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National Reporter
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A demerger can in our opinion be defined as the reorganization of a company whereby its assets and liabilities are divided into one or more new or existing companies and the shares of those companies are distributed to the original company or to its shareholders. It is the reverse of a merger.

A demerger is normally achieved in Belgium by (i) transferring assets and liabilities to one or more new or existing companies in exchange for the allocation to the demerging company of shares in the receiving companies, possibly followed by the selling of the shares of the receiving companies (“ransfer of assets”, or (ii) transferring all the assets and liabilities of a company, after it has been wound up without going into liquidation, into two or more new or existing companies, in exchange for the allocation to the shareholders of the demerging company of shares in the receiving companies, whereby the original company ceases to exist (“split-up”. The demerger by means of spin-off or split-off, i.e. by maintaining the original company and setting up one or more new companies whose shares are transferred to the shareholders of the original company, either through distribution (“pin-off” or through full or partial exchange of their shares in the original company (“plit-off”, is seldom used in Belgium because a split-up generally accomplishes the same objective and is favored by the company and tax laws explained below.

I. Relevant Company Law Aspects of Domestic Demergers

Until recently, Belgium did not have specific legal provisions relating to demergers, but recent legislation has to some extent remedied this and proposed legislation will further improve the situation.

1. Split-up

A split-up was traditionally achieved by winding up and liquidating the original company, and by contributing all the assets and liabilities of that company into two or more new or existing companies in exchange for shares of the receiving companies which were distributed by the liquidator to the shareholders of the original company. The original company ceased to exist.

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However, Belgium has recently implemented Directive 82/891/EEC of 17 December 1982 concerning the division of public limited liability companies[1] (the "Sixth Directive") by the Law of 29 June 1993 on the modification of the company law with respect to mergers and split-ups of companies.[2] This law became effective on 1 October 1993. The Belgian company law as amended by the Law of 29 June 1993 is hereinafter referred to as the "Company Law".

In accordance with the Sixth Directive the Company Law now provides for three types of split-ups: (i) split-up by acquisition i.e. into existing companies, (ii) split-up by the formation of new companies, (iii) split-up by acquisition and the formation of new companies which is a combination of (i) and (ii). A split-up is now defined as the transaction whereby, after being wound up without going into liquidation, a company transfers all of its assets and liabilities to two or more new and/or existing companies in exchange for the allocation of shares in the receiving companies to the shareholders of the demerging company, possibly with a cash payment not exceeding more than one fifth[3] of the nominal value or par value of the shares allocated.

The main consequences of a split-up are that (i) the demerging company ceases to exist, (ii) the shareholders of the demerging company become shareholders of the receiving companies, but not necessarily in the same proportion as in the demerging company[4] and (iii) all assets and liabilities (including "intuitae personae" contracts) are transferred by universal succession,[5] which means that the transfer of assets and liabilities is enforceable against third parties without further formalities (except in the case of real estate).

Since a split-up may prejudice the creditors of the demerging company, the Company Law basically provides three types of guarantees for the creditors, including the tax authorities, of the demerging company:

a. the creditors of each company participating in the split-up may request guarantees within 2 months following the publication of the split-up in the *Belgian Official Gazette*, provided that their receivable arose, but has not yet matured, prior to such publication (Art. 174/40 of the Company Law).
b. the creditors may request the Commercial Court to declare the split-up null and void in a number of situations listed in Article 190bis of the Company Law. Such a procedure must be instituted within the 6 months following the publication of the split-up in the *Belgian Official Gazette.*
c. the Company Law provides that the receiving companies are jointly liable for the liabilities which have not been clearly allocated to one of the receiving companies in the split-up documentation (Art. 174/28, para. 2 of the Companay Law). Moreover, a bill has been submitted to the Parliament to provide

1 *O.J.* No. L 378 of 31 December 1982.
2 *Belgian Official Gazette* (hereinafter "BOG") of 21 July 1993.
3 Article 35 of the bill on the modification of the Company Law dated 13 May 1993 (*Gedr. St.*, Kamer, 1992-93. No. 1005/1, 40) would reduce this to 10%.
4 A disproportional distribution assumes that the shareholders of the demerging company who are present or represented approve this unanimously (Art. 174/34 § 3 of the Company Law).
5 The Supreme Court had already applied this theory in the context of mergers: Cass., 30 April 1970. *pas*., 1970, I, 749.

that the receiving companies remain jointly liable for all the liabilities of the demerging company.[6] It appears from the above that the legislator is struggling with the reconciliation of two different objectives: the facilitating of demergers and the protection of the creditors of the demerging company.

In addition, creditors may always invoke the "actio pauliana" provided for in Article 1167 of the Civil Code, if the split-up has been enacted with malicious intent to prejudice the creditors of the demerging company. If the actio pauliana instituted by a creditor is accepted, the split-up will not be enforceable against the creditor, who will be able to recover his receivable on the assets of the demerging company.

2. Transfer of Assets

In the absence of a specific legal framework in Belgium for a transfer of assets (which is achieved by the contribution by the demerging company of one or more branches of its activity or of all of its branches of activity into one or more new or existing companies in exchange for the allocation to the demerging company of shares in the receiving companies), such transfer is governed by the general commpany law provisions with respect to the contribution in kind of assets in exchange for shares.

A bill on the modification of the Company Law dated 13 May 1993 provides for a specific legal framework for the transfer of a branch of activity and of all branches of activity (the latter being less relevant in the context of demergers).[7] The transfer of a branch of activity is defines in Article 40 of the bill as a transaction in which a branch of activity together with the assets and liabilities related thereto is transferred to another company in return for a remuneration consisting only of shares of the receiving company. A branch of activity is defined as an entirety which carries on an autonomous activity from a technical and organizational point of view, that is to say an entity capable of functioning by its own means. The transfer of a branch of activities would imply that the assets and liabilities related thereto are transferred by operation of law to the receiving company.

II. Tax Treatment of Domestic Demergers

Belgium has specific tax legislation to achieve tax-free demergers in a purely domestic situation. A distinction must be made between a transfer of assets and a split-up as defined above. As a rule, the tax treatment of a demerger is the same regardless of whether the receiving companies are new or existing companies.

6 *Gedr. St.,* Kamer, 1992-93, No. 1005/1 (Art. 40 of the bill on the modification of the Company Law dated 13 May 1993). An amendment to this bill has already been submitted to limit such liability to the net assets of each of the receiving companies in accordance with Art. 12 § 7 of the Sixth Directive (*Gedr. St.,* Kamer, 1992-93, No. 1005/8, 7-8).

7 *Gedr. St.,* Kamer, 1992-93, No. 1005/1, 14-15, 41-42.

A. Conditions for Obtaining Tax Relief

The conditions for tax relief are basically of two types: some conditions relate to the nature of the qualifying transaction as defined in the Company Law or in proposed company law while another condition (i.e. that the transaction fulfils legitimate needs of a financial or economic nature) is specifically tax related.

1. Transfer of Assets

The transfer of assets in a domestic situation is regulated by Article 46, §1, 2° of the new Belgian Income Tax Code (hereinafter "ITC") as modified by the law of 28 July 1992 which has partially implemented the Council Directive on the Common System of Taxation Applicable to Mergers, Divisions, Transfers of Assets and Exchanges of Shares concerning Companies of Different Member States 90/434 of 23 July 1990[8] (the "Merger Directive"). This Article provides for an *optional* exemption regime where a company transfers, without being dissolved, one or more branches of its activity ("branche d'activité") or all of its branches of activity ("universalité des biens") in exchange for shares of the receiving company. In the context of demergers only the transfer of one or more branches of activities needs to be discussed. The tax relief only applies if the following four conditions are met (Art. 46, § 1, 2° jo Art. 46, § 1, para. 2, ITC).

a. Qualifying Receiving Company

A first requirement is that the receiving company must be a resident company or a foreign company having its registered office, principal establishment or seat of management in an EC Member State. The legal form of the receiving company is irrelevant. On the other hand, the demerging company may be either a Belgian resident company or a non resident company.

b. Branch of Activity

A second requirement is that one or more branches of activity must be transferred. A branch of activity is defined as all the assets invested in a division of a company which from a technical point of view constitute an independent business, i.e. an entirety capable of functioning by its own means.[9] This definition is in line with the definition set forth in Article 2 (i) of the Merger Directive and with Article 40 of the company law bill dated 13 May 1993 (see supra I.2).

8 *O.J.*, L 255/1 of 20 August 1990. A proposal for a Council Directive amending Directive 90/434/EEC has been presented by the Commission on 26 July 1993. Com. (93) 293 fin.

9 Administrative Comments on the ITC (herinafter "Com. ITC") 39/17. For a detailed discussion, *see* Servais, T., *L'apport de branche(s) d'activité ou de l'universalité des biens entre sociétés belges,* Bruylant, Bruxelles, 1982, 16-28.

