Mergers & Acquisitions

The Belgian perspective[1]

Isabel Denduyver and René Rabaey

STATEMENT OF PURPOSE

Transactions such as a merger, division, transfer of assets or exchange of shares often have an international dimension. If so, these reorganizations cause one of the countries to lose a taxable entity. As a result, the state that has to watch one of its residents leave will be prone to charge some sort of 'exit'-tax, especially upon value built but never taxed within its territory. These taxes can be justified, but only insofar capital gains are actually cashed in. Whenever on the contrary, the transaction is a mere transfer of ownership without any material change nor any distribution of capital gain, the source state remains entitled to taxation on behalf of the company that has been transferred. Exit-taxation therefore should be prohibited in the latter situations. Otherwise, international cooperation and integrations of companies would be impeded.

It took more than twenty years before the European Council was able to enact the Directive 90/434/EEG of July 23rd 1990 concerning the fiscal regulation of mergers, divisions, transfer of assets and exchange of shares regarding companies from different member states. It provides for a system of deferral of taxation – not cancellation – for the state of the acquired company, in order to solve the issue as aforesaid. However, the Directive does not provide an answer to all problems.

Tax regulation should continuously be harmonized all over Europe, principles as well as percentages. The preservation of different kinds of country-specific measures is harmful for the free movement of investment capital. These individual regimes must be modified because they jeopardize the initiatives taken by various European Directives.

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1. INTRODUCTION

1. The fiscal treatment of mergers & acquisitions is a hot topic in Belgium. In 1998, direct foreign investment from and towards Belgium has grown spectacularly. Incoming investments have increased from 2.5 billion euros in 1998 to 14,85 billion euros in 2000. Outgoing investments have risen from 1.7 billion euros in 1998 to 11.95 euros in 2000.[2]

In the year 2002 however, the total value of worldwide mergers and acquisitions has plunged with 47% in comparison with the year 2001.[3] The setback was extremely intense and according to Peter Lauwers of KPMG Corporate Finance there are no indications that the M&A market has already reached its all-time low. On average, M&A activity in Belgium declined less than elsewhere in the world. Therefore, Belgium was just a net seller on the world market. Furthermore, the transaction value of the average Belgian deed of sale is much lower than that of the average acquisition file.

2. A uniform, European legislation is important for Belgium. After all, the major part of the Belgian outgoing direct investments goes to its four neighbour countries[4].[5] The rest of it is mainly meant for Europe. Belgium has also invested a lot in the Visegrad-countries[6]. These countries have now been admitted to become full members of the European Union. Also, most of the incoming direct investments in Belgium originate from its neighbour countries and other EU member states. Belgium seems less attractive for American Investors.[7]

[2] P. VANDENHOVE, “Directe investeringen in het buitenland. De investeringsstroom vanuit en naar Beglië”, *Federaal Planbureau Working Paper* 2001, 19-20.
[3] W. DE PRETER, “Overnamehonger bedrijfsleven gehalveerd”, De Standaard, 1, 2002 according to KPMG Corporate Finance, data from Dealogic.
[4] France, the Netherlands, Germany and Luxemburg
[5] P. VANDENHOVE, “Directe investeringen in het buitenland. De investeringsstroom vanuit en naar Beglië”, *Federaal Planbureau Working Paper* 2001, 41-42.
[6] Poland, the Czech Republic, Hungary
[7] For this reason, Belgian government has recently launched an international advertising campaign, to attract non-European investors.

2. IMPLEMENTATION OF THE DIRECTIVE

3. Thus far, Belgium has only partially implemented the European Merger Directive[8] of 1990. The subject matters of 'transfer of assets' and 'exchange of shares' have already been implemented.[9] As far as 'mergers and divisions' is concerned, the Directive has still not been carried out.[10]

4. According to former Belgian legislation, a merger, division or equivalently treated transaction between two or more companies always brought about the liquidation of the transferring company. The winding-up of the transferring company gave rise to a special liquidation-tax. For this reason, tax-free mergers were almost impossible in practice. The notions 'merger' and 'division' have been introduced in Belgium by the law of the 29th of June 1993.[11] This Belgian law has thus converted the third and sixth EG Directive[12], concerning domestic mergers and divisions respectively, into national legislation. The law in question allows mergers and divisions of domestic companies to take place without the liquidation of the acquired company. In addition, the law of 6 August 1993 adjusted the Belgian Income Tax Code to the new corporate notions.[13] Because mergers of Belgian companies nowadays result in 'liquidation without settlement' of the acquired company, these transactions can be exempted from taxation if they fulfil the necessary conditions attached to the exemption rules.[14] The Belgian legislator has however refused to introduce the exemption method for cross-border mergers as set down in the merger Directive.[15]

5. A rationale why Belgian law has not yet recognised the legal concept of cross-border mergers was the existing inconsistency of this notion with the Belgian Company Code. Until recently, Belgian companies could not lawfully finalize their acquisition by a foreign company because 'nationality' was

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[8] Directive of the Council 90/434/EEC, 23 July 1990 regarding fiscal treatment of mergers, divisions, transfer of assets and exchange of shares, concerning companies of different member states., P.B. Nr. L225 of 20/08/1990, 0001-0005 (hereinafter quoted as European Merger Directive).

