidelines as to when income is subject to a "substantially more beneficial tax regime" than the Belgian regime for the purposes of article 54 ITC, and how the comparison with the Belgian regime should be made. The official guidelines state that it is practically impossible to determine a general rule and that the TA will consider the facts of each case separately.[43] The Minister of Finance has declared that the list of countries which are indicated on the blacklist for par-

38 Ghent, 27 September 1988, *AFT*, 1989, No. 3, 82; Ghent, 5 February 1998, *Fisc.*, No. 655, 1998, 9; Ghent, 30 September 2003, *Fisc.Act.*, 2003, 34/4; Antwerp, 9 September 2008, *Fisc.Act.*, No. 34, 2010, 1–5.

39 Com.I.T. 54/28.

40 Antwerp, 6 February 2001, *FJF*, No. 2003/389; Antwerp, 2 March 2004, *Fisc. Koer.*, 2004/456.

41 Antwerp, 2 March 2004, *Fisc. Koer.*, 2004/456.

42 Tr. Brussels, 26 January 2005, *Fisc. Koer.*, 2005/333.

43 Com.I.T., No. 54/24.

ticipation exemption purposes (see below) as countries the common tax regime of which is considered to be more beneficial than the Belgian regime can be used as a guideline for the TA.[44]

However, such a list is only indicative since the second test of article 54 ITC requires that the income is subject in that country to a substantially more beneficial tax regime than the Belgian tax regime whereas on the participation exemption blacklist countries are mentioned of which the common tax regime is considered to be more beneficial than the Belgian regime (see also article 198, §1(11) ITC). For example, the deduction of a commission fee paid to an entity located in a jurisdiction with a commonly applicable offshore regime could be denied[45] since the interest received from Belgium would not be taxable under a common offshore regime whereas it would be taxable in Belgium. On the other hand, dividends from that same entity could benefit from the participation exemption at the level of the Belgian parent.

This lack of clear rules to determine when income has to be considered as being taxed substantially more beneficially than in Belgium has led the ECJ to condemn article 54 ITC as being in breach of the EU treaty freedom of services. According to established case law of the ECJ, a measure to combat tax evasion and avoidance is allowed if its specific objective is to prevent the creation of wholly artificial arrangements (see above) which do not reflect economic reality, with a view to escaping the tax normally due on the profits. By just referring to the level of taxation, the anti-abuse provision does not provide sufficient guarantees that only such artificial constructions fall within its scope.[46]

Finally, article 54 ITC targets also "indirect payments" without defining the term. According to the explanatory notes this should avoid the routeing of income to "tax havens" via intermediaries located in an "unsuspected" country.[47] No further explanation is given. Given the principle of the liberty to choose the least taxed route, the only way for the TA to set aside an interposed legal owner is when the TA can evidence that his intervention was a sham or tax abuse within the meaning of article 344, §1 ITC.

3.1.2. Payments to blacklist countries

As from 2010 all direct or indirect payments (exceeding EUR 100,000 per accounting year) made by Belgian companies to specific blacklisted countries have to be notified to the TA in an enclosure to the annual tax return (article 198(10) and 307, §1, paragraph 3 ITC). Absent such a notification, the deduction of the payments is simply rejected. It is immaterial whether the payment is made to a related or unrelated party. Again, the law creates a reversal of the burden of proof because even if the payments are duly notified the deduction is only allowed if the taxpayer shows that the payments are related to "genuine and legitimate" (see article 54 ITC) transactions with persons other than "artificial constructions". Transactions are considered genuine and legitimate if they have a business purpose and are at

44 Question No. 408, 21 October 2003, Chamber Commission Finance, Com 26, 21–22.
45 Antwerp, 14 September 2010, *Fisc.Act.*, No. 34, 2010, 1–5.
46 C-318/10, 5 July 2012, C-318/10 (*SIAT*).
47 Chamber, 1991-92, 444/1, 6.

arm's length.[48] The explanatory notes refer to the ECJ case law regarding artificial constructions and define it as a construction that has no connection to economic reality and is aimed at "evading" (read also "avoiding") Belgian tax. The TA indicate that even if there is no real economic activity at the level of the beneficiary, the deduction is still allowed provided the payments have occurred within a "framework that was not aimed (by the parties or at least one of them) at avoiding directly or indirectly Belgian income tax".[49] This mitigation is aimed at the situation where the Belgian taxpayer pursuant to a third party contract pays to an unrelated person that has set up a low-tax structure for its own tax planning needs. In such a situation the Belgian taxpayer has no intention of avoiding Belgian taxes.[50]