Financial fixed assets and other portfolio securities do not as such constitute a branch of activity. Such assets may be considered to be part of a branch of activity, provided that they are integrated in a normal way into that branch of activity without constituting an essential part of it (Art. 46, § 1, last paragraph, ITC). Nevertheless, the Belgian tax authorities treat a transaction in which a company transfers all of its assets and liabilities other than financial fixed assets as a transfer of a branch of activity and not as a transfer of all branches of activity.[10] Accordingly, it is possible for a mixed holding company to demerge into a pure holding company and an operating company in a tax free manner.

c. Remuneration by Shares

In line with Article 2 (i) of the Merger Directive, the transfer of assets must be remunerated solely by shares representing the capital of the receiving company. Accordingly, and contrary to the split-up, no cash payment may be made. However, the tax authorities accept that compensation in cash is allowed, provided that it does not exceed reasonable limits to be determined on a case-by-case basis.[11] Although not expressly provided in Article 46 ITC, it goes without saying that the transfer may also be remunerated by the commitment of the receiving company to pay the liabilities transferred and that only the net asset value of the contribution (assets less liabilities) must be remunerated by shares.

d. Legitimate Needs of a Financial or Economic Nature

In line with Article 11 (a) of the Merger Directive, Article 46, § 2, ITC requires that the transaction fulfils legitimate needs of a financial or economic nature. This requirement is effective for transactions which have taken place since 27 March 1993.

According to the parliamentary discussions, this requirement is intended to deny tax relief if the main purpose of the transaction is to avoid tax[12] (e.g. the use of tax losses of a receiving company which has been inactive for some years); it is not intended to allow the tax authorities to interfere in the economic or strategic options of the companies or to become a censor of the merits of their decisions.[13] The demerger must thus be carried out for valid financial or economic reasons, such as the rationalization or the restructuring of the activities of the companies involved. On the basis of the rule "actori incumbit probatio", the burden of proof falls on the taxpayer.

Article 345, § 1, para. 1, 1° ITC provides for the possibility (but not for the obligation) of applying for an advance ruling confirming that the transfer of assets ful-

10 Com. ITC 105/65.

11 Circular of 21 January 1993, which confirms the previous practice reflected in Com. ITC 39/16.

12 *Gedr. St.,* Kamer 1992-93, No. 1005/1, 13; *Gedr. St.,* Kamer, 1991-92, No. 444/1, 13.

13 *Gedr. St.,* Kamer, 1990-91, no. 1641/1,19. This confirms the doctrine of the Supreme Court: *see inter alia* Cass., 23 January 1959, *J.P.D.F.,* 1958, 33; Cass., 26 March 1968, *Pas., 1968, I, 913.*

fils legitimate needs of a financial or economic nature. The ruling procedure was implemented by a Royal Decree of 9 November 1992[14] and became effective on 1 January 1993. If a ruling is issued, it remains binding if the transaction was outlined to the tax authorities in good faith prior to its implementation (Art. 345, § 2, ITC). The tax authorities are no longer bound by the ruling if the transaction was not correctly and completely described by the taxpayer, was not implemented in the manner described by the taxpayer, or if the results of the transaction are modified later by other subsequent transactions in such a way that the transaction no longer meets the criteria of economic or financial necessity (Art. 345, § 3, ITC).

An interesting question is what the relationship is between this specific anti-avoidance rule and the recent general anti-avoidance rule provided for in Article 344, § 1, ITC.[15] According to the latter rule, the legal qualification that the parties give to an act – or to separate acts which realize the same transaction (which introduces the step transaction doctrine in Belgian income tax law) – is not binding on the tax authorities if they show, by means of presumptions or other evidence, that this qualification is aimed at tax avoidance. However, the taxpayer is allowed to provide the counterevidence that the qualification fulfils legitimate needs of a financial and economic nature. Although the meaning of this recent provision is far from clear at this stage, some learned authors have argued that the tax authorities may only invoke this provision if they show that a taxpayer has, for the purpose of avoiding taxes, created for himself, by means of legitimate and non shammed transactions, a situation of tax exemption which is so close to the situation which is not exempted by the law that the purpose of the law would be denied if the exemption would apply.[16] Article 344, § 1 ITC is a reaction to the case law of the Supreme Court which has held that there is no sham ("simulation"), and accordingly no tax fraud, when taxpayers carry out transactions, without violating any legal provisions but in an abnormal manner, to benefit from more favourable tax treatment, provided that they accept all the legal consequences of their transactions.[17] Since 1 October 1993 it is possible to apply for an advance tax ruling confirming that the general anti-avoidance rule does not apply.[18]

The differences between those two anti-avoidance provisions relate to the burden of proof and to the scope of application. As to the burden of proof, this falls on the taxpayer under the specific anti-avoidance rule, whereas it falls, at least in the first stage, on the tax authorities in the framework of the general anti-avoidance rule. As to the scope of application of both provisions, the specific anti-avoidance rule requires that the transaction itself fulfils legitimate needs of a fin-

14 *BOG of 25* November 1992.

15 This rule was introduced by the Law of 22 July 1993, *BOGof* 26 July 1993 (in replacement of the publication in *BOGof* 24 July 1993) and became effective for transactions entered into as from 31 March 1993.

16 Van Crombrugge, S., "De invoering van het leerstuk van *fraus legis* of wetsontduiking in het Belgisch fiscaal recht", *T.R.V,* 1993, 275, 280, 282 and 286.

17 Cass., 6 June 1961, *Pas.*, 1961, I, 1082; Cass., 29 January 1988, *F.J.F.*, No. 88/73; Cass., 22 March 1990, *F.J.F., No. 90/95.*

18 Royal Decree of 22 September 1993, *BOG,* 6 October 1993. For transactions entered into between 31 March 1993 and 1 October 1993, it is possible to apply for an "advance ruling" *a posteriori* prior to 30 November 1993.

ancial or economic nature whereas the general anti-avoidance rule requires that the legal qualification of an act fulfils legitimate needs of a financial or economic nature. Although both provisions will very often lead to the same result in the context of a demerger (i.e. that tax relief is not available), they may be complementary in certain circumstances (e.g. in the situation where the demerger is only a step in a chain of different transactions intended to accomplish one transaction) which has the objective of avoiding taxes. In such a case, the tax authorities may recharacterize the different transactions including the demerger into another transaction based on the general anti-avoidance rule (and the step transaction doctrine reflected therein) whereas under the specific anti-avoidance rule, they would only be able to deny tax relief but would not be able to recharacterize the demerger into another transaction.[19]

e. No Other Conditions

There is no need for prior government authorization[20] or an advance tax ruling in order to qualify for tax relief. There is also no requirement of continuity of shareholders in order to qualify for tax relief, so that the demerging company can sell the shares received in exchange for its contribution following the transfer of assets (subject to possible recharacterization under Article 344, § 1, ITC).

2. *Split-up*

Article 211, § 1, ITC (as modified by the law of 6 August 1993,[21] which became effective on 1 October 1993), provides for a mandatory[22] tax relief regime for a domestic split-up if the following three conditions are met.

a. Qualifying Receiving Companies

The receiving company must be a resident company i.e. a company having its registered office, principal establishment or seat of management in Belgium.

b. Compliance with the Company Law

Another condition for tax relief is that the split-up is enacted in accordance with the Company Law (see supra I.1, above). Accordingly, the tax authorities may re-

19 *See also Gedr. St.,* Senaat, 1992-93, No. 765/2, 34-36.

20 Until the Law of 28 July 1992, such approval was needed if a company contributed all its branches of activities.

21 *BOG* of 31 August 1993, 19106.

22 Notice in *BOG* of 12 August 1993, 18018.

fuse tax relief if the formalities provided for in the Company Law have not been entirely complied with. Taking into account that the company law procedure for a split-up is formalistic and complex and that it is unclear how serious the violation of the company law rules must be to deny tax relief, this requirement may prove to be dangerous in practice. From a theoretical point of view, one may also question whether it is appropriate to make more and more the tax authorities the protector of the Company Law.

c. Legitimate Needs of a Financial or Economic Nature

As is the case for a transfer of assets, a split-up must fulfil legitimate needs of a financial or economic nature in order to qualify for tax relief. The same principles described in the context of the transfer of assets apply fully here. Since 31 August 1993, it has been possible to apply for an advance tax ruling confirming that the split-up fulfils legitimate needs of a financial and economic nature, provided that the split-up occurs after 1 October 1993.[23]

d. No Other Conditions

Also in this context, there is no need for prior government authorization or an advance tax ruling in order to qualify for tax relief. There is also no requirement of continuity of shareholders so that the shareholders of the demerging company, who will normally become shareholders in the receiving companies in the same proportion, are not required to remain shareholders in the receiving companies, but can freely sell their shares (as a rule with an exemption of capital gains tax) amongst each other so that one or more shareholders end up with all the shares of one receiving company while one or more shareholders end up with all the shares of the other receiving companies ("scission répartition").

B. Tax Treatment of the Demerging Company

The technique of tax relief applied in this context consists of the deferal of corporate income tax at the level of the demerging company. Here again a destinction should be made between a demerger taking the form of a transfer of assets and a demerger taking the form of a split-up.

1. Transfer of Assets

The tax free regime is optional so that the demerging company may waive the tax deferral regime if a taxable transaction is more beneficial. This may be the case if

23 Notice in *BOG* of 12 August 1993, 18018.

the demerging company has losses to neutralize the capital gains resulting from the transfer of assets (since a taxable transaction may create a stepped-up basis for the receiving company) or if the receiving company has a loss carried forward which would otherwise be reduced as a result of a tax free demerger (contrary to what is the case in a taxable demerger – see infra II.D.2).