[9] Laws of October 23rd, 1992 and July 28th, 1992.

[10] C. AMAND, M. DE MUYNCK, G. DE NEEF, *Overdracht van ondernemingen*, Larcier, 1999, 317; L. A. DENYS, *Liber Amicorum Paul de Vroede; Over de opheffing van de fiscale barrières voor grensoverschrijdende reorganisaties: de Europese fiscale fusierichtlijn*, Antwerpen, Kluwer Rechtswetenschappen, 1994, 539.

[11] TH. BLOCKEYRE & J.P. LYCOPS, *Reorganisatie van Belgische naamloze vennootschappen. Juridische, boekhoudkundige en fiscale aspecten.*, Diegem, ced.samsom, 1994, 143.

[12] Directive of the Council nr. 78/855, 20 oktober 1978, P.B. nr. L. 295, 36.
Directive of the Council nr. 82/891, 31 december 1982, P.B. nr. L. 378, 47.

[13] The Belgian law of August 29th, 1993 is not a full implementation of the Merger Directive [see I. TITECA, *Boekhoudkundige verwerking en fiscaal regime van fusies*, Leuven, kuleuven, 1996, 34.].

[14] Article 210, § 1, Belgian Income Tax Code (hereinafter quoted as BITC).

[15] S. EMMERECHTS, "De grensoverschrijdende fusie onder de loep: vennootschapsrechtelijk en fiscaalrechtelijk", *V&F* 2000, 212.

considered to be one of the essential elements of a company that could not be altered by a change of the statutes (except with unanimity of the shareholders). The acquisition of a foreign company by a Belgian one was already possible, but only insofar the national laws of the acquired company did not offer resistance.

The nationality of a company determines which legal system is appropriate for its establishment, functioning and liquidation. Nationality itself is determined by the law of the country according to which the company is established (the incorporation theory) or by the law of the country where the company has its actual seat of business. In Belgium the effective seat theory is being used, which implies that a company has the Belgian nationality whenever that company has its place of management in Belgium. If a foreign company takes over a Belgian one, the nationality of the acquired -formerly Belgian- company changes. The provisions about nationality in Belgian company law impeded however this cross-border transaction.[16] Basically, the cross-border acquisition conflicted with the argument that the General Meeting of shareholders could not decide upon a change of nationality except with unanimity.

From the last update of Belgian corporate legislation the concept of nationality constitutes no more hindrance for cross-border transactions. To be more precise, nationality does no longer represent an essential element of a company.[17] This has lead to the proposal of law that provides for the further implementation of the Merger Directive because nationality is no longer a problem.[18]

6. The lack of legal foundation for mergers and divisions in Belgian/European corporate law, as opposed to the existing regulation concerning transfer of assets and exchange of shares, has been the key justification for the partial integration of the Merger Directive into the Belgian Income Tax Code. Consistent with this belief, the Merger Directive is deemed to offer tax solutions for problems which are not yet faced on corporate level. However, the proposal for the tenth EG Directive[19] regarding the corporate regulation of cross-border mergers of public limited companies, has reached a dead end. The introduction of the Directive is being impeded by the intrinsic tax issue and the problem of post-merger employee participation.[20] An analogous proposal for divisions has not yet been made.

7. Nonetheless we suppose that within the foreseeable future the Belgian Income Tax Code will enable cross-border mergers and divisions to take place. The possibility from 8th of October 2003 to found a European company (or

[16] B. PEETERS, "De Europese vennootschap: fiscale aspecten", *Fiscoloog Internationaal* 2001, 5.
[17] B. PEETERS, "De Europese vennootschap: fiscale aspecten.", *Fiscoloog Internationaal*,2001, 5.
[18] Parl. St., 2000-2001, Nr. 1517/1.
[19] Bull. EG, 1985, Supplement 3.
[20] G. VAN SOLINGE, *Grensoverschrijdende juridische fusie*., Deventer Kluwer 1994, 14.

Societas Europaea) will facilitate the creation of cross-border mergers given that such companies will be subject to a uniform European company law. The reality of a *Societas Europaea* (SE) will not only provide for a corporate legal foundation for cross-border transactions on community level, but will also put an end to other arguments on the basis of which other member states oppose cross-border transactions. The former nationality problem illustrated above will be inexistent, since the SE will have one European 'nationality'. Other member states (especially Germany, the Netherlands and some Scandinavian countries) always opposed the idea of cross-border mergers because of the problems of employee participation following such transactions. The issue of employee participation has played without doubt an important role in the delay by which the SE regulation came about.[21] This viewpoint was also the most important obstacle impeding the realization of the proposed tenth EG Directive.

8. The final justification for Belgium's reluctant attitude towards implementing the Merger Directive was tax xenophobia.[22] The Belgian tax Administration was alarmed by the possible loss of tax revenue. This concern for the loss of taxable substance as a result of the emigration of a national company is however unjustifiable. The Merger Directive determines explicitly that, within the scope of cross-border mergers and divisions, the acquired/divided company maintains a permanent establishment in the member state where it is located. By way of this permanent establishment all assets and liabilities of the acquired/divided company continue to be Belgian taxable substance[23].

3. DEFINITIONS

3. 1. MERGERS & DIVISIONS

9. The description of **domestic mergers and divisions** given in the Belgian Company Code corresponds to the concepts regarding mergers and divisions illustrated in the third and sixth EU Directive. Domestic mergers and divisions have four important implications[24]: (1) the dissolution of the acquired/divided company without going into liquidation, (2) the shareholders of the acquired/divided company become shareholder of the acquiring/receiving company, (3) all assets and liabilities of the acquired/divided company are transferred to the acquiring/receiving company,

[21] F. DORSSEMONT, "Werknemersparticipatie in de Societas Europaea", *Juristenkrant* 2001, 13.
[22] S. EMMERECHTS, "De grensoverschrijdende fusie onder de loep: vennootschapsrechtelijk en fiscaalrechtelijk", *V&F* 2000, 215.
[23] TH. BLOCKERY & J.P. LYCOPS, 'Fusie en splitsing van vennootschappen', *A.F.T.* 1993, 198.
[24] Article 671, Belgian Company Code; Third European Directive of 9 October 1978; J.VAN BAEL, *Fusies en splitsingen*, Kluwer Rechtswetenschappen 1993, 50-57.

and (4) the exclusive compensation with shares, with the exception of a limited cash payment.

Belgian law does however go further, given the fact that domestic mergers and divisions are not restricted to public limited companies (as in the third and sixth EU Directive), but also extend to all companies with legal personality. In addition, the Belgian legislator increased the potential mark-up in cash up to 20% of the nominal value, or in absence of a nominal value, of the accounting par value of those shares.[25]

10. The European Merger Directive covers three types of **cross-border mergers**: (a) the operation of two or more companies by which one acquires all assets and liabilities of the other company, (b) the operation of two or more companies whereby they transfer all their assets and liabilities to a company that they form, (c) merger by acquisition of a 100% subsidiary by its mother company. In all cases the acquired company ceases to exist as a separate legal entity, without liquidation. In exchange the shareholders of the acquired company receive new issued shares of the receiving company, and if applicable, a cash payment that should not exceed 10% of the nominal value, or in absence of a nominal value, of the accounting par value of those shares.[26]

A division is an operation whereby a company, on being dissolved without going into liquidation, transfers all its assets and liabilities to two or more existing or new companies, in exchange for the pro rata issue to its shareholders of securities representing the capital of the companies receiving the assets and liabilities. Whenever relevant, this compensation in shares can be adjoined with a cash payment, not exceeding 10 % of the nominal value or, in the absence of a nominal value, of the accounting par value of those securities.[27]

11. Because cross-border mergers & divisions are still not dealt with in the Belgian Company Code, a comparison with the European Directive definitions is not yet possible. However, whenever such reorganisations will be made possible in Belgian corporate legislation, it is likely that these European definitions will be adopted, since Belgium did follow the third and sixth EU Directive for domestic mergers & divisions.[28] (*cfr. supra* no. 9).

12. With regard to the relationship between the definitions of mergers and divisions in the Belgian Company Code and the Belgian Income Tax Code, conformity can be observed for the domestic reorganisations. In Belgium, tax laws of 6 August 1993 adjusted the Belgian Income Tax Code to the new

[25] J.VAN BAEL, *Fusies en splitsingen*, Kluwer Rechtswetenschappen 1993, 50.
[26] Article 2, a, European Merger Directive.
[27] Article 2, b, European Merger Directive.
[28] C. AMAND, M. DE MUYNCK, G. DE NEEF, *Overdracht van ondernemingen,* Larcier, 1999, 403.

corporate notions of national merger and division[29] (*cfr. supra* no. 4). The primary reform in corporate law was the concept of 'dissolution without liquidation' of a company. The introduction of this concept into Belgian tax law brought about important changes concerning tax exempted mergers and divisions.[30]

A comparison between the corporate and fiscal treatment of cross-border mergers and divisions in Belgium is yet again impossible since the Belgian Company Code does not mention the legal concept of cross-border mergers and divisions.

3. 2. TRANSFER OF ASSETS

13. The transactions in Belgium that correspond to the concepts of 'transfer of a universality of goods' and 'transfer of one or more branches of activity' (a business section or branches of business activities) are classified by the Merger Directive in one single category, called 'transfer of assets'.[31] According to the European Merger Directive a transfer of assets is an operation whereby a company transfers, without being dissolved, all or one or more branches of its activity to another company in exchange for the transfer of shares representing the capital of the company receiving the transfer.[32] Contrary to the provisions with regard to mergers and divisions the European Merger Directive does not provide the possibility to use as consideration for a transfer of assets an additional payment in cash.

14. The Belgian law of 28th July 1992 changed the fiscal treatment of transfer of assets in order to be in accordance with the Merger Directive of 23rd July 1990. Article 46 of the Belgian Income Tax Code was modified, so that the fiscal principle of neutrality applicable to transfers of assets in a Belgian company, would also be applicable to similar transfers in any European company.[33]

15. According to Belgian company and tax law, a business (transfer of all assets and liabilities) can be transferred to one or more existing or new companies. The merger Directive does not mention the option of transfer to more than one or to a newly founded company.[34]

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[29] The Belgian law of August 29th, 1993 is not a full implementation of the Merger Directive [see I. TITECA, *Boekhoudkundige verwerking en fiscaal regime van fusies*, Leuven, Kuleuven, 1996, 34.].
[30] TH. BLOCKEYRE & J.P. LYCOPS, *Reorganisatie van Belgische naamloze vennootschappen. Juridische, boekhoudkundige en fiscale aspecten*, 1994, ced.samsom, 215.
[31] J. COUTURIER, "Inbreng van een algemeenheid of van een bedrijfstak", *A.F.T.,* 1998, 139.
[32] European Merger Directive [art 2 (c)]
[33] TH. BLOCKERYE & J.F. LYCOPS, *Reorganisatie van Belgische naamloze vennootschappen. Juridische, boekhoudkundige en fiscale aspecten*, ced.samsom, 1994, 383.
[34] J. COUTURIER, "Inbreng van een algemeenheid of van een bedrijfstak", *A.F.T.,* 1998, 142.

16. It is important to notice that opposite to a merger or division, in a transfer of assets the company part of which is being transferred, does not disappear but on the contrary, becomes shareholder of the acquiring company. A transfer of assets can be a useful option in a number of cases. A non resident company might consider transferring the activities from her Belgian permanent establishment to one of her Belgian subsidiaries, to enjoy favourable taxation measures. Or, if an operational Belgian company that already has participations in one or more subsidiaries of the group wants to transfer its activities towards these subsidiaries, and become the holding company of the group.[35]

3. 3. EXCHANGE OF SHARES

17. According to the European Merger Directive an exchange of shares or a share merger is the operation whereby a company acquires a holding in the capital of another 'target' company so that it obtains a majority of the voting rights in this company. The shareholders of the target company obtain in exchange for their shares securities issued by the acquiring company, representing its own capital. If applicable, these shareholders obtain also a cash payment, which should not exceed 10% of the nominal value or, in absence of nominal value, of the accounting par value of the securities issued in exchange.[36] The Belgian Company Code does not explicitly mention a definition of exchange of shares.

18. Share-for-share M&As are a good introduction to the more modern cross-border M&A structures like triangular mergers etc. All these structures tend to allow shareholders in the target company to have post-purchase shares in an entity of their home jurisdiction even if the purchaser is a foreign group. Although emotional or nationalist flag issues certainly come into play, one main reason for developing these cross-border M&A structures is the tax consequences.[37]

3. 4. MERGERS AND DIVISIONS, DOMESTIC REORGANISATIONS

19. Under the Belgian Income Tax Code, and as a general principle, a merger is treated as a liquidation of the acquired company.[38] This has two consequences. Firstly, all gains, realized or only recognised, on the assets and liabilities of the acquired company, are subject to corporate income taxation and will have their proper tax treatment (sometimes exemption, as for realized

[35] TH. BLOCKERYE & J.F. LYCOPS, *Reorganisatie van Belgische naamloze vennootschappen. Juridische, boekhoudkundige en fiscale aspecten*, ced.samsom, 1994, 383.
[36] Article 2, d, European Merger Directive.
[37] W. DEJONGHE & W. VAN DE VOORDE, *M&A in Belgium*, Kluwer law international, 2001, 171.
[38] Article 210, § 1, 1° BITC.

gains on shares, mostly effective taxation for other gains).[39] Secondly, all elements of the acquired company's equity are treated as if they were distributed. A distribution of effectively paid-in share capital and of previously taxed earnings does not trigger corporate income tax again, but a distribution of previously tax-exempt funds does trigger corporate income tax.[40]

20. The dissolution of a company that does not comply with the conditions for tax exemption (*cfr. infra* no. 30) will go into liquidation and will therefore be subject to the usual corporation tax during the liquidation period. The company's profits will include among other things the gain realized or determined as a result of the distribution of the assets.[41] The distribution of the assets results in payments in cash, securities, assets in kind or in any other form. The positive difference between these payments and the re-estimated value of the effectively paid-in capital constitutes the liquidation distribution. This liquidation distribution is considered to be a dividend on behalf of the acquired company.[42]

The payments made in the context of a company's liquidation originate in first instance from the re-estimated value of the fiscal capital. Subsequently these payments stem from the previously taxed reserves, i.e. the previously reserved profit already subjected to the corporation tax (including the capital gains realized due to the reorganisation). Ultimately, the payments arise from the previously tax exempted profit.[43] Only this final part of the liquidation distribution is subject to corporation tax, because the 'condition of blocked reserve' is not fulfilled anymore.[44] These profits were exempted from corporation tax in the past insofar that they were booked on one or more separate blocked reserve accounts. These reserves are blocked because they cannot be used in anyway to be included in the profits of a particular financial year. As soon as this condition stops from being satisfied, the – tax exempt – reserves become taxable.[45]

According to legal doctrine the liquidation distribution, which is considered to be a dividend on behalf of the acquired company, is not subject to a withholding tax.[46] The law of 23 October 1993 confirmed this viewpoint by explicitly stipulating that no withholding tax is due on such liquidation-dividends.[47] The logic behind this rule can nevertheless be doubted. A distribution of reserves as dividends will be subject to a withholding tax,

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[39] Article 208, BITC.
[40] Article 209, BITC.
[41] Article 208, BITC.
[42] Article 209, firt paragraph, BITC.
[43] Article 209, second paragraph, BITC.
[44] A. HAELTERMAN, *Fiscaal recht*, 2000, 116.
[45] Article 190, fourth paragraph, BITC.
[46] P. ERNST, J. VERSTRAELEN, *Reorganisatie van vennootschappen*, ced.samsom, 2002, 312.
[47] Article 264, BITC.

depending on the time of distribution, i.e. before or after the dissolution and liquidation of the company.[48]

A proposal of law however foresaw the introduction of a withholding tax of 10% on the dividend realized in the context of liquidation.[49] This proposal states that withholding tax is applicable to all liquidation distributions granted from 1st January 2002 if the liquidation has not been closed before 25th March 2002.[50] The law of December 24th, 2002 has turned this proposal into law.

21. The liquidation bonus which shareholders-individuals receive as a result of the splitting up of the assets of the liquidated company is not considered as income from capital.[51] If the shares in the liquidated company belong to the private estate of the shareholder individual, then the capital gains realized by the shareholder will be tax exempted. A loss in value is not tax deductible. If the shares are however used by the shareholder in the framework of his professional activities, the realized capital gains will belong to the taxable profit of that shareholder. If the shares are used for more than 5 years during the course of one's professional activities, the capital gain is taxable at the rate of 16,5%.[52] In the other situations, the capital gain will be taxed at the progressive income tax rate. A loss in value realized by the shares exerted professionally is however tax deductible.

The realized capital gain by the shareholder-company will qualify for a tax deduction as 'participation exemption' if the quantitative and qualitative conditions to that end are fulfilled.[53] A possible decrease in value is not tax deductible, unless the endured loss is so enormous that part of the fiscal capital represented by the participation is lost. Only in this case, and to the degree of the lost fiscal capital, will the loss be fiscally deductible.[54]

22. When the dissolving company does not comply with the conditions for tax exemption, for tax purposes it will be deemed to liquidate, under company law there is no liquidation however. Because the dissolving company looses its separate legal personality, it will be unable to transfer its losses from previous fiscal years to the acquiring company.[55]

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[48] *Cf.* J. KIRKPATRICK, *Le régime fiscal des sociétés en Belgique*, 2ème Ed, Bruylant, Bruxelles, 1995, 231.
[49] *Parl.St.,* Kamer, 2001-2002, Doc 50 1918/001, art 16.
[50] *Parl.St.,* Kamer, 2001-2002, Doc 50 1918/001, art 32.
[51] Article 21, 2° BITC. The payments mentioned in art 19,§1, 4° are however considered as interest.
[52] Article 171, BITC.
[53] Article 202, §1, 2° BITC.
[54] Article 198, first paragraph, 7° BITC.
[55] C. AMAND, M. DE MUYNCK, G. DE NEEF, *Overdracht van ondernemingen*, Larcier, 1999, 340.

3. 5. MERGERS AND DIVISIONS: CROSS-BORDER REORGANISATIONS

23. Fiscal treatment of cross-border mergers and divisions in Belgium is an issue impossible to deal with, because these cross-border reorganisations are still not legally acceptable. The problem is Belgian corporate legislation. It does not yet provide a legal framework for cross-border reorganisations. After all, the tenth Directive has not yet been adopted, and EU member states are still free to regulate international mergers themselves. (*cfr. supra* no. 6 and 11) As a consequence, Belgium still treats this kind of cross-border transactions as taxable subject matter.

Although some authors have defended the opinion that the rules for domestic mergers also apply to international mergers, this is far from being generally accepted. Moreover, they would most often be extremely complex to implement. The only choice therefore seems to wind up the company to be merged and contribute all of its assets and liabilities to the surviving company. The question also arises whether the other company's national law accepts this.[56]

24. If Belgium was to introduce the concept of cross-border mergers and divisions into its Company Code, then the fiscal treatment in Belgium of these cross-border reorganisations will most likely correspond with the European Merger Directive. Article 4 of this Directive guarantees fiscal neutrality on behalf of the acquired company. This implies that the transfer of properties (or part of it) does not give rise to immediate taxation upon capital gains, on condition that the transferred assets preserve all their previous characteristics[57]. Appreciation, depreciation etc. shall be calculated as before the merger. Legislation of the member states may deviate from this condition, but then the tax relief is not applicable.

3. 6. TRANSFER OF ASSETS, DOMESTIC REORGANISATION

25. The most important difference with mergers and divisions is that in case of a transfer of assets the transferring company does not cease to exist.[58] Contrary to the merger case, the shares issued by the acquiring company are received by the transferring company itself, not its shareholders.[59] Consequently, realized capital gains will be taxed on behalf of the company, not its shareholders. The fiscal treatment of these capital gains will depend upon the nature of the underlying asset. Capital gains of shares are exempted from corporate income tax, insofar all conditions of article 192 of the Belgian

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[56] W. DEJONGHE & W. VAN DE VOORDE, *M & A in Belgium*, Kluwer law international, 2001, 137-138.
[57] Article 4, second paragraph, European Merger Directive.
[58] TH. BLOCKERYE & J.F. LYCOPS, *Reorganisatie van Belgische naamloze vennootschappen. Juridische, boekhoudkundige en fiscale aspecten.*, 1994, ced.samsom, 398.
[59] J. COUTURIER, "Inbreng van een algemeenheid of van een bedrijfstak", *A.F.T.* 1998, 140.

Income Tax Code are met. Capital gains of material, immaterial or financial assets are exempted from taxation on the monetary part. The non-monetary part of these assets is however fully taxable, just as any other asset.

26. The acquiring company must take over all the transferred activities, together with all their fiscal features (depreciation, deductions for investments, appreciation) as if they had not been transferred at all.

3. 7. EXCHANGE OF SHARES, DOMESTIC REORGANISATION

27. From a Belgian legal and tax perspective, a transfer of shares in exchange for the shares of the acquiring company is a contribution to the capital of the acquiring company (especially when those shares are new shares). For income tax purposes all the rules apply for a sale of shares in which the consideration is cash. This means that in general capital gains are tax exempt. Distinction must be made between ‘individual’ sellers and ‘company’ sellers.

A seller of shares in a Belgian company may be an individual, which is usually the case when an incorporated business is family-owned. Under this assumption, capital gains on an individual’s private assets are tax exempt if these assets concern securities, tangible assets or real estate.[60] Secondly, the gains must be recognised on transactions that are still within the limits of the ‘normal management of a private estate’ (i.e. the transactions are not to be considered as professional transactions, or as speculative transactions. If these conditions are not met, capital gains on an individual’s private assets may be treated as ‘miscellaneous income’, which will be subject in this case to a 33% individual income tax rate.

The tax-free nature of gains on shares has one exception, namely for gains on a ‘substantial shareholding’. The exception applies to capital gains on a sale of shares belonging to a ‘substantial shareholding’ in a Belgian company if that sale is to a foreign entity.[61] As we are dealing with a cross-border border situation here, we refer to the next section.

When the seller is a Belgian company, the Belgian corporate income tax supports a system commonly known as the ‘participation exemption’, under which most realized capital gains on shares are totally tax exempt.[62]

[60] Article 90, 1. In some cases capital gains on real estate are however taxed as miscellaneous income (article 90, 8° and 10° BITC).
[61] Article 90, 9°, BITC.
[62] Article 192, BITC.

3. 8. EXCHANGE OF SHARES, CROSS-BORDER REORGANISATION

28. If an M&A is structured as a share exchange, some countries only allow for tax relief on gains exchanged if the shares received in return are also domestic shares. This is not systematically true for Belgium, because, as we explained in the previous section, Belgium has almost no capital gains tax on shares. However, the 16.5% capital gains tax on substantial shareholdings has the inconvenience that it is triggered by having foreign shares as consideration.[63] A 'substantial shareholding' exists if an individual seller with his or her close relatives holds more than 25% of the Belgian target company at any time during the 5 years prior to the sale.

29. Conclusively there is the case where the sale of shares is performed by a foreign company. In most cases, no tax is due on the capital gains derived from the sale. If the shares sold did not belong to a Belgian 'permanent establishment' of the seller, Belgian tax law does not even permit Belgium to tax these capital gains.[64] If the shares sold did belong to a Belgian 'permanent establishment', Belgium can levy a tax. But the same 'participation exemption' of Belgian corporate income tax is applicable.[65]

4. CONDITIONS FOR TAX EXEMPTION

4. 1. MERGERS AND DIVISIONS

30. For a **domestic merger** to be entitled to tax exemption, three conditions should be fulfilled. First, the acquiring company must be a Belgian one. Secondly, the realization of the merger must be in accordance with Belgian Company Code (new since June 29th, 1993). Finally, the motives of the merger should be of a financial or economic nature.[66]

31. The first condition explicitly excludes cross-border mergers and divisions from the scope of the article dealing with tax exemptions. For clarification of the concept 'Belgian firm' we should refer to the definition mentioned in the Belgian Income Tax Code. It defines a Belgian, domestic company as any company, association, institution or establishment which has lawfully been established, has legal corporate personality and exploits an enterprise or performs profitable activities. Moreover, the company must have its business seat, principal important establishment or place of effective management in Belgium without being exempted from corporation tax.[67]

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[63] Article 90, 9°, BITC.
[64] As these gains are not covered by article 228 of the Belgian Income Tax Code.
[65] Article 235, 2°, BITC.
[66] Article 211, §1, second paragraph, 1°, 2° and 3°, BITC.
[67] Article 2, §2, 1° and 2°, BITC.

According to corporate law it is of no importance whether the company was set up according to domestic or foreign legislation, as long as the seat of the company is located in Belgium.[68] Takeover of another company located abroad by a Belgian company within the framework of a merger should be no problem, provided that the legislation of the member state of the acquired company does not oppose such transaction.[69]

32. The second condition requires that the merger occurs without liquidation of the acquired company. Furthermore, additional cash payments to shareholders of the acquired company may not exceed 10% of the nominal value (or par value if there is no nominal value) of the shares they have received.[70] At least two or more companies should be involved in the transaction and all properties of the acquired company must be transferred to the acquiring company. With reference to this argument the Belgian tax Administration has tried to refuse tax exemption in some cases, stating that the acquiring company had no own existence (activity).[71]

33. As far as the third condition is concerned, it has to be pointed out that interpretation problems might arise when comparing Belgian with European expressions. Firstly, Belgian law requires that the motives of the merger are of a financial or economic nature. This implies that only the mergers which are not exclusively or mainly concluded for tax-saving or tax-avoiding reasons will pass the test.[72] Previous to the actual merger, companies can request a ruling to make sure their action corresponds to financial economic needs.[73] According to the European Directive member states cannot apply general criteria determined in advance which cause an automatic presumption of fraud in order to exclude the transaction from tax exemption.[74] Some authors argue however that Belgian law does not violate the European Directive because the requirement for financial or economic purpose of the merger is independently assessed for each transaction *in concreto*.[75]

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[68] Article 56, Belgian Company Code.

[69] S. EMMERECHTS, "De grensoverschrijdende fusie onder de loep: vennootschapsrechtelijk en fiscaalrechtelijk", *V&F,* 2000, 210.

[70] Article 671, Belgian Company Code.

[71] J.P. LYCOPS and TH. BLOCKERYE, "Fusie en splitsingen van vennootschappen", *A.F.T.*, 1993, 197.
Arrest Firestone, Antwerpen, 13 januari 1976, A.F.T., 1976, 155.

[72] D. BEECKMAN, D. PIENS, W. VANDENBERGHE, E. DE LEMBRE, *Van ontbinding tot fusie*, ced.samsom, 1999, 380.

[73] Article 20 van de Wet van 24 december 2002 tot wijziging van de vennootschapsregeling inzake inkomstenbelastingen en tot instelling van een systeem van voorafgaande beslissingen in fiscale zaken [*Cfr*. J.P. LYCOPS and TH. BLOCKERYE, 'Fusie en splitsing van vennootschappen', *A.F.T.*, 1993, 211.].

[74] S. EMMERECHTS, "De grensoverschrijdende fusie onder de loep: vennootschapsrechtelijk en fiscaalrechtelijk", *V&F*, 2000, 214.

[75] *Cfr.* TH. BLOCKERYE & J.F. LYCOPS, *Reorganisatie van Belgische naamloze vennootschappen; Juridische, boekhoudkundige en fiscale aspecten*., 1994, ced.samsom, 385.

Secondly, in Belgium the burden of evidence concerning the purpose of the transaction rests upon the taxpayer. Consequently, the taxpayer is excluded from exemption whenever he does not succeed at proving the financial or economic reasons of the merger, irrespective of the presence of fraudulent intentions. S. Emmerechts doubts if this can still be maintained in the light of the Leur-Bloem judgement.[76]

34. When each of the three above-mentioned conditions for tax exemption are fulfilled, the taxpayer cannot refuse the exemption regime.[77] As aforesaid, it is possible to have an advance tax ruling on whether the merging companies' (or only the target company's) business or financial motivations for merging are justified.[78]

35. The conditions under which a fiscal neutral regime applies to **cross-border mergers and divisions** have already been mentioned (*cfr. supra* no. 24). All transferred assets must preserve their tax features, as if they had never been transferred at all. Member states can deviate here-from, but they subsequently lose their privilege of application of the tax-neutral regime.

4. 2. TRANSFER OF ASSETS

36. Tax exemption for a **domestic transfer of assets** is, contrary to the exemption system of a merger, still optional. The company can choose to make use of the exemption regulation of article 46, § 1, 2° of the Belgian Income

[76] On 17th of July the European Court of justice made a pioneering judgement concerning an exchange of shares. Madame Leur-Bloem owned 100% of the shares of a profit earning company and 100% of the shares of a loss-making company. She decided to transfer all of these shares to a newly founded company by means of an exchange of shares in order to compensate the profits and losses of the previously independent companies. The Dutch tax administration reasoned that this reorganisation could not constitute a (tax exempted) exchange of shares because the operation did not bring about a financial and economic enduring entity. This condition was required by the Dutch tax law in addition to the anti-abuse rules of the European Merger Directive. However, the European Court of Justice decided that this requirement of an enduring merger of two companies is not in accordance with art 11.1 (a) of the European Merger Directive. This article states that member states do not have to grant a tax exemption for a reorganisation if there exists a presumption that the operation has tax evasion or tax avoidance as its principal objective or as one of its principal objectives. This presumption can however only exist when the reorganisation is examined in all its aspects *in concreto.* According to the European Court of Justice member states cannot apply general criteria determined in advance which cause an automatic presumption of fraud in order to exclude the transaction from tax exemption. Consequently, the fact that Madame Leur-Bloem was the exclusive shareholder of both the acquired and acquiring company is not an impediment for the legal transaction to constitute an exchange of shares. [S. EMMERECHTS, 'De grensoverschrijdende fusie onder de loep: vennootschapsrechtelijk en fiscaalrechtelijk', *V&F,* 2000, 215.]

[77] C. AMMAND, M. DE MUYNCK, G. DE NEEF, *Overdracht van ondernemingen*, 1999, Larcier, 419.

[78] Article 20 van de Wet van 24 december 2002 tot wijziging van de vennootschapsregeling inzake inkomstenbelastingen en tot instelling van een systeem van voorafgaande beslissingen in fiscale zaken

Tax Code.[79] Whenever the company prefers to enjoy tax exemption, it should fulfil four conