2018 BELGIAN TAX REFORM: A FIRST REVIEW OF THE KEY NEW PROPOSALS

The Belgian federal government has reached an agreement on the 2018-2020 tax reform package. Below we have made a first review of the most important new proposals. These political decisions now need to be further refined and enacted. It is expected that a first batch of legal texts will be voted on by the end of this year.

Most important proposals

- Reduction of corporate income tax rates
- Increased limitations on the use of tax losses carried forward and other tax deductions
- Stricter conditions for the tax exemption for capital gains on shares
- Withholding tax on capital decreases
- Introduction of tax consolidation
- VAT option for standard letting agreements

Gradual decrease of corporate income tax rate

The standard corporate income tax rate will decrease from 33% to 29% as from 2018, and from 29% to 25% by 2020.

The reduced progressive corporate income tax rate applicable to SMEs will decrease, as from 2018, from 24.98% on the first €25,000 of profits to 20% on the first €100,000 of profits. However, one of the conditions to benefit from this regime will also be changed, i.e. the minimum director salary of €36,000 to be paid out per year will be increased to €45,000 (with a possible exception for start-ups).

Additionally, the government announced the reduction of the supplementary 'crisis' tax of 3%, which is calculated on the basic corporate income tax rate (e.g. 3% crisis tax on 33% CIT = total Belgian CIT rate of 33.99%), to 2% by 2018, and intends to completely abolish this crisis tax by 2020.

There has been no specific communication as to a decrease of the exit tax rate. This is applicable to certain real estate transactions involving Belgian REITs and has always been set at 50% of the standard applicable corporate income tax rate. However, it is expected that this rate will also be decreased.

Minimum corporate income tax

The government proposes to introduce a minimum tax for large companies by limiting their use of tax losses and other tax deductions on annual profits exceeding €1 million.

Under the proposed measure, the annual profits above €1 million can only be offset with tax losses carried forward, dividend received deductions and notional interest deductions up to 70%. The remaining 30% would therefore constitute a "minimum taxable basis".

Tax losses and dividend received deductions carried forward which cannot be used are not lost, but instead are reported to subsequent taxable years, resulting in an effective spreading in time of the tax benefits,and hence a reduction of the net present value of these tax benefits.

When budgeting the effective tax cost of a company, or when allocating value to existing tax losses in the context of a company takeover, these new limitations need to be factored in.

Capital gains on shares

The current 0.412% capital gains taxation on gains realised upon the disposal of shares held for a minimum duration of 1 year will be abolished by 2018.

On the other hand, it is envisaged to introduce minimum participation conditions in order to benefit from the tax exemption on share capital gains which will be identical to the participation condition applicable in order to benefit from the participation exemption on dividends (*i.e.* a minimum shareholding of 10% or with an acquisition value of at least €2.5 million).

As a result, Belgian companies holding shares which do not meet these minimum participation requirements will become fully taxable at the ordinary applicable corporate income tax rate, *i.e.* 29% or 25% on the capital gains realized on these shares,whereas today they would generally only be taxable at 0.412% or even 0%.

As a result, the introduction of these minimum participation thresholds may lead to a substantial increase of the tax burden for smaller portfolio companies, carried interest structures and other management participation schemes structured through a personal management company.

Withholding tax on capital decreases

Under Belgian law, and unlike in some neighboring countries, it is at present still possible to structure distributions to shareholders by way of a share capital reduction (not subject to withholding tax), even if the company has sufficient reserves to distribute a dividend (subject to withholding tax). A share capital reduction can be beneficial, especially for investors not benefitting from a withholding tax exemption (for example individuals, investment funds, etc).

The government now plans to introduce a certain level of withholding tax on capital decreases in situations where the company has available reserves. As a reminder, the current level of withholding tax on the distribution of dividends is 30% (subject to a number of exemptions and reductions).

Notional interest deduction

At present the notional interest deduction is calculated on the total amount of qualifying equity. The government now proposes to apply the notional interest deduction only on the average amount of the incremental equity increase over a 5 year period.

The elevated deductibility rate for SMEs will be maintained.

Tax consolidation

The government announced the introduction of a system of tax consolidation in Belgium as from 2020 in order to enhance tax neutrality within international groups.

This long-awaited measure will allow groups to use their tax losses and possibly other tax deductions across the different Belgian group companies. Tax consolidation may simplify post-acquisition tax integration to the extent that interest expenses on the acquisition loans can be offset against operational income of the target, and may therefore make the use of Belgian acquisition vehicles attractive once again.

Tax on stock exchange transactions

The stock exchange transaction tax rates will be increased from 0.27% to 0.35% on the sale and purchase of shares, and from 0.09% to 0.12% on the sale and purchase of debt securities. The tax rate applied to transactions in funds will not be modified, nor will the maximal taxation amounts applicable under the current tax regime.

Furthermore it is envisaged to make the stock exchange transaction tax applicable to legal constructions falling under the so-called 'Cayman-tax regime'.

Optional VAT on real estate letting

Under the currently applicable Belgian VAT rules, subject to certain specific exceptions, the standard letting of real estate is not subject to Belgian VAT. As a result, real estate investors cannot generally recover input VAT on construction or renovation costs.

The government has now announced that it is looking to introduce an optional regime to submit standard letting agreements to VAT, thereby allowing input VAT recovery for real estate investors. This measure is comparable to what already exists in most other EU jurisdictions and has been long awaited by the real estate sector. The exact details of the optional VAT regime remain to be announced and it will be interesting to learn what the impact will be for existing agreements, as well as the impact of the VAT option on the tax treatment upon a sale of the asset.

Tax on securities accounts

Individuals holding a securities account (holding assets including e.g. stocks, bonds, funds etc., but not pension savings or life insurance products) with a total value exceeding €500.000 will be taxed on the entire amount of the securities held on such an account at a tax rate of 0.15%

Other tax measures announced

The government announced a wide variety of other changes to the Belgian tax regime, the details of which still need to be clarified. Some notable changes are:

- A further extension of the scope of the so-called 'Cayman-tax' regime to include, among others, trusts, Luxembourg *fonds dédies* and intermediary entities, which will improve the efficiency of the current regime.
- An extension of the scope of the tax shelter for start-ups to include certain growth companies.
- The introduction of a withholding tax exemption on the first €627 of income from equity instruments (dividends) received by private individuals. As

compensation, interest on savings accounts will now only be exempt up to €940 instead of the previous €1,880.

- A temporary increase of the investment deduction from 8% to 20% for certain SMEs.
- An extension of the scope of the current 15% reduced withholding tax rate for certain investors in certain social real estate projects to include investments in other types of real estate.
- The implementation of the European ATAD (I and II) rules. This means the introduction of CFC legislation, exit taxation upon the transfer abroad of certain assets, and special provisions in order to avoid hybrid mismatches and tax residency mismatches. Moreover, this entails the implementation of a limitation of interest deductibility to 30% of the EBITDA, although there will be a minimal interest deductibility of €3 million, a grandfathering clause for loans entered into before 17 June 2016, and a carry forward of "unused" interest expenses.
- A limitation on the deductibility in Belgium of foreign losses accrued by foreign branches of Belgian companies. These losses will only remain deductible in Belgium if the losses cannot be used to be offset the profits of the Belgian branch abroad.

What's next?

At this stage, the government has only announced general guidelines which they stressed might take some time to implement. The proposals will now have to be technically addressed and drafted in the form of sound legislative proposals and voted on by Parliament. Given the fact that the government indicated that some of the proposals would be implemented as soon as 2018, and given the upcoming elections in 2018 (municipal) and 2019 (regional and federal), we assume that the government will want to hold a vote on at least part of the proposed measures before the end of this year.

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