If the conditions for tax relief do not apply or if the demerging company waives tax relief, the demerging company will be taxable on the capital gains realized on the transfer of assets, i.e. the difference between the contribution value of the net assets or the value of the shares received and the tax value of the net assets contributed. The capital gains will be taxed at the ordinary rate (39% plus a crisis surcharge of 3%) in the year of the demerger since capital gains realized on the contribution of assets cannot benefit from the tax deferral regime provided for in Article 47, ITC.

If the conditions for tax relief apply and the demerging company does not waive tax relief, the demerging company is (temporarily) exempted from corporate income tax on the capital gains realized or recorded at the time of the contribution. These capital gains are considered unrealized capital gains, the taxation of which is deferred to the extent that they meet the “intangibility condition” provided for in Article 190, ITC (i.e. that they are and remain included in a separate reserve account of the demerging company).

Notwithstanding the fact that the receiving company must use a carry-over basis (see infra II.C.l), the shares received by the demerging company are attributed a value equal to the tax value of the assets received (and not their contribution value) so that any gain or loss realized in case of a subsequent disposal of the shares by the demerging company must be computed on the basis of the value corresponding to the demerging company’s tax basis for the transferred assets (Art. 46, § 3, para.l, ITC). However, the subsequent disposal of the shares received by the demerging company will as a rule not trigger effective taxation since capital gains realized on qualifying shares (i.e. shares the dividends of which would qualify for the dividend received deduction – which is normally the case for shares in Belgian companies) are unconditionally exempt from corporate income tax (Art. 192, ITC). In other words, the temporary exemption of the capital gains realized on the transferred assets is as a rule converted into a definitive exemption at the time the shares in the receiving company are disposed of. On the other hand, any write down recorded or any loss realized on the shares received will not be tax deductible since a transfer of assets does not involve a liquidation of the demerging company (i.e. the only case in which losses on shares are still deductible up to the amount of the paid-up capital) (Art. 198, 7°, ITC).

2. *Split-up*

If the conditions for a tax free split-up are met, the tax free regime applies.[24] Contrary to the case of a transfer of assets and to past practice,[25] the taxpayer can no longer opt in such case for a taxable split-up.

If the tax free regime applies, the demerging company is exempt from corporate income tax on the capital gains realized on the occasion of the split-up as well as on the unrealized capital gains and on the realized capital gains provided for in Article 47 ITC which were exempt from tax at the time of the demerger (Art. 211, §1, 1°, ITC).

However, a tax problem may arise if the demerging company has tax free retained earnings[26] and its transfer of assets to the receiving companies is not remunerated solely by the issuance of shares (because additional cash payments are made by the receiving companies or because the receiving companies own shares of the demerging company prior to the split-up).[27] This problem arises because:

(a) in the case of a taxable split-up, liquidation tax rules apply so that the liquidation gain (i.e. the difference between the value of the distribution to the shareholders and the paid-up capital of the demerging company) is treated as a dividend for purposes of the taxation of the demerging company (Art. 209, para. 1, ITC). As such, it results in taxable income to the demerging company to the extent that it is paid out of tax free retained earnings;

(b) the provisions with respect to tax-free split-ups exempt the demerging company from such taxation, but only to the extent that its contributions to the receiving companies are remunerated by shares (Art. 211, § 1, para. 1,2°, ITC);

(c) for this purpose, when such contributions are remunerated partly by shares and partly by cash or other consideration, the portion of the contributions remunerated by shares does not reduce tax free retained earnings (which carry over to the receiving companies) but the portion thereof allocable to the other consideration may do so and therefore result in taxation to the demerging company.[28] Such portion is first allocated to taxed retained earnings, so that taxation occurs only if such taxed retained earnings are not sufficient (Art. 211, § 2, para. 2, ITC);

(d) if the receiving company owns shares of the demerging company prior to the split-up, the tax situation of the demerging company is essentially the same, except that its retained earnings which do not carry over to the receiving companies are first allocated proportionally between paid-up capital and retained earnings; the portion allocated to retained earnings is allocated first to

24 Notice in *BOG* of 12 August 1993, 18018.

25 Com. ITC 39/21.2 (for a transfer of assets); Com. ITC 124/1 (for a split-up prior to the Law of 6 August 1993).

26 For examples thereof, *see Gedr. St.,* Senaat, 1992-93, 26.

27 For examples and more details thereof in the context of tax free mergers, *see* Annex 4 to the Report of the Commission of Finance, *Gedr. St.,* Senaat, 1992-93, No. 765/2, 68-77; De Broe, L., "Fiscale aspecten", *Fusies en Splitsingen,* Mys & Breesh, 1993, 96-104.

28 In such a case, the taxpayer can choose which retained earnings are reduced first, which allows him to benefit from the reduced rates provided for in Article 519bis ITC: *Gedr. St.,* Senaat, 1992-93, No. 765/2,29.

taxed retained earnings and is then allocated to tax free retained earnings (Art. 211, § 1, para. 3, ITC). Thus, allocation to tax free retained earnings is less likely to occur than in the case of cash payments.

It follows from the above that certain tax free split-ups (i.e. where the demerging company has tax free retained earnings and its contributions were not fully remunerated by shares of the receiving companies) are not entirely tax free. The tax neutrality would have been further increased if the law had allowed that, in line with Article 5 of the Merger Directive, the reduction of net equity could not only be allocated to the paid-up capital and taxed retained earnings of the demerging company, but also to those of the receiving companies.[29] An amendment to this effect was rejected during the parliamentary discussions.[30]

C. Tax Treatment of the Receiving Company

1. General

If the conditions for tax relief do not apply or if the demerging company waives tax relief in case of a transfer of assets, the assets transferred may benefit from a stepped-up basis in the hands of the receiving companies so that they may depreciate such assets at their contribution value. The capital increase of the receiving companies resulting from the contributions of the demerging company will for accounting and tax purposes be entirely treated as paid-up capital.

If tax relief applies, the receiving company must, in accordance with Article 4(2) of the Merger Directive, use a carry-over basis for tax purposes with respect to the assets transferred both in case of a transfer of assets (Art. 46, § 2, para.l, ITC) and in the case of a split-up (Art. 212, para.l, ITC). More specifically, the depreciation allowances, capital gains and capital losses and investment deductions relating to the transferred assets must be determined in the hands of the receiving companies as if the demerger had not taken place (neutrality or continuity principle). Based on this principle, the receiving company may not depreciate goodwill that would be booked as a result of the demerger and which was not shown in the books of the demerging company and it must take over the depreciation methods used by the demerging company. Accordingly, there will often be a difference between the accounting and tax results of the receiving company.

Moreover, the specific rules applicable to capital gains, write downs, provisions, undervaluations or overvaluations, subsidies, receivables and, in case of a split-up, retained earnings which were part of the demerging company remain applicable to the receiving company, provided that those elements are part of the assets contributed (Art. 46, § 2, para.2, ITC for a transfer of assets and Art. 212, para.2, ITC for a split-up). For instance, in applying Article 47 ITC, which provides that capital gains realized on the sale of fixed assets used for more than 5

29 *See also* Lycops, J.P., and Blockerye, T., "Fusie en splitsing van vennootschappen", *A.F.T.,* 1993, 207.

30 *Gedr. St.,* Senaat, 1992-93, No. 765/2, 37-39.

years are, provided that the sales proceeds are re-invested within 3 (or 5) years in qualifying assets, taxed over the period of depreciation of the assets in which they have been reinvested, the five year period starts to run as from the acquisition date of the relevant assets by the demerging company and the reinvestment period is not extended as a result of the demerger.

In the same line of reasoning, only that part of the capital increase resulting from a transfer of assets that corresponds to the tax net asset value of the transferred assets will be treated as paid-up capital for tax purposes (Art. 184, para. 2, ITC). In the case of a split-up, the paid-up capital of the receiving company resulting from the split-up is determined for tax purposes as if the split-up had not taken place (Art. 212, para. 1, ITC), i.e. by a prorata allocation of the paid-up capital of the demerging company.

The neutrality or continuity principle described above will also be introduced in the accounting legislation for tax free transfers of assets and for split-ups enacted in accordance with the Company Law so that as a rule there will no longer be discrepancies between the tax treatment of the contribution (which is based on the tax value of the contribution) and the accounting treatment of the contribution (which is based on the contribution value of the contribution). Indeed, a proposed Royal Decree on the modification of the Royal Decree of 8 October 1976 on the financial statements of companies[31] provides that all contributed assets and liabilities and all revenues and expenses relating to the current accounting year of the demerging company are transferred to the receiving companies at the value at which they were accounted for in the demerging company at the time at which the demerger occurs for accounting purposes. Importantly, all the elements of the net equity will keep their original qualification in the receiving companies and will no longer be recharacterized and booked as capital or issue premium in the hands of the receiving companies.[32]

In the context of a split-up, a number of specific issues arise, such as the division of the net assets of the demerging company. Article 213 ITC provides that the paid-up capital as well as the taxed and tax free retained earnings of the demerging company are deemed to be received by the receiving companies in proportion to the *tax* net asset value of the contributions made by the demerging company to each of the receiving companies.[33] The tax net asset value, a term which is not defined in the Income Tax Code, is equal to the difference between the tax value of the assets and the tax value of the liabilities.[34] To this effect, the book value of the assets and liabilities must be adapted to the tax rules, e.g. hidden reserves

31 The text thereof is published as Annex 3 to the Report of the Commission of Finance, *Gedr. St.*, Senaat, 1992-93, No. 765/2, 65.

32 However, the accounting treatment will remain different from the tax treatment in certain situations (Art. 36bis, § 4, § 5 and § 6 respectively of the proposed Royal Decree). For more details, *see* Bats, G., “Fusies en splitsingen. Revisorale aandachtspunten naar de praktijk toe”, Tax Seminar Fiskale Hogeschool of 17 September 1993, 45-72.

33 This is a confirmation of Com. ITC 124/21; Com. ITC 124/29 and Com. ITC 124/37, although the latter comment may lead to another result for capital gains which are not part of the tax net asset value.

34 *Gedr. St.*, Senaat, 1992-93, No. 765/2, 13-15.

(such as depreciation excesses or undervaluations in inventory) must be added to the book value whereas the expressed non-realized capital gains and the capital gains realized at the time of contribution are not taken into account for the purposes of calculating the tax value. For tax purposes, the liabilities also include the tax free provisions. The use of the tax net asset value instead of the book net asset value may give rise to complications,[35] e.g. if the tax net asset value of the contribution is negative whereas the conventional value of the contribution is positive (which is an essential requirement for company law purposes).

A surprising consequence of the above may arise in the event that the demerging company has tax free retained earnings set up in the framework of Article 47, ITC with respect to capital gains, the taxation of which is deferred. Since such tax free retained earnings are divided between the receiving companies in case of a tax free split-up, the capital gain originally exempt and remaining exempt at the time of the split-up will be taxed over the depreciation period of the re-invested asset to all the receiving companies and not only to the company which has received the asset in which reinvestment was made. In the case of a transfer of assets the paid-up capital, the taxed and tax free retained earnings and the provisions of the demerging company are not transferred to the receiving company but remain with the demerging company.[36] This may cause surprising results in the context of Article 47, ITC since the tax free retained earnings will become taxable in the hands of the demerging company and not in the hands of the receiving company.

2. Treatment of Losses

a. Losses of the Demerging Company

In case of a taxable demerger, the losses of the demerging company may never be transferred to the receiving companies. In case of a tax free demerger, the neutrality principle is only partly applied to losses of the demerging company. In a tax free transfer of assets, the receiving company is not allowed to take over the losses of the demerging company.[37] On the other hand, the Law of 6 August 1993 has made it possible in a tax free split-up to transfer losses from the demerging company to the receiving companies within certain limits.[38]

The carry-over of losses of the demerging company is calculated as follows. First, the loss carry forward of the demerging company is divided between the receiving companies on the basis of the tax net asset value contributed to each of

35 *See* Cougnon, J., “La répartition entre les sociétés issues d’une scission des fonds propres d’une société scindée”, *R.G.F.*, 1989, 197.

36 Servais, T., *op.cit*, 67, 189 and 206.

37 This is based on the doctrine of the Supreme Court that a loss may only be deducted in the hands of the company which has sustained the loss: Cass., 17 May 1926, *Pas.*, 1926, I, 378 and Cass., 8 June 1936, *Pas.*, 1936, I, 282.

38 This rule is intended to make the choice of the absorbing company in a merger tax neutral and to put an end to the widespread phenomenon of the “reverse mergers” where the loss-bearing company absorbed the profitable company.

them. Second, the losses attributed to each receiving company are only available in the proportion that the tax net asset value of the contribution received (as determined prior to the split-up) bears to the tax net asset value of the contribution received increased by the tax net asset value of the receiving company (as determined prior to the split-up) (Art. 206, § 2, para. 2, ITC). If the tax net asset value of the contribution is negative, the tax authorities deem it equal to zero, with the practical result that no losses can be transferred.[39] This point of view is subject to criticism.

It follows that, if the assets and liabilities of a (loss-bearing) demerging company are transferred to two or more new companies, the entire losses of the demerging company will remain available since the new receiving companies do not have a tax net asset value prior to the split-up. If the receiving companies are existing companies, the amount of the losses that may be transferred to them will be limited according to the prorata rule described above unless the receiving companies would have a negative tax net asset value (since the tax authorities deem it equal to zero). The amount of the transferable losses would be increased by increasing the tax net asset value (e.g. by means of a capital increase) of the demerging company prior to the split-up. However, the tax authorities might disregard such capital increase, treating it as only one step in a chain of transactions, on the basis of the general anti-avoidance rule of Article 344, § 1, ITC.[40]

b. Losses of the Receiving Companies

In addition to the limitations mentioned above, Belgium also imposes restrictions on the losses that the receiving companies had at the time of the demerger, which assumes that the receiving companies are existing companies. More specifically, in case of a *taxfree* transfer of assets or split-up, the losses of the receiving companies are only deductible following the demerger in the proportion that the tax net asset value of the receiving company before the transaction bears to the tax net asset value of the receiving company before the transaction increased by the tax net asset value of the contributed assets (Art. 206, § 2, para. 1, ITC).[41] If the tax net asset value of the receiving company is negative (and is therefore deemed by the tax authorities to be equal to zero[42]), the previous losses of the receiving company will no longer be deductible.

On the other hand, in the case of a *taxable* transfer of assets or split-up, the receiving company is entitled to fully set off its losses against any profits relating to the transferred assets. This may be a reason in certain cases to opt for a taxable

39 *Gedr. St.,* Senaat, 1992-93, No. 765/2, 17-18.

40 *Gedr. St.,* Senaat, 1992-93, No. 765/2, 19; Van Crombrugge, S., “Fusies en splitsingen in het inkomstenbelastingrecht anno 1993”, *T.R.V.,* 1993, 362-363; *contra:* De Broe, L., *op.cit.,* 121-122.

41 Prior to the Law of 6 August 1993, the deduction of the receiving company’s losses (possibly limited according to the prorata rule) was allowed only if the demerger met ligitimate needs of a financial and economic nature; the limitation of losses according to the prorata rule was in our opinion not applicable to the receiving company in a tax free split-up.

42 *Gedr. St.,* Senaat, 1992-93, No. 765/2, 17.

transfer of assets. Since it is no longer possible to opt for a taxable split-up once the conditions for tax relief are met, the demerging company may have an interest in deliberately putting oneself outside the scope of the new company law rules on split-ups (e.g. by winding up and liquidating the demerging company[43]) or in arguing that the conditions for tax relief are not met (e.g. that the split-up does not fulfil legitimate needs of a financial or economic nature) in order to avoid a limitation of losses pursuant to Article 206, ITC. It is unclear whether the tax authorities may in such case invoke the general anti-abuse rule in order nevertheless to limit the losses of the receiving companies. In any event, it is not possible to apply for an "advance negative ruling" which would confirm that the conditions for tax relief are not met.

Moreover, the loss recovery of the receiving companies is further reduced by the general (and very anti-economic) rule pursuant to which the maximum amount of losses that may be offset per year is equal to the greater of 50% of the annual taxable profits or BF 20,000,000 (Art. 206, § 1, para. 2, ITC).

D. Tax Treatment of the Shareholders of the Demerging Company

The tax treatment of the shareholders of the demerging company must be considered at the time of the demerger and at the time of a subsequent disposal of the new shares received from the receiving companies. Only the situation of the Belgian shareholders will be discussed.

1. Transfer of Assets

In case of a transfer of assets, the demerging company itself, and not its shareholders, receives the shares issued by the receiving company at the time of the capital increase resulting from the transfer of assets. Accordingly, a transfer of assets has no direct tax impact on the shareholders of the demerging company, but only on the demerging company itself (see supra II.B.1.).

2. Split-up

2.1. At the Time of the Split-up

At the time of the split-up, a distinction must be made depending upon the qualification of the split-up (taxable, tax free or partially tax free split-up) and depending upon the capacity of the shareholders (individuals holding the shares as a private investment, individuals holding the shares for business purposes[44] and com-

43 This possibility has been confirmed in the explanatory statement to the Law of 6 August 1993: *Gedr. St.,* Senaat, 1992-93, No. 765/1,4-5.

44 This hypothesis is not discussed here since it is very exceptional in practice.

panies). In all these events, the liquidation gain distributed by the demerging company (i.e. the difference between the value of the distribution to the shareholders and the paid-up capital of the demerging company – see supra II.B.2.) which is treated as a dividend for purposes of the taxation of the demerging company, is exempt from witholding tax (Art. 264, 2°, ITC jo Art. 209, para. 1, ITC).

a. Taxable Split-up

Belgian resident individuals who held the shares of the demerging company as a private investment are not taxable on the "liquidation bonus" received, i.e. on the capital gains realized on the exchange of shares in the demerging company against the shares of the receiving companies (Art. 313, 1°, ITC). Conversely, losses realized on the shares by such individuals are not tax deductible.

Belgian corporate shareholders are taxable on the difference between the value of the new shares in the receiving companies and the tax value of their shares in the demerging company. This "liquidation bonus" will benefit from the dividend received deduction and will thus be 95% exempt (Art. 202, 1° and 204 para. 2, ITC), provided that the shareholders had a participation of at least 5% or of an acquisition value of at least BF 50,000,000 in the demerging company at the time the liquidation bonus is paid[45] and that dividends distributed with respect to these shares would qualify for the dividend received deduction – which is normally the case for Belgian companies – (Art. 203, ITC). If the conditions for the dividend received deduction are not met, the liquidation bonus is fully taxable. If corporate shareholders realize a loss on their shares in the demerging company at the time of the split-up, the loss is, in our opinion, tax deductible to the extent of the paid-up capital represented by the relevant shares pursuant to Article 198, 7°, ITC.[46]

b. Tax Free Split-up

Capital gains realized by a Belgian resident individual on his shares in the demerging company held as a private investment are in principle tax exempt (Art. 90, 1°, ITC), even if he had a substantial shareholding in the demerging company (Art. 95, ITC). Conversely, losses realized on the shares of the demerging company are not tax deductible.

Capital gains realized or recorded by Belgian corporate shareholders of the demerging company on the occasion of the split-up are treated as unrealized capital gains, which are exempt from income tax, subject to the "intangibility condition" (i.e. that the capital gains are and remain included in a separate reserve account) (Art. 45, para. 1, ITC). As capital gains realized on shares are as a rule unconditionally exempt since the Law of 23 October 1991, it has been argued that capital

45 This condition does not apply to credit institutions and insurance companies (Art. 203, para. 3, ITC).

46 The reason is that a split-up is for tax purposes still treated as a liquidation (Art. 210, § 2, ITC). This opinion is reportedly not followed by the Minister of Finance. *See also* Lycops, J.P., and Blockerye, T, *op.cit.,* 210;Tilquin,T, *Traité des fusions et scissions,* Kluwer, 1993,468.

gains realized on shares on the occasion of a tax free split-up should also be unconditionally exempt or that the violation of the intangibility condition is not sanctioned,[47] but this point of view is not shared by ourselves and by the tax authorities.[48]

Accordingly, if the new shares received in exchange for the shares in the demerging company are never desposed of, the capital gain originally exempt at the time of the demerger will become taxable at the time the intangibility condition is no longer met and in any event at the time of the liquidation of the corporate shareholders. This issue will become less relevant since the accounting legislation will provide that the shares in the receiving companies received in exchange for the shares in the demerging company must be booked at the value at which the shares in the demerging company were booked. If corporate shareholders realize a loss on their shares in the demerging company at the time of the split-up, the loss is in our opinion tax deductible to the extent of the paid-up capital represented by the relevant shares.[49]

c. Partially Tax Free Split-up

If the shareholders of the demerging company receive a cash payment in addition to shares of the receiving companies, this payment will be considered as a dividend (Art. 18,1°, ITC).[50] Belgian resident individuals who held the shares as a private investment will not be taxable on such dividend. Belgian corporate shareholders will be taxable on the dividend, but will normally benefit from the 95% dividend received deduction (Art. 202, 2°, ITC).

If one or more of the receiving companies had shares in the demerging company, the positive difference between the net contribution value of the demerging company represented by the shares in the demerging company and the tax value of the shares in the demerging company held by the receiving company is treated as follows.[51] That part which is treated as a dividend in the hands of the demerging company will as a rule benefit from the dividend received deduction of 95% in the hands of the receiving company, to the extent that this part corresponds to the difference between the tax net asset value of the demerging company corresponding to the shares in the demerging company and the tax value of the shares in the demerging company held by the receiving company (Art. 202, 2°, ITC). Any excess must be treated as an unrealized capital gain, which is exempt subject to the "intangibility condition" (Art. 45, ITC).

47 De Broe, L.,"Fiscale Aspecten", *op.cit.,* 85; Van De Woesteyne, I., "De nieuwe fiscale regeling inzake fusies en splitsingen", *Het nieuwe stelsel inzake fusies en splitsingen van vennootschappen,* Biblo-dossier-21, 1993, 58.

48 In the same sense: Lycops, J.P., and Blockerye, T., *op.cit.*, 213; Kirkpatrick, J., *Le régime fiscal des sociétés en Belgique,* Bruylant, Bruxelles, 1992, 188; *Gedr. St.,* Senaat, 1992-93, No. 765/2, 30.

49 *See* footnote 46.

50 Tilquin, T., *op.cit.*, 470.

51 Explanatory statement to the Law of 6 August 1933 *(Gedr. St.,* Senaat 1992-93, no. 765/1, 7), which also explains how a negative difference must be treated. *See also* De Broe, L., *op.cit.,* 105-111.

2.2. At the Time of the Subsequent Disposal of the New Shares

Capital gains realized at the time of the subsequent disposal of the new shares received on the occasion of the demerger will as a rule not trigger effective taxation while the capital losses will as a rule not be tax deductible.

Capital gains realized by resident individuals who held the shares as a private investment are as a rule exempt from individual income tax (Art. 90, 1°, ITC). There are, however, two exceptions to this rule. First, if the sale of the shares were to be considered a speculative activity,[52] the capital gain would be taxed at a rate of 33% (Art.90, l°and 171, 1°, a, ITC). Second, if the shares are part of a “substantial shareholding” and the buyer is a non-resident company, the capital gains realized on such shares are taxed at a rate of 16.5% (Art. 90,8°; 94;171,4°, d, ITC). In order to determine whether there is a substantial shareholding, one must take into account the extent of the shareholding prior to the split-up (Art. 96, ITC).

Capital gains realized by Belgian corporate shareholders on shares in Belgian companies are as a rule unconditionally exempt from corporate income tax (Art. 192, ITC). Capital gains realized on non qualifying shares (e.g. shares in certain Belgian joint investment companies) will be fully taxable. The capital gains (or losses) on the new shares received on the occasion of the split-up are determined on the basic of the tax value of the old shares (Art. 45, para. 2, ITC).

On the other hand, any loss realized at the time of the subsequent disposal of the shares in the receiving company will not be tax dedeuctible, except if the loss is realized by a corporate shareholder at the time the receiving company is liquidated, in which case the loss is deductible to the extent that the tax value of the shares in that company would be less than that company’s paid-up capital (Art. 198, 7°, ITC).

E. Shareholders of the Receiving Companies

In case of a transfer of assets, the demerging company itself receives the shares issued by the receiving companies. The tax treatment of the shares received by the demerging company has been described under II.B.l. In case of a split-up, the shareholders of the receiving companies will as a rule be the same as those of the demerging company (see supra II.D.2.) provided that the receiving companies were new at the time of the split-up. If the receiving companies already existed at the time of the split-up. If the receiving companies already existed at the time of the split-up, the split-up will normally not have a tax impact on the original shareholders of the receiving companies.

52 There are only a few cases where the courts have concluded to a speculative intent or to a transaction falling outside the scope of the normal management of a private patrimony in the context of the sale of shares: Bruxelles, 20 January 1981, *J.D.F.*, 1982, 119; Antwerpen, 3 May 1982, *F.J.F.*, 83/46; Liège, 19 December 1991, *Bull.Bel.*, 1993, 121.

F. Transfer Taxes

The capital increase resulting from a domestic transfer of assets and a split-up is exempt from the 0.5% capital tax provided that there is no cash payment in excess of 10% (Art. 117 of the Code on Registration Duties). No transfer taxes are due on the transfer of real estate or other assets within the framework of a demerger. A transfer of assets and a split-up are also exempt from VAT provided that the receiving company is a VAT taxpayer[53] (Art. 11 of the VAT Code).

III. Cross-border Demergers

For tax purposes, a distinction must be made between cross-border demergers depending upon whether or not the receiving companies are located in the EC. If they are located in the EC, the Merger Directive should apply as of 1 January 1992. Before discussing the tax treatment of cross-border demergers, their feasibility from a company law point of view will be shortly discussed.

A. Company Law Aspects of Cross-border Demergers

A transfer of assets by a Belgian demerging company to a foreign company is possible from a Belgian company law point of view since it does not require the dissolution of the demerging company and is equivalent to a contribution in kind to the foreign company, which as a result increases its capital. Conversely, a transfer of assets by a foreign company to a Belgian receiving company is also possible from a Belgian law point of view provided that the Belgian Company Law formalities with respect to contributions in kind are met.

On the other hand, a cross-border split-up (i.e. the situation where assets and liabilities of a Belgian demerging company are transferred to one or more new or existing foreign companies) is more difficult since the new Belgian company law rules on split-ups do not apply to cross-border transactions. By analogy to what has been said in the context of mergers, a Belgian company may not be split-up under the new company law rules (i.e. by means of dissolution without liquidation) by transferring its assets and liabilities to one or more foreign companies, because such a split-up would result in a loss of the nationality of the demerging company, an essential feature which cannot be changed by the shareholders.[54] This argument is in our opinion subject to criticism and in any event does not apply in case of unanimous vote.[55] Cross-border split-ups without liquidation are also not yet regulated at EC level, nor are they covered by the proposal for a 10th

53 If the receiving company is not yet a VAT taxpayer, it will normally become a VAT taxpayer as a result of the transaction, in which case the exemption also applies: *Gedr. St.*, Kamer, 1968, no. 88/1, 14.

54 *Gedr. St.*, Kamer, 1989-90, no. 1214/1, 1.3.

55 *See also* Ronse, J., "Vennootschappen – Overzicht van rechtspraak (1964-1967)", *T.P.R.*, 1967, 654; Tilquin, T., *op.cit.*, 521, 534.

EEC Directive concerning cross-border mergers of public limited companies.[56] In the meantime, cross border split-ups of a Belgian company will have to occur through the winding up and liquidation of the demerging company, as was the case for domestic split-ups prior to the Law of 29 June 1993. Conversely, a foreign company may be split-up and transfer its assets and liabilities to one or more Belgian companies, provided that the “lex societatis” of the demerging company does not prohibit this.[57]

B. Cross-border Demergers within the EC

Belgium has only partially implemented the Merger Directive.[58] Only a cross-border transfer of assets within the EC can be done in a tax free manner. A tax free cross-border split-up within the EC is not yet possible under domestic tax law and will be taxed as a liquidation.

1. Direct Effect of the Merger Directive?

The reason invoked for the non implementation of the Merger Directive in the context of a split-up is that the company law, either at the level of EC directives, or at national level, does not yet permit such transactions.[59] Later on, Belgium also put forward the excuse that it is not the only country which takes that position[60] and that the European Commission has not yet urged Belgium to implement the Merger Directive.[61] The Conseil d’Etat (an advisory board on the drafting of legislation) rightly objected that the non-implementation of the Merger Directive is not consistent with the obligations imposed upon Belgium by the European legislation.[62]

Since the Merger Directive imposes “clear and unconditional obligations” on the Member States, the Merger Directive has in our opinion direct effect from 1 January 1992. It follows that taxpayers should be entitled to the benefits thereof if the Merger Directive is more favorable than the domestic law provisions (which is certainly the case in Belgium for cross-border split-ups and to a certain extent also for cross-border transfers of assets) and that a national judge must, at the request of a taxpayer, apply the Merger Directive as if it had been implemented on time. Moreover, the European Court of Justice has ruled in the Francovich decision that “Community law imposes the principle that Member States are obliged to make good any damage suffered by an individual as a result of their violations

56 *O.J.,* C 23 / 11 of 25 January 1985.
57 *Gedr. St.,* Kamer, 1989-90, No. 1241/1, 3.
58 *See* footnote 8.
59 *Gedr. St.,* Kamer, 1989-90, No. 1214/2, 5.
60 Also Germany, Greece and the UK take this position.
61 *Gedr. St.,* Senaat, 1992-93, No. 765/2,4 and 9.
62 Advice of the Conseil d’Etat, *Gedr. St.,* Kamer, 1989-90, No. 1214/3, 9-10.

of Community law".[63] The fact that Belgian company law does not cover cross-border split-ups and that therefore such split-up will occur through the dissolution and liquidation of the demerging company and not by universal succession (on which concept the Merger Directive is based) is, in our opinion, not an obstacle to the above conclusion.[64] Indeed, we believe that, on the basis of the purposes of the Merger Directive (i.e. the removal of tax barriers in the context of cross-border reorganizations, the Merger Directive should also be applicable to transactions similar to the ones considered (e.g. transactions involving the liquidation of the transferring company). Notwithstanding the above, it may be expected that no or few companies will rely on the above doctrine to implement a cross-border split-up.

It should be noted that taxpayers cannot rely on the Merger Directive for domestic demergers since Article 1 of the Merger Directive explicitly provides that it only applies to crossborder reorganizations and since the non-discrimination principle laid down in Article 7 of the EC Treaty is not violated if a domestic transaction is treated less favorably than a crossborder transaction.[65] It follows that, if and when Belgium implements the Merger Directive in the context of cross-border split-ups or fully implements the Merger Directive in the context of a transfer of assets (which is, in our opinion, not yet the case for certain specific issues) cross-border demergers may benefit from a more favorable treatment than domestic demergers under current law.[66] However, the Minister of Finance has already announced that, in such case, the tax regime on domestic reorganizations will also be adapted to the new rules on cross-border reorganizations in order to avoid a different set of rules for domestic and cross-border reorganizations.[67]

2. Cross-border Transfer of Assets

Belgium has inplemented the Merger Directive as far as the transfer of assets in concerned, but the implementation legislation is on certain points more restrictive than the Merger Directive.

63 European Court of Justice, 19 November 1991, C-6/90 and 9/90, *Jur.,* 1991 5357. *See also* C-271 /91, *Marshall c'Southampton and South West Hampshire A rea Health A uthority,* 2 August 1993, not yet published; Steiner, J., "From direct efects to Francovich: shifting means of enforcement of Community Law", *E.L.R.,* 1993, 3.

64 *Contra:* Malherbe, J., "La loi du 6 août 1993 modifiant le régime fiscale des fusions et des scissions", *Le Nouveau droit des fusions et des scissions de sociétés,* Tax Seminar U.C.L. of 22 October 1993, 3.

65 *Contra:* Kleynen, G., "Le droit fiscal au regard de la directive européenne sur les fusions et apports transfrontaliers", *R.G.F.,* 1993, 50.

66 Such discrimination would be contrary to Article 6 of the Constitution according to Vanistendael, F., "De belasting van grensoverschrijdende fusies", *A.F.T.,* 1991, 152.

67 *Gedr. St.,* Senaat, 1992-93, No. 765/2, 3-4 and 9.

a. Domestic Law Rules

In order to qualify for tax relief, the receiving company must be a resident company or a foreign company having its registered office, principal establishment or seat of management in an EC Member State (hereafter an "EC company"). The other conditions to qualify for tax relief are the same as for a domestic transfer of assets (see supra II.A.1.) but there is the additional condition that the assets and liabilities transferred become part of, and be effectively connected with, a permanent establishment of the receiving company in the Member State where the demerging company is located. Under Article 46, para. 3, ITC, if the receiving company is situated in another EC Member State, the assets transferred are deemed to constitute a Belgian establishment of the receiving company. The meaning of a Belgian establishment, as defined in Article 229, § 1, ITC, is somewhat broader than a permanent establishment within the meaning of Article 5 of the 1993 OECD Model Convention.

The tax is deferred until the assets transferred are disposed of or are no longer connected with the Belgian establishment (in which case they are considered to have been disposed of). In such a case, the Belgian establishment is deemed to realize the transferred assets at market value.[68] There may be circumstances in which Belgium is not able to tax the capital gains realized by the foreign receiving company on the alienation of assets forming part of its Belgian establishment, namely if such establishment is not considered a permanent establishment under the relevant tax treaty. Indeed, under Article 13(4) of the 1993 OECD Model Convention, the State of residence of the receiving company has the right to tax the capital gains realized by it on the alienation of assets not forming part of a permanent establishment.

The other tax implications of a tax free cross-border transfer of assets within the EC are the same as for a domestic tax free transfer of assets (see supra II.B.1.). At the time of subsequent disposal of the shares received, the tax treatment of a Belgian demerging company which receives shares in EC companies may, however, be different from a Belgian demerging company which receives shares in a Belgian company. Indeed, the capital gain tax exemption on shares does not apply to shares in (i) tax haven companies, (ii) foreign holding companies or financing companies which enjoy a privileged tax status in their country of residence, (iii) joint investment companies, and (iv) foreign intermediary holding companies holding shares in the afore-mentioned types of companies (Art. 192, ITC).[69]

b. Compatibility of the Implementation Legislation with the Merger Directive

As a rule, the domestic tax rules on a transfer of assets within the EC described above are in line with the Merger Directive. However, the conditional and tem-

68 *Gedr. St.,* Kamer, 1991-92, No. 444/1, 12.

69 The Belgian tax authorities have published a black list of countries and companies falling under (i) and (ii) in *BOG* of 24 August 1991, 18431.

porary nature of the tax relief to the Belgian demerging company is in our opinion incompatible with the Merger Directive. More specifically, the fact that the taxation of the capital gains realized by the Belgian demerging company is only deferred to the extent that the intangibility condition is met and the fact that the shares received are attributed only a value equal to the tax value of the assets transferred, is, in our opinion, contrary to Article 9 of the Merger Directive.[70] On the other hand, the scope of application of the Belgian implementation legislation (which applis to all forms of commercial companies) is broader than that of the Merger Directive (which only applies to the forms of companies enumerated in the annex to the Merger Directive).

c. Transfer by an EC Company of its Belgian Establishment to a Foreign Company

As a rule, capital gains realized by non-residents on the disposal of a Belgian establishment are taxable in Belgium (Art. 228, § 2(3), ITC), provided that Belgium is allowed to tax them in accordance with Article 13(2) of the 1993 OECD Model Convention (which will be the case if the Belgian establishment qualifies as a permanent establishment under the relevant tax treaty). In line with Article 10(1) of the Merger Directive, Article 231, § 2, ITC provides for an exception to this rule if a Belgian permanent establishment is among the assets transferred by an EC demerging company in a tax free demerger. The capital gains established as a result of the transfer of the Belgian permanent establishment or of some of its assets are exempt from Belgian income tax, provided that such establishment or such assets remain invested in Belgium. Since the location of the receiving company is not specified, it may also be a company established outside the EC. As is the case in a domestic split-up or transfer of assets, the Belgian establishment of the receiving company must use a carry-over basis for tax purposes with respect to the transferred assets and most of the tax attributes (but not the losses) of the Belgian permanent establishment are carried over as if the transfer had not taken place (Art. 231, § 2, para. 3, ITC).

We believe that Article 231, § 2, ITC covers only three-country situations in which a company situated in one EC Member State transfers its Belgian establishment to a company of a third country and that it does not cover two-country situations where a foreign company contributes its Belgian establishment to a Belgian company (see III.B.2.d.).

[70] *See also* Kirkpatrick, J., “Les Fusions et apports transfrontaliers régis par la directive fiscale européenne sur les fusions de 1990 et l’état du droit belge au 1er janvier 1992”, Tax Seminar K.U.Leuven of 14 March 1992.

d. Transfer by a Foreign Company of its Belgian Establishment to Belgian or EC Company

If a foreign EC or non-EC company transfers its Belgian establishment to a Belgian or EC company (i.e. the roll-over of a branch into a company) or a division of a Belgian establishment to a Belgian or EC company, tax relief is only available to the extent that the shares received by the non-resident company in exchange for the transfer of assets are used in the exercise of a business activity in Belgium and that the capital gain is and remains included in a separate reserve account of the Belgian permanent establishment (Art. 236, ITC). This assumes that the shares are invested in a Belgian establishment of the non-resident company. Accordingly, a non-resident company may transfer one or more branches of activity of its Belgian establishment provided that the shares received remain part of the remaining part of the Belgian establishment. When the shares cease to be invested in a Belgian establishment, they are considered to have been disposed of and taxation may arise at that time. The tax authorities deem that no tax relief is available if a non-resident company transfers the entirety of its Belgian establishment to a Belgian or EC receiving company since the additional requirement cannot be met in such case.[71] While it is uncertain whether this additional requirement conflicts with Article 10 of the Merger Directive,[72] the ratio legis therof is unclear since capital gains realized on qualifying shares are unconditionally exempt pursuant to Article 192, ITC.

e. Transfer by Belgian Company of a foreign Permanent Establishment

A distinction must be made depending upon whether or not the foreign permanent establishment is located in a treaty country. If the permanent establishment is located in a country that has a tax treaty with Belgium, the right to tax capital gains which relate to the foreign permanent establishment is attributed to the State where the permanent establishment is located, in accordance with Aricle 13(2) of the 1993 OECD Model Convention. Accordingly, the capital gains tax regime will be governed by the rules ofthat country. If the permanent establishment is located in a country that does not have a tax treaty with Belgium, Belgium will tax the capital gains resulting from the transfer of the permanent establishment and will use the Belgian tax rules for purposes of determining the tax base. The Belgian tax due on those capital gains is reduced to one fourth of the ordinary corporate income tax (Art. 217, ITC).

The transfer of a foreign permanent establishment involves the problem of the recapture of previously deducted losses of the permanent establishment. The Belgian tax legislation does not provide for a special recapture rule for previous losses of a foreign permanent establishment at the time the permanent establish-

71 Com. ITC 142/11.

72 *See* Van De Velde, L, “Filialisation d’un établissement belge: taxation des plus-values?”, *Fiscologue International*, 22 October 1993, 4.

ment is transferred. More specifically, Belgium has not incorporated the particular recapture mechanism provided for in Article 10(1) of the Merger Directive. This rule authorizes the State of the transferring company (Belgium) to reinstate in the taxable profits of the company the losses of the permanent establishment as may previously have been set off against the taxable profits of the transferring company and which have not been recovered at the time of transfer. Importantly, such recapture does not require any effective deduction of the losses in the permanent establishment.

The only recapture rule is found in the tax treaties, in which Belgium reseres the right to tax income from a foreign permanent establishment if it is not taxed abroad as a result of loss deduction and if the deducted loss at the level of the permanent establishment was already deducted from taxable income in Belgium (which is only possible to the extent that such losses exceed the aggregate profits from treaty countries)[73] in a previous taxable year. Accordingly and contrary to the rule provided for in the Merger Directive, this recapture rule will only apply if the previously deducted losses have been effectively deducted twice. It follows that, if assets transferred by a Belgian company in a tax-free split-up or transfer of assets include a foreign permanent establishment, the recapture rule in the tax treaties will not apply since there will be no effective loss deduction in the foreign permanent establishment.

3. Cross-border Split-up

Depending upon whether or not one accepts the direct effect of the Merger Directive, the current tax regime on cross-border split-ups may be summarized as follows.

a. Domestic Law Rules

If one does not accept the direct effect of the Merger Directive, a cross-border split-up of a Belgian company in which one of the receiving companies is a resident in another country will be considered a taxable liquidation of the Belgian demerging company under current domestic tax law. As described under II.B.2. there are two basic tax consequences for the demerging company. First, the demerging company will be taxable on the capital gain realized or recorded on the occasion of the split-up. Second, the liquidation proceeds are treated in the hands of the demerging company as a dividend to the extent that they exceed the paid-up capital for corporate income tax purposes (Art. 209, para. 1, ITC), thus triggering taxation of tax free retained earnings. Importantly and somewhat surprisingly, under Belgian domestic tax law there is no withholding tax on the liquidation proceeds distributed to Belgian or foreign shareholders (Art. 262, 2°, ITC), so the qualification of such proceeds under the tax treaties becomes less relevant.

[73] Article 78, para. 2 of the 1992 Royal Decree implementing the ITC.

On the other hand, the foreign receiving companies, which will normally have a permanent establishment in Belgium as a result of the split-up, are entitled to depreciate the transferred assets on a stepped-up basis. They are not allowed to take over the tax attributes of the Belgian demerging company. The Belgian corporate shareholders of the demerging company will become taxable on the "liquidation bonus" received, but may under certain conditions benefit from the dividend received deduction of 95% (see supra II.D.2.a.).

b. Rules Based on the Direct Effect of the Merger Directive

If one accepts the direct effect of the Merger Directive, the tax implications of a Belgian demerging company transferring its assets and liabilities to EC receiving companies may be summarized as follows. The capital gains realized on the assets transferred to an EC receiving company would not give rise to any taxation, provided that the assets and liabilities are effectively connected with a permanent establishment of the receiving companies in Belgium (Art. 4(1) of the Merger Directive). Taxation will arise at the time the permanent establishment is closed down. The tax free retained earnings and provisions constituted by the demerging company which are not derived from permanent establishments abroad would be carried over, with the same tax exemption, to the permanent establishment of the receiving company in Belgium (Art. 5 of the Merger Directive). The receiving companies would have to use a carry-over basis for tax purposes with respect to the assets transferred (Art. 4(2) of the Merger Directive). Since Belgium already allows the receiving company in a domestic split-up to take over within certain limitations tax losses of the transferring company, such tax losses may within the same limitations be carried over in a cross-border split-up to the permanent establishment of the receiving companies in Belgium (Art. 6 of the Merger Directive). The taxation in respect of the shares in the EC receiving company received by the Belgian shareholders would be deferred in accordance with Article 45 ITC, but without the intangibility condition being met (Art. 8 of the Merger Directive).

When an EC company is split-up and transfers its assets and liabilities to one or more Belgian receiving companies, the Belgian companies will normally have a permanent establishment in the Member State of the demerging company. The Member State of the demerging company must treat the demerger in the same way as described above. Belgian shareholders in the EC demerging company will also benefit from the tax deferral regime provided for in Article 45 ITC on the shares received in exchange for their shares in the demerging company.

C. Tax Treatment of Cross-border Demergers Outside the EC

A transfer of assets by a Belgian company to a non-EC country or a split-up of a Belgian company in which one of the receiving companies is a non-EC company cannot be realized in a tax free manner.

A transfer of assets by a Belgian company to a non-EC company will be treated in the same manner as a taxable domestic transfer of assets in the hands of the demerging company (see supra II.B.l.) so that any capital gains realized or recorded on the occasion of the demerger will become taxable at the ordinary corporate tax rate of 40.17%. The non-EC receiving company will, following the transfer of assets, normally end up with a permanent establishment in Belgium, in which case the assets transferred may benefit from a stepped-up basis in the hands of the Belgian establishment.

A cross-border split-up outside the EC will be treated in the same manner as any taxable domestic split-up in the hands of the demerging company (see supra II.B.2.), the Belgian receiving company, if any, or the Belgian permanent establishment of the foreign receiving company (see supra II.C.) and the Belgian shareholders of the demerging company (see supra II.D.2.a.).

D. Transfer Taxes in Case of Cross-border Demergers

The capital increase of a Belgian receiving company as a result of a transfer of assets by or a split-up of an EC demerging company is exempt from the 0.5% capital tax provided that there is no cash payment in excess of 10% (Art. 117 of the Code on Registration Duties). If the demerging company is not an EC company, the capital tax of 0.5% will be due.

A transfer of assets by or a split-up of a Belgian company in which one of the receiving companies is a resident of another country will be exempt from Belgian VAT since the foreign receiving company will normally become a VAT taxpayer as a result of the transaction (Art. 11 of the VAT Code).

Résumé

En Belgique, une scission s’effectue normalement par un transfert d’actifs ou par division (split-up); les scissions sont rarement opérées par séparation (split-off) ou par intégration (spin-off). La Belgique a récemment introduit des dispositions spécifiques sur les scissions par division dans la législation sur les sociétés pour l’application de la sixième Directive de la CE (fondée sur le concept de succession universelle), et des propositions sur l’introduction de règles régissant les transferts d’actifs sont à l’étude.

La Belgique possède une législation fiscale spécifique pour procéder à des scissions exemptes d’impôts dans une situation purement interne. Les conditions requises pour le dégrèvement fiscal sont essentiellement de deux types: en premier lieu, des conditions de groupe ont trait à la nature de la transaction; en second lieu, la scission doit répondre aux besoins légitimes de caractère financier ou économique. Le régime du dégrèvement fiscal pour un transfert d’actifs est optionnel, alors qu’il est impératif pour une scission par division si les conditions requises pour un dégrèvement fiscal sont remplies. Si la société cédante et/ou les sociétés cessionnaires sont en déficit, la société cédante peut avoir intérêt à re-

noncer au dégrèvement fiscal ou à ne pas remplir les conditions requises pour un tel dégrèvement.

Le régime de dégrèvement fiscal applicable aux scissions internes concorde sensiblement avec les règles prévues par la Directive de la CE sur les fusions. Dans un transfert d'actifs, la société cédante est temporairement exemptée de l'impôt sur les gains en capital réalisés à la date de la scission, alors que, lors d'une scission par division, la société cédante est définitivement exemptée de l'impôt sur ces gains en capital et sur les gains résultant de la liquidation, bien que, dans certaines circonstances, elle puisse devenir imposable sur ses gains exonérés d'impôts. D'un autre côté, les sociétés cessionnaires doivent utiliser la méthode du report pour les actifs transférés et peuvent reprendre les caractères fiscaux de la société cédante sauf pour ce qui concerne ses pertes, qui ne peuvent être reportées que dans certaines limites lors d'une scission par division exempte d'impôts. Les pertes fiscales des sociétés cessionnaires peuvent également être réduites à la suite d'une scission exempte d'impôts. Les gains en capital réalisés par les actionnaires belges de la société cédante en cas de division ou par la société cédante elle-même en cas de transfert d'actifs sont normalement exempts d'impôts tant à la date de la scission qu'à la date de la cession ultérieure des actions reçues.

La législation belge sur les sociétés prévoit la possibilité d'un transfert d'actifs transfrontalier alors qu'une scission par division transfrontalière sans liquidation de la société cédante n'est pas possible à l'heure actuelle. Une telle scission devrait nécessairement passer par une liquidation de la société cédante.

La Belgique n'a que partiellement appliqué la Directive sur la fusion qui, selon nous, a un effet direct depuis le 1 er janvier 1992. Une société belge peut procéder à un transfert d'actifs transfrontalier à l'intérieur de la CE sans payer d'impôts, à condition que l'actif et le passif fassent partie d'un établissement stable de la société cessionnaire en Belgique. D'un autre côté, une scission par division transfrontalière exempte d'impôts d'une société belge à l'intérieur de la CE n'est pas possible à l'heure actuelle et la division serait imposée au même titre qu'une liquidation, à moins que l'effet direct de la Directive sur la fusion ne soit accepté.

Zusammenfassung

Eine Spaltung von Gesellschaften wird in Belgien in der Regel durch eine übertragung der Wirtschaftsgüter oder einen split-up erreicht; eine Spaltung mittels eines split-off oder spin-off kommt nur selten vor. Vor kurzem wurden in Belgien im Rahmen der Umsetzung der Sechsten EG-Richtlinie (deren Grundgedanke die Gesamtrechtsnachfolge ist) spezielle gesellschaftsrechtliche Regelungen über split-ups eingeführt. Ein Entwurf gesellschaftsrechtlicher Regelungen über die Übertragung von Wirtschaftsgütern liegt vor.

Das belgische Steuerrecht enthält spezielle Bestimmungen, die bei einer rein inländischen Spaltung steuerliche Neutralität gewährleisten. Die Voraussetzungen für diese steuerliche Vergünstigung sind im wesentlichen zweierlei: die eine ist konzernrechtlicher Art und bezieht sich auf das Wesen der alle Voraussetzungen erfüllenden Transaktion; nach der zweiten müssen der Spaltung Gründe finanzieller oder wirtschaftlicher Natur zugrundeliegen, die eine solche Transaktion rechtfertigen können. Die steuerliche Begünstigung einer übertragung von Wirtschaftsgütern steht dem betroffenen wahlweise offen, während es sich im Fall des split-up um zwingendes Recht handelt, wenn die Voraussetzungen der steuerlichen Vergünstigung gegeben sind. Machen die sich spaltende Gesellschaft und/oder die

aufnehmenden Gesellschaften Verluste, so kann die sich spaltende Gesellschaft ein Interesse daran haben, auf die Steuervergünstigung zu verzichten oder deren Voraussetzungen nicht zu erfüllen.

Die steuerliche Behandlung inländischer Spaltungen entspricht im wesentlichen den Regelungen der EG-Fusionsrichtlinie. Überträgt die sich spaltende Gesellschaft Wirtschaftsgüter, so sind die zum Zeitpunkt der Spaltung aufgedeckten stillen Reserven nicht sofort steuerpflichtig. Im Fall eines split-up sind solche Gewinne und Liquidationserlöse sogar entgültig steuerbefreit; allerdings unterliegen under bestimmten Voraussetzungen die bisher steuerfreien thesaurierten Gewinne der Besteuerung. Auf der anderen Seite müssen die aufnehmenden Gesellschaften die Werte der übertragenen Wirtschaftsgüter fortführen und können die steuerlichen Merkmale der sich spaltenden Gesellschaft beibehalten. Das gilt allerdings nicht für deren Verluste, diese können nur unter bestimmten Bedingungen im Fall eines steuerneutralen split-up übertragen werden. Auch die steuerlichen Verluste der aufnehmenden Gesellschaften können sich als Folge einer steuerneutralen Spaltung verringern. Die Veräusserungsgewinne der belgischen Anteilseigner der sich spaltenden Gesellschaft im Fall eines split-up oder diejenigen der sich spaltenden Gesellschaft selber im Fall der Übertragung von Wirtschaftsgütern sind grundsatzlich zum Zeitpunkt der Spaltung und der nachfolgenden Verfügung über die erhaltenen Gesellschaftsanteile steuerbefreit.

Eine grenzüberschreitende übertragung von Wirtschaftsgütern ist nach belgischem Gesellschaftsrecht zulässig, während ein grenzüberschreitender split-up ohne Liquidation der sich spaltenden Gesellschaft derzeit noch nicht möglich ist. Ein solcher split-up muss dementsprechend mit der Liquidation der sich spaltenden Gesellschaft verbunden sein.

Belgien hat die Fusionsrichtlinie nur teilweise in innerstaatliches Recht umgesetzt. Sie gilt aber nach unserer Auffassung seit dem 1. Januar 1992 unmittelbar. Eine grenzüberschreitende übertragung von Wirtschaftsgütern durch eine belgische Gesellschaft kann innerhalb der EG steuerneutral durchgeführt werden, wenn die Wirtschaftsgüter und Verbindlichkeiten Teil einer Betriebstätte der aufnehmenden belgischen Gesellschaft werden. Andererseits ist ein steuerneutraler grenzüberschreitende split-up durch eine belgische Gesellschaft innerhalb der EG noch nicht möglich. Das bedeutet, dass der split-up zu steuerpflichtigen Liquidationserlösen führt, wenn man nicht die unmittelbare Wirkung der Fusionsrichtlinie anerkennt.

Resumen

Normalmente, la escisión se lleva a cabo en Bélgica median te transmisión de activos o división (split-up); raramente por separación (split-off) o por integración (spin-off). Se han introducido recientemente disposiciones especificas sobre escisiones por división en la legislación societaria, en aplicación de la Directriz de la CE (basada en el concepto de sucesión universal), y están en estudio propuestas sobre introducción de normas que rijan las transmisiones de activos.

Bélgica goza de una legislación específica tributaria para escisiones exentas de impuestos en una situación puramente interna. Las condiciones requeridas para la desgravación fiscal son fundamentalmente de dos tipos: en primer lugar, condiciones de grupo que se derivan de la naturaleza de la transacción; en segundo lugar, la escisión debe responder a necesidades legítimas de carácter financiero o económico. El régimen de desgravación fiscal de una transmisión de activos es opcional, siendo imperativo en el caso de una escisión por división si se han cumplido las condiciones requeridas para la desgravación fiscal. Si la so-

ciedad cedente y/o las cesionarias presentan déficit, la cedente puede tener interés en renunciar a la desgravación fiscal o en no cumplir las condiciones requeridas para la misma.

El régimen de desgravación fiscal aplicable a las escisiones internas es concordante en gran medida con las normas previstas por la Directriz CE sobre fusiones. La sociedad cedente queda, en una transmisión de activos, temporalmente exenta de impuestos sobre las plusvalías de capital afloradas en el momento de la escisión, en tanto que, en una escisión por división, queda definitivamente exenta de dicho Impuesto y del Impuesto sobre los beneficios resultantes de la liquidación; aunque, en determinadas circunstancias, pueda resultar gravada sobre los beneficios exentos de impuestos. Por otra parte, las sociedades cesionarias han de utilizar el método del aplazamiento para los activos transmitidos y pueden recuperar las características fiscales de la cedente excepto en lo que se refiere a sus péridas, que en una escisión por división exenta de impuestos únicamente pueden ser aplazadas hasta cierto límite. Las pérdidas fiscales de las sociedades cesionarias pueden también ser reducidas tras una escisión exenta de impuestos. Las plusvalías en capital realizadas por los accionistas belgas de la sociedad cedente en caso de división, o por la propia sociedad cedente en caso de transmisión de activos, quedan normalmen te exentas de impuestos tanto en el momento de la escisión como en el de la posterior cesión de las acciones recibidas.

La legislación societaria belga prevé la posibilidad de transmisión internacional de activos. Actualmente no cabe una escisión por división internacional sin liquidación de la sociedad cedente. Tal escisión tiene que pasar necesariamente por la liquidación de la sociedad cedente.