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Belgium: A tax haven?

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Belgium, which is both multicultural and multilingual, is undoubtedly one of the most attractive European countries to consider for establishing a company.

Next to its pleasant lifestyle with its rich cultural and historical heritage, the country offers an attractive business environment with political and economic stability. Belgium is well known as The Capital of Europe and is often called the Essence of Europe, due to its distinctive character and for being an important meeting point in Western Europe. This means that Belgium is an internationally oriented country, with legislation and regulations that are based upon this principle in many areas.

Belgium is one of the 15 countries that form the Schengen area. If you have a residence permit for Belgium, you may apply for a Schengen Visa. This visa enables you to travel to all other Schengen countries without individual visa for each of the country.

Surprisingly, Belgium is not well known worldwide as an attractive country to establish a company. The same applies to its Holding Company or Financing Company structures.

This is probably due to the fact that Belgium always ranks at the top of the list of the Organisation for Economic Cooperation and Development (OECD) for its high individual and corporate tax rates.

However, there are other factors that are more important than rates.

Instead of focusing on the tax rates one should rather focus on the several tax incentives and tax treaties Belgium has concluded. As a result of these incentives and treaties, the effective rate will be much lower and could be even zero when carefully planned.

Based upon this legislation, Belgium is an interesting place to live in and undoubtedly a sound choice to establish a company, however paradoxical it may seem.

Interesting factors to consider

Notional Interest Deduction, fictitious deduction on equity

As of January 1, 2006, Belgium grants a new tax incentive to companies: the interest deduction for risk capital, better known as the Notional Interest Deduction (NID). The NID allows Belgian companies and foreign companies with a Belgian taxable branch to deduct a fictitious interest from their tax base.

The deduction is calculated on the basis of a fictitious interest on the adjusted equity capital. This adjusted equity capital includes share capital, retained earnings, surpluses on revaluation, capital subsidies and share premiums.

The NID rate is based upon the annual average interest rate for the 10-year Belgian Government bonds. The basic rate for the tax year 2008 is 3.781 percent (tax year 2008 means calendar year 2007). If a company qualifies as small, it will be entitled to an additional deduction of 0.5 percent.

A company qualifies as small if the following conditions are fulfilled:

- Company's turnover does not exceed €50 million;
- Company's balance sheet total is not higher than €43 million;
- The company has less than 250 employees.

In effect, a Holding Company will be entitled to a deduction of almost 4 percent on the equity of the company.

To promote capital equity-financing, the Belgian government has abolished the 0.5 percent registration duty on capital contributions.

The NID complies with existing E.U. law and thus offers companies certainty.

Patent income tax rate 6.8 percent

Belgium has recently decided to implement a favourable regime in respect of patent income, applicable to income derived from the licensing of patents or the use of patented products. This patent income deduction (PID) reduces the tax burden on the net income to 6.8 percent instead of the normal corporate income rate of 33.99 percent.

The Belgian ruling system

As of 2003, it is possible to consult the tax authorities in order to obtain an early decision in particular situations. As a result, it is possible to obtain 100 percent certainty about the tax burden before actually restructuring the company. This offers advantages especially to multinationals and is therefore worth considering.

Belgian participation exemption

In principle, there is a 95 percent participation exemption for dividends received provided that certain conditions are met. One of these conditions is that the dividends should be paid by a company that is subject to a normal tax regime. In principle, this is the case if a company is taxed at a rate of at least 15 percent. When a company is situated within the European Union the tax rate is not relevant. The shares in the distributing company must be held for one year at least and the quantity of shares in the subsidiary should not be less than 10 percent.

Capital gains on shares are tax exempt

Capital gains on shares are 100 percent exempt except for fixed income securities. This is without a reinvestment condition or any other condition. The condition relating to the participation threshold as mentioned above is not applicable to capital gains. This allows a Belgian Company to hold a portfolio under favourable conditions. When carefully planned, a very low taxation can be achieved.

Belgian-Hong Kong tax treaty, the gateway to Asia

Belgium has closed a very beneficial treaty with Hong Kong. While using this treaty E.U. entrepreneurs and even U.S. entrepreneurs (in cases where the new U.S.-Belgian treaty is effective) active in China and Hong Kong can transfer their profits in a very beneficial way to Belgium while Asian investors in Europe can transfer their profits tax free, without any withholding tax to Asia or Hong Kong.

How does it work?

When doing business in China one can set up a company in Hong Kong. This company is liable to a tax rate of 17.5 percent. However, this tax rate is only applicable to profits arising from a trade, profession or business which has taken place in Hong Kong only. So when doing business in China, the taxpayer is not doing business in Hong Kong and therefore, there will be no taxation in Hong Kong.

In the case where a Belgian Holding Company holds the shares of the Hong Kong Company, the dividends distributed to the Belgian Holding Company will be exempted based upon the Belgian participation exemption. The Belgian authorities have stated that the participation exemption is applicable even if the Hong Kong Company is not actually taxed but only liable to a tax rate of 17.5 percent.