Countries are blacklisted if they do not effectively and substantially apply the OECD standard on exchange of information. This part of the provision cannot yet be applied since the TA have to rely on a final list of countries that has not yet been issued by the OECD's Mondial Forum. In addition, countries that levy no or low taxes, i.e. have a statutory corporate income tax rate below 10 per cent, are also blacklisted. These countries are identified on an official blacklist (article 179 RD/ITC), which creates a legal presumption of being a "tainted" jurisdiction, which cannot be rebutted by the taxpayer.

On the other hand, payments to countries not mentioned on the list, but with a statutory rate below 10 per cent are not covered. It is the government's intention to update the list every two years.

The fact that no EU Member States are listed does not completely avoid the question on compatibility with EU freedoms and more particularly the freedom of capital. This freedom is also applicable in relations with third countries. The TA are of the view, however, that there should be no issue since the taxpayer can safeguard the deduction if he shows the genuine and legitimate nature of the expense in the absence of an artificial construction.[51]

Similar to article 54 ITC, this provision targets also "indirect payments" without, however, defining them. According to the TA it has the same meaning as under article 54 ITC. They further specify that one has to look at the "economic" owner and not at the legal owner if the latter is only an intermediary. It is of no importance to the TA whether the intermediary has received the income on his own behalf.[52] However, as a consequence of the principle of the freedom to choose the least taxed route, disregarding the legal owner should only be possible if it is proved that his intervention was a sham or tax abuse within the meaning of article 344, §1 ITC.

3.1.3. Thin capitalization rules

A 1:1 debt-to-equity ratio applies to loans (other than public bonds) of a Belgian company granted by a non-resident company being a member of the board of directors of that Belgian company. The interest on the loan in excess of the equity is

48 Parliamentary notes (DOC 52 2278/016) refer to Com.I.T., No. 54/28.
49 Ci.RH.421/607.890.
50 P. Smet, "'Betalingen aan belastingparadijzen': nog veel onduidelijkheden", *Fisc.*, 2009, No. 1185, 1.
51 Ci.RH.421/607.890.
52 *Ibid.*

converted into non-deductible dividends (article 18(4) ITC). Since the provision goes beyond targeting non-arm's length transactions, this rule has been found incompatible with the EU freedom of establishment and, therefore, should not be applicable in the case of an EU (and EEA) lender.[53]

A 5:1 debt-to-equity ratio applies to loans (other than public bonds or loans from financial institutions) when the "beneficial owner" of the interest is part of the same group as the Belgian debtor[54] (article 198, §1(11) ITC). A qualifying group is defined in article 11 of the Belgian Company Code (BCC). Belgian finance companies that borrow and lend intra-group are not excluded from the scope of this provision. In order to calculate the excess non-deductible interest they are, however, allowed to net the interest incurred on group payables against the interest income earned on group receivables, provided that these receivables and payables are related to and embedded into a framework agreement whereby the Belgian entity is charged with the central treasury management of the group. Interest received from borrowers not subject to Belgian corporate income tax or to a foreign tax similar to the Belgian one or established in a country where the common tax regime is substantially more beneficial than the Belgian common tax regime are excluded from the netting.

The law provides that the commonly applicable tax rules in Member States of the European Economic Area cannot be considered as substantially more beneficial than in Belgium. One can, however, rightfully question whether the exclusion from the netting of interest payments from a payer in a third country that is not an artificial construction, but with a substantially more beneficial tax regime, could be contrary to the freedom of capital.

There is no possibility for the taxpayer to prove in a given case that, although its debt exceeds the 5:1 ratio, its debt level and interest expenses are still at arm's length and consequently should not be disallowed. The impossibility of proving the contrary appears to breach the EU treaty freedoms.

A 5:1 debt-to-equity ratio is also applicable, even outside a group context, when the "beneficial owner" is not subject to income tax or with respect to the interest is subject to a tax regime (foreign or Belgian) that is substantially more beneficial than the Belgian common tax regime (article 198, §1(11) ITC). Again, as mentioned under article 54 ITC, the requirement "with respect to the interest is subject to a tax regime that is substantially more beneficial than the Belgian common tax regime" is a test at income level and not at country level. In other words, the loan from a FC which as an entity is subject to normal corporate income tax can still be tainted if the interest in the hands of the FC is taxed more favourably compared to its treatment under the Belgian common tax regime.[55]

Both forms of the 5:1 limitation apply even where the creditor is not tainted but where the loan has been guaranteed by a tainted person (see above) or where the

53 C-105/07, 17 January 2008 (*Lammers & Van Cleeff*); see also C-324/00, 12 December 2002 (*Lankhorst*).

54 Leasing and factoring within the financial sector are excluded from this limitation. The same is true for certain companies charged with certain public projects.

55 The RC seems to uphold a rather restrictive interpretation on when the income can be considered as being taxed in a much more favourable way compared to the Belgian common tax regime (see Decisions Nos. 600,099, 4 May 2006 and 700,065, 5 June 2007 with respect to a profit participating loan).

latter has provided the necessary funds to the formal creditor without transferring the credit risk. This is, however, only the case where the main purpose of the intervention of the formal creditor is tax avoidance.[56]

3.2. Beneficial owner

Withholding tax is due on dividends, interest (15 per cent, 21 per cent or 25 per cent) and royalty (15 per cent) payments. There are, however, various domestic (including EU)[57] and treaty exemptions or deductions available depending on the nature of the debtor or the creditor, the nature of the instrument, the affiliation between and/or residence of the debtor and creditor.

Eligible for these exemptions/reductions is the "recipient", "beneficiary" or "final/effective beneficiary". None of these terms is defined. The Belgian legal system is not familiar with the general concept of economic ownership as opposed to legal ownership. As a consequence, a rather formal legalistic approach is taken by the legislator (article 117, §§5bis, 6, 6bis RD/ITC), the TA (including the RC)[58] and a majority of scholars. The entitlement consequently needs to be assessed at the level of the owner (or usufructuary) of the income generating asset, excluding the agent or intermediary acting on behalf of the recipient.

The refusal of the exemption or reduction, therefore, seems to be a matter of whether the payments to the beneficiary are a sham or can be considered as tax abuse within the meaning of article 344, §1 ITC (similar to the discussion under articles 54 and 198(10) ITC).

3.3. Transfer pricing adjustments

The general at arm's length principle is codified in article 185, §2 ITC and is defined in a fairly similar manner to article 9 of the OECD model. The TA can invoke this provision to prevent profit shifting to a FC of the same multinational group, the latter being a group within the meaning of article 11 BCC. The TA have to prove that the transaction is not at arm's length.

In addition, all abnormal or gratuitous advantages granted to a directly or indirectly affiliated non-resident person have to be reinstated in the taxable profit of the Belgian company (article 26, paragraph 2(1) ITC). Whether the entities are affiliated is a factual situation and is broader than being part of a group within the meaning of article 11 of the BCC. The TA have to prove the existence of an abnormal or gratuitous advantage. This provision has been found not to be in breach of the EU freedom of establishment, even though it goes beyond targeting purely artificial constructions devoid of any economic reality, created with the aim of avoiding the tax normally due.[59] As mentioned above, the ECJ considers that cross-border transfer

[56] A guarantee provided by a parent company to facilitate the granting of a bank loan to its subsidiary should not be captured if there are sound business reasons.

[57] The Parent–Subsidiary, Interest and Royalty Directives as well as the EU–Switzerland agreement was implemented in Belgian domestic law, sometimes even beyond their scope.

[58] Com.Conv., No. 10/204; 11/204; and 12/203. Question No. 802, 28 March 2006, Chamber Commission Finance, Com. 906, 8. Decision No. 600,478, 21 November 2006; No. 700,324, 11 September 2007.

[59] C-311/08, 21 January 2010 (*SGI*).

pricing rules justify measures to combat artificial constructions if they require that the transaction occurs at arm's length conditions, irrespective of whether they target only transactions with a foreign person and irrespective of whether the latter has a sufficient level of economic activity/substance.

The same advantages are also reinstated in the tax base if they have been granted to a non-resident person or a foreign establishment that in its country of establishment is not subject to income tax or subject to a substantially more beneficial tax regime than that to which the Belgian company is subject. No affiliation is required. The TA have to prove that the beneficiary is effectively subject to a substantially more beneficial tax regime.[60]

Finally, specifically with respect to interest, articles 18(4) and 55 ITC reiterate that only the interest exceeding the market interest rate is not deductible.

3.4. Transfers of income producing assets to FC

The transfer to a FC of the ownership of (in)tangible assets is a "realization" event triggering corporate income tax on the realized capital gain (if any). According to a decision of the RC, such a taxable realization event does not occur when assets are "attributed" by the Belgian head office to its foreign PE.[61]

Pursuant to article 344, §2 ITC the TA can disregard a sale, transfer or contribution of certain assets (shares, bonds, debt claims or other securities, patents, manufacturing processes, manufacturing or trade brand names, or cash) to a low-taxed non-resident person.[62] The latter does not have to be related to the transferor. The allocation of assets by the Belgian head office to its own low-taxed foreign branch located in a treaty country does not, however, fall under this provision.[63]

Where applicable, this provision triggers a legal fiction[64] as a result of which the assets transferred in violation of the provision are deemed not to have left the Belgian transferor's estate, and therefore the assets and income remain attributed to and taxable[65] in the hands of the transferor.[66] In order to trigger the fiction, the TA must demonstrate that its conditions are met, i.e. that there is a transfer of qualifying assets to a low-taxed non-resident. By doing so, a reversal of the burden of proof is created. The Belgian transferor can rebut the fiction if he demonstrates (a) that the transfer is justified by "legitimate needs of a financial or economic nature" (i.e. commercial non-tax purposes) or (b) that he has received for the transfer an actual consideration producing income effectively subject in Belgium to a

60 Tr. Mons, 18 January 2006, *Fisc.Koerier*, 06/498.
61 Decision No. 600,524, 19 December 2006.
62 This provision does not install a traditional CFC regime, but under certain circumstances can produce the same effect.
63 De Broe, *op. cit.*, 133.
64 The fact that it is a "fiction" and not an assumption of sham means that the TA have to prove the existence of it within the normal three-year statute of limitations (Cass., 18 December 1982, *Journ. prat. dr. fisc. fin.*, 1963, 278).
65 Without any relief for double taxation if the income is taxed abroad as well.
66 Cass., 18 December 1962, Pas. 1963, I, 489; Tr. Antwerp, 17 June 2003, *TFR* 2004/8 and Tr. Antwerp, 3 March 2006, www.fisconet.be.

tax burden which is normal compared to the tax burden which would have applied if the transaction had not taken place.

The "low-tax" test here is similar to that in article 54 ITC with respect to interest deduction, i.e. the non-resident recipient is in its country of location either not subject to income tax or with respect to the income produced by the transferred qualifying assets subject to a tax regime that is substantially more beneficial than the tax regime to which the income is subject in Belgium.

From the wording it is clear that not only transactions to commonly regarded tax havens (i.e. jurisdictions that do not levy any income tax) are targeted, but also transfers to jurisdictions that do levy income tax but where the recipient as such is not subject to income tax[67] or benefits from a more favourable regime than the Belgian regime with respect to the income concerned.[68] In other words, entities located in the EU or in other "regular" tax jurisdictions, in principle, can also fall within the scope of article 344, §2 ITC. In line with the ECJ recent case law, it seems very likely that this provision, the scope of which is not limited to artificial constructions, breaches the EU freedom of establishment or capital.

Notwithstanding its importance, this provision is rarely applied in practice.[69] Little official guidance is available, especially with respect to the operation of the fiction.[70] The TA seem to be reluctant to apply this provision due to the many open and unresolved questions. If possible, they rather apply specific anti-abuse provisions whereby the transfer as such is not denied, but the arm's length consideration for it or the subsequent payments (e.g. royalties, interest, etc.) by the Belgian company to the transferee are challenged. If the transferee is a subsidiary (first or subsequent tiers) of the Belgian transferor, the TA might ultimately deny the participation exemption.

3.5. Taxation of payments to non-residents

Payments by Belgian residents to non-residents for services which do not trigger a treaty and/or domestic PE in Belgium are under current legislation usually not taxable in Belgium. According to a recently introduced draft proposal of law, such payments might under certain conditions become taxable in Belgium provided a treaty allocates the taxation power to Belgium or, if no treaty is applicable, the non-resident is not able to prove that he is not effectively taxed in his home country on this payment.

[67] Entities that are subject to tax, but do not effectively pay tax due to certain deductions, carryforward losses, tax consolidation rules, etc. are not meant. This can be deduced from the rules on the participation exemption where it is required that the foreign entity is subject to a tax similar to the Belgian corporate income tax. It is generally accepted that this only relates to the nature of the tax, being a tax on profit irrespective of the applied rate and irrespective of how the tax basis is determined.

[68] The dividends that are exempted from tax in the Netherlands by virtue of the normal participation regime do not benefit from a more favourable regime than the Belgian regime (Question No. 1252, 19 October 1994, *Bull.Bel.*, No. 749, 1307).

[69] The RC has issued a positive decision ruling, but without really going into the details of all conditions and requirements (Decision No. 800,456 of 31 March 2009).

[70] P. Lion, "Artikel 344, §2 van het WIB 1992: 'een papieren tijger'", *AFT*, 1995, No. 11, 317–344.

3.6. Subject to tax requirement

3.6.1. Dividend received deduction (DRD)

Article 202 ITC provides for a 95 per cent deduction for dividends received (i.e. participation exemption). This deduction is subject to a rather complex series of "subject to tax" tests. These tests are currently included in five exclusion grounds in article 203, §1 ITC. A number of rules mitigating these tests are provided by article 203, §2 ITC. The taxpayer has to demonstrate that all conditions for the deduction are fulfilled, including that the exclusion grounds do not apply.

Most treaties Belgium has concluded do not override the subject to tax requirement as applicable under domestic law. Some treaties provide, however, for a more relaxed subject to tax requirement or provide for a tax credit if the exemption cannot be applied for.[71]

The Belgian model convention even provides for an exemption when the subsidiary conducts an active trade or business irrespective of whether it has been subject to tax or not.

The subject to tax requirement seems to comply with the EU Parent–Subsidiary[72] Directive which also imposes a subject to tax test upon the subsidiary and allows Member States to take proportionate anti-abuse provisions.

3.6.1.1. General exclusion

As a general rule, the DRD does not apply if the dividend is paid by a FC that is (a) not subject to a foreign tax similar to the Belgian corporate income tax, or (b) is established in a country the common tax regime of which is substantially more beneficial than Belgium's. The condition of being subject to a "similar" foreign tax requires a tax based on profit. It is not required that the taxable basis or the tax rate is similar to Belgium's.[73] It is sufficient that the FC as such is subject to tax even though its income has not been effectively taxed. In this context the RC allows the DRD for dividends coming from a FC that benefits from a "tax holiday" provided it has no general and unrestricted application in terms of income/activity and time.[74] The official guidelines of the TA contain a list with countries where no entity is considered to be subject to a tax similar to the Belgian tax regime as well as a list with countries where certain entities are not subject to such a similar tax regime.[75] The lists have not been updated since 1997 and therefore should not be considered as providing conclusive guidance. Furthermore, these lists are merely an assumption and the taxpayer can always provide proof to the contrary.

Article 203 ITC provides that the common tax regime of EU Member States by default cannot be considered as substantially more beneficial. That same provision clarifies that a country's tax regime is not substantially more beneficial if both the commonly applicable statutory tax rate and the commonly applicable effective rate

[71] E.g. treaties with the USA, Tunisia, Congo and Rwanda.
[72] See also protocol to the treaty with Tunisia that requires an active trade or business.
[73] Senate, 1989–1990, 806/3, 87.
[74] E.g. Decision No. 700,025, 13 March 2007. The government does not want to "punish" investments in certain regions that provide tax incentives to encourage investment and development.
[75] Com.I.T., No. 199/34.

are at least 15 per cent. The condition of a minimum statutory and effective tax rate is a requirement to be considered on a country level basis and not on an entity level basis. As a consequence, dividends from an entity located in a country that has a statutory and effective tax rate of at least 15 per cent cannot be excluded from the DRD even though its effective tax rate is below 15 per cent due to for example the use of losses, being part of a tax consolidation or the benefit of a (limited) tax holiday.

However, such a company still needs to comply with the requirement that it is subject to a tax regime that is similar to the Belgian tax regime (see above).[76]

It is therefore surprising that the RC recently decided that the dividends from a Curacao company benefiting from a tax holiday could not be excluded from the DRD without effectively testing (or at least without making any reference to such a test) whether the common effective tax rate in Curacao is at least 15 per cent and if so whether the tax holiday is of a temporary and limitative nature.[77]

The TA are of the view that a generally applicable offshore regime (foreign income is not taxable on the basis of territoriality) cannot be considered as a substantially more beneficial tax regime.[78] The government has issued a list of countries the common tax regime of which is considered to be more beneficial (i.e. statutory or effective tax rate below 15 per cent) than the Belgian regime.[79] Contrary to the opinion of the Minister of Finance in this respect, the reporter is of the view that the text of the law implies that only jurisdictions appearing on the list are excluded.[80] In any case, the taxpayer always has the possibility to prove that a country mentioned on the list does not or no longer has a more beneficial tax regime than the Belgian tax regime.[81]

The consequence of applying the general exclusion is a complete denial of the DRD. The dividends from, for example, a Cayman Islands company do not benefit from any DRD even if all the dividends or other income that such a company redistributes are sourced from normally taxed EU subsidiaries.

3.6.1.2. Specific exclusions

3.6.1.2.1. Finance, treasury or investment company

The DRD is denied if dividends are paid by a finance company, a treasury company or an investment company that is subject, in its country of tax residence, to a tax regime that deviates from the common tax rules applicable in that country. A tax regime is considered to deviate from the normal regime whenever the profits of the company are either not taxed or are taxed at a substantially lower level than the common applicable tax regime.[82]

76 DOC 50, 1918/1, 48–49.
77 Decision No. 2011,426, 22 November 2011.
78 AFZ/97.0060 (AFZ 4/2005), 31 March 2005 (*Hong Kong*); Decision No. 600,411, 7 November 2006; Question No. 802, 28 March 2006, Chamber, Commission Finance, Com 906, 8–13.
79 Art. 74(3) *quater* RD/ITC.
80 Question No. 1481, Q&A, Chamber, 2006–2007, Nos. 51–164, 30 April 2007, 32,128–32,129.
81 The list contains only a rebuttable assumption. Question No. 1481, Q&A, Chamber, 2006–2007, Nos. 51–164, 30 April 2007, 32,128–32,129; see regarding *Panama* Decision No. 700,383, 13 November 2007.
82 Ci.RH.421/506,082, 4 September 2001 and addendum 31 May 2006 and 22 June 2009.

A "finance company" is defined as a company the activities of which consist solely or mainly of providing financial services to unrelated parties, i.e. to parties that do not form part (direct or indirect) of the same group[83] to which the finance company belongs.[84] A "treasury company" is defined as a company the activities of which consist solely or mainly of making portfolio investments as defined by accounting law. Cash pooling activities for the benefit of other group companies do not qualify as treasury activities for this definition.[85] An "investment company" is defined as a company the purpose of which is the collective investment of funds.

It has to be said that dividends from EU based finance and investment companies under certain specific circumstances are not necessarily (fully) excluded from the DRD. One of the conditions for an EU finance company is that it is not "fat capitalized". This requirement is intended to discourage Belgian companies from converting taxable interest income into exempt dividends by highly capitalizing such an EU subsidiary.

3.6.1.2.2. Offshore

Dividends do not benefit from the DRD if sourced out of offshore income (other than dividends) subject in the country of residence of the dividend distributing company to a tax regime that deviates from the common tax rules applicable in that country.[86]

Foreign source income that is not taxed as a result of the generally applicable tax regime in the country of residence of the dividend distributing subsidiary is not targeted by this exclusion. Subsidiaries in countries with a generally applicable territorial tax regime (i.e. no taxation of offshore income) should therefore not be an issue.[87]

3.6.1.2.3. Foreign branch income

Dividends sourced out of profit derived through one or more foreign PEs that are overall (i.e. tax in head office and branches together) subject to a tax regime substantially more beneficial than the tax regime to which such profits would have been subject in Belgium are also excluded from the DRD. The foreign cumulative and effective tax charge will be considered substantially more beneficial than Belgium's if it is lower than 15 per cent.

The exclusion will, however, not apply if both the head office and the PE are established in an EU Member State.

3.6.1.2.4. Intermediary holding company

The subject to tax and exclusion rules do not stop at the first-tier subsidiary. According to this look-through rule, the DRD is not available for dividends distributed by

83 Specifically defined as companies connected through 20 per cent direct or indirect shareholdings or voting rights; Ci.RH.421/506,082, 4 September 2001 and addendum 31 May 2006 and 22 June 2009.

84 This was to avoid dividends from Belgian coordination centres (group financing entities by nature) being excluded.

85 Ci.RH.421/506,082, 4 September 2001 and addendum 31 May 2006 and 22 June 2009.

86 Decision Ci. COM/082 (11 July 1994) and Ci. COM/089 (20 September 1994).

87 AFZ/97.0060 (AFZ 4/2005), 31 March 2005 (*Hong Kong*); Decision No. 2012/146, 5 June 2012; see, however, Tr. Mons, 17 April 2012.

an intermediary company (not being an investment company) which redistributes dividends that are tainted under the previous exclusion rules for more than 10 per cent of the amount of dividends (re)distributed. The dividends that would not be eligible for the DRD if they were received directly by the Belgian parent company are thereby excluded even if a (conduit) company is interposed the dividends of which would normally not be excluded under the other exclusion rules.

Under certain conditions the DRD remains available for dividends from above-described EU finance companies, treaty country companies quoted on a stock exchange and Belgian and foreign entities that are taxed on the basis of the Belgian subject to tax/exclusion rules or a similar foreign regime.

3.6.2. Exemption of PE profit

In line with the OECD model, most Belgian treaties do not provide for a subject to tax requirement. Consequently, profit from a foreign PE located in a country with which Belgium has concluded such a treaty is exempt from Belgian tax, irrespective of whether that profit is taxable, effectively taxed, or benefits from a favourable regime or rate. Belgian companies can therefore exempt their e.g. Swiss or Luxembourg finance PE provided the latter has sufficient means to effectively conduct its financing activity.[88]

Some treaties do, however, impose some kind of subject to tax requirement. This is certainly the case for most treaties signed or negotiated over the last 10 years. The new policy of the Belgian government is to include by preference a subject to tax clause in the treaty.[89] Basically, the TA distinguish between two kinds of subject to tax clauses.[90] Under the first, it is required that the foreign income is "taxed", which implies, according to the TA, that the income is subject to a tax regime, but not that it has been effectively taxed. The treaty with the United Arab Emirates contains such a clause as a consequence of which profit generated by a UAE PE should be exempt in Belgium.[91]

The second kind of clause requires that the income is "effectively taxed", which implies that the income is subject to a tax regime without benefiting from any exemption. The fact that the income ultimately is not effectively taxed due to the use of tax deductions, losses or certain specific incentives does not, however, jeopardize the exemption in Belgium. According to the TA the total profit of a PE should be considered to be effectively taxed even if a part of the profit is exempted unless the taxed part of the profit is only artificially linked to the PE. This will be the case if the taxable part of the income is substantially lower than the exempted income or is not derived as a result of a real economic activity taking into account premises, staff and equipment ("artificial construction").

This rather flexible view of the TA with respect to treaty PE income stands in stark contrast to the strict and complicated subject to tax requirements on dividends (see above). Knowing that Belgium concludes more and more treaties with low-taxed jurisdictions this might result in the situation where the profits in such a

88 See Decision No. 600,524, 19 December 2006 and Decision No. 2010,372, 14 December 2011.
89 See art. 23 Belgian model convention.
90 AFZ No. 4/2010, 6 April 2010 Addendum to AOIF No. Ci.R9.Div/577,956, 11 May 2006.
91 Decision No. 800,465, 17 February 2009 and No. 2010,023, 23 February 2010.

country earned by a local PE would be exempt in Belgium whereas similar profits would not benefit from the DRD regime if they were distributed by a subsidiary in that country.

3.7. Foreign tax credit

See previous IFA report.[92]

4. EU issues

See prior sections and previous IFA report.[93]

92 S. Martin and P. Smet, *Cahiers de droit fiscal international*, Vol. 93b, 2008, pp. 145–146.
93 M. Bourgeois and E. Traversa, *Cahiers de droit fiscal international*, Vol. 95a, 2010, pp. 128–148.