Furthermore, Hong Kong does not impose a withholding tax on dividends distributed to Belgium.

Similarly, Chinese companies investing in Europe can also use a Belgian Holding Company. If a Belgian Holding is placed between a European Company and a Hong Kong Holding Company, European profits can be transferred to Hong Kong almost tax-free.

The Belgian Holding Company will receive dividends under the conditions of the Belgian participation exemption. This Belgian Holding Company can distribute the dividends received from its European subsidiaries to the Hong Kong Holding without any withholding tax.

No withholding tax for dividends derived from Belgian companies

Belgium has a very large tax treaty network, having concluded tax treaties with more than 70 countries. In principal, all treaties are according to the OECD Model. For international tax planning opportunities it has to be stressed that Belgium even has a treaty with the United Arabian Emirates; Dubai is one of those countries.

Presently, some treaties have already been signed but are not yet effective. Amongst them are the new treaties with the United States and with the Seychelles.

Based on European legislation, Belgium has exempted the withholding tax for countries with which Belgium has concluded tax treaties.

There are some conditions which have to be met by the corporate shareholder. The shareholder has to be resident in a treaty country and must hold at least 15 percent of the shares in the Belgian subsidiary. The shares must also be held for at least 12 months.

Thus, a corporate structure having a Dubai Company as a Holding Company and a Belgian company for financing purposes is an example of a tax effective structure.

New tax treaty between Belgium and the United States

The treaty with the United States has been signed but has not taken effect yet. However, it is expected to become effective this year.

This treaty appears to be very beneficial since under certain conditions, no withholding tax is levied on dividends, royalties and interest between a Belgian Holding and a United States subsidiary as well as between a U.S. Holding and a Belgian subsidiary. It appears to be very promising. Combined with the very beneficial treaty between Belgium and Hong Kong, Belgium could be America's gateway to Asia. Dividends can be distributed without any withholding tax from Hong Kong *via* Belgium to the United States and *vice versa*.

Individual Taxes

In terms of taxes, Belgium is a very interesting country to consider, not only for companies but also for individuals.

There is no capital gains tax on the sale of shares. Moreover, there is no taxation on the capital gains on the sale of shares in a fully owned company.

Interest is taxed at a final rate of 15 percent. Dividends are taxed at a rate of 25 percent. There are insurance products that are not taxable, it is possible not to pay inheritance or gift tax, and there is no wealth tax.

For expatriate employees who are part of an international group, there is a specific taxation regime. This regime applies to employees with temporary contracts at the Belgian company. They have to be recruited directly from abroad or seconded by an international group company and may be directors or specialists. These employees will be regarded as non-resident taxpayers in Belgium, which means that the employee will only be taxed for work actually done within the Belgian territory.

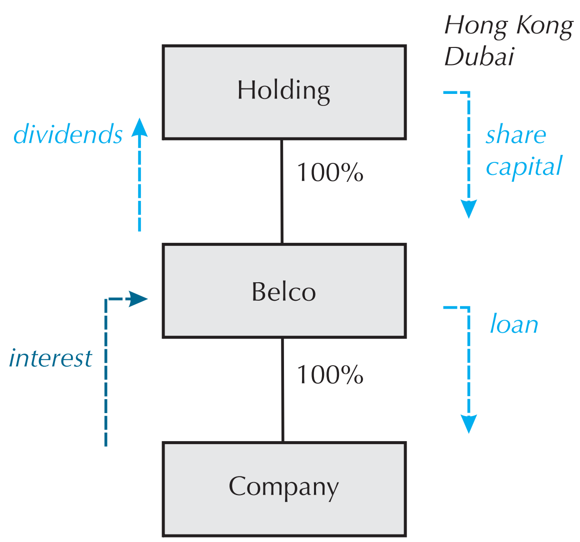
For instance, in the case where the employee works 20 percent outside of Belgium, only 80 percent of his income will be taxed. The income related to his foreign activities will be calculated on the basis of the working days spent outside Belgium. Furthermore, the employer may grant the employee an expense allowance of €30,000 at most.

How the Belgian company works

For international companies, a Belgian branch can play an important part in reducing the overall tax burden.

The use of the NID together with the treaty network and the zero withholding tax makes Belgium a particularly choice.

Structure



In a situation in which a Holding Company located in a low tax jurisdiction like Hong Kong or Dubai wants to finance activities in Europe, a withholding tax could apply according to the country of interest. Furthermore, tax regulations could apply under which interest paid to low tax countries is not deductible. A Belgian Holding may be a solution in this case.

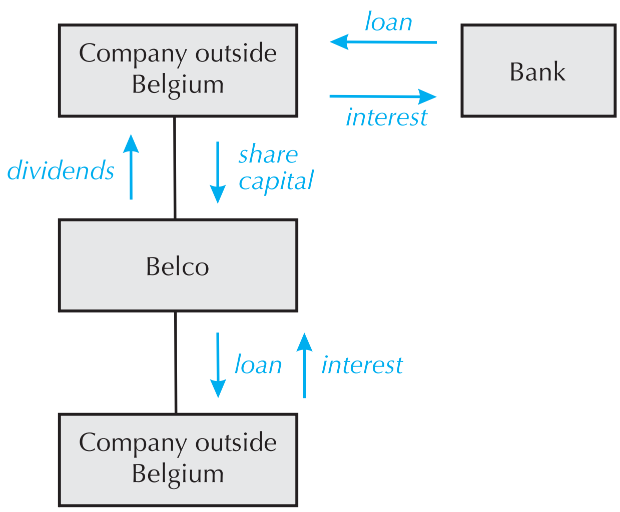
For example, the Holding Company (Dubai or Hong Kong) contributes €30 million to the share capital of the Belgian Company named Belco. Belco lends this money to another group company situated somewhere in Europe at an interest rate of 4.5 percent. The interest will be deductible according to the tax regulations in the country of the payer, resulting, in this case, in a deductible amount of €1,350,000.

The interest received will be added to the result of Belco. However, the NID, in this case calculated at €1.2 million can be deducted for tax purposes from the tax base. Thus, €150,000 will be the tax base in Belgium at a rate of almost 34 percent. This means that the tax burden in Belgium could be €51,000. Of course, there will be operational costs in Belgium that also may be deducted, so the actual tax burden will be even lower.

The effective tax rate in this example is less than 4 percent while the profit of €1,299,000, can be distributed tax-free to the Holding Company.

If a Holding Company is situated in any other country, the Belgian company can act as a financing company in which the portfolio may be held or loans to other companies may be granted.

The structure can be outlined as follows:



The Holding Company can contribute to the shares of Belco. As mentioned, there is no capital tax. Belco can lend out the monies to other companies. The profit from Belco can be distributed tax-free to companies situated in other (treaty) countries. In the case where no loans are granted to other companies, Belco can also keep the portfolio investment in a tax-friendly manner.

There is no taxation on capital gains on shares in the company.

If, for example, a relative company in an international group wants to invest and this investment must be financed by another group company or bank, establishing a Belgium company may create some tax advantages.

Within the group, a company may get a bank loan. Interest on this loan could be deductible in the country in which this company is situated. This company in turn deposits the monies derived from the bank in the share capital of a Belgian company. In Belgium, the NID deduction will be applicable. The Belgian company shall grant a loan to the company in which the investments should take place.

See Diagram below

In this example a double dip, two times deduction within the group, can be reached. However, one should always check whether or not tax deduction in the countries outside Belgium will be granted based upon the respective legislation.

In the case of an acquisition of patents, Belgium offers a tax incentive. Most of the income derived from patents is tax free. It is possible to combine the NID with this royalty exemption. One can combine the above-mentioned way of financing the acquisition of the patent with the NID.

In the case of an acquisition of patents as described above, a group company deposits share capital in a Belgian company.

This Belgian company in turn will acquire the patent with the monies acquired. Because of the NID, almost 4 percent of the equity can be deducted. Furthermore, 80 percent of the royalty income is tax free. When the group company that has deposited the share capital in the Belgian company attracts this deposited share capital from a bank, the tax situation will even be more favourable if the interest in the country of this group company is deductible. The tax deduction of the group company, NID deduction of the Belgian company and 80 percent tax exemption on royalty income in Belgium can be achieved in such a case.

For mergers and acquisitions, using a Belgian company may also be highly tax-effective when capital increases. As mentioned, the NID is based upon the equity of the company.

Thus when equity increases tax deduction increases too.

The private holding

For private shareholders of the holding company there are possibilities to be seconded to the Belgian company. In these situations, possibilities such as split-employment may be beneficial.

An individual who actually resides in Belgium has the possibility of transferring his equity tax-free. Please be aware of the fact that there is no capital gains tax on the sale of shares of the Holding Company.

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Belgian residence and citizenship

Based upon the current legislation there are several possibilities for individuals investing in Belgium to apply for a resident permit and even Belgian citizenship after three years. A Belgian residence permit allows visa-free travel to all Schengen countries. These opportunities will certainly exist when investing in Belgium through a company.

I shall, however, not describe this in detail in this article.

Conclusion

Belgium is a country with high tax rates. However, it seems to have a tax system which is very internationally orientated and very friendly to companies and individuals from abroad. In combination with other jurisdictions, a very tax-effective structure can be built. Furthermore, besides the tax incentives, Belgium can be hostile to individuals who reside and later apply for citizenship. Being a Belgian resident also offers many tax benefits to individuals.

Perhaps at first Belgium appears to be an expensive country due to high tax rates, but when all its tax opportunities are taken into consideration it can indeed prove to be a tax haven for individuals and companies.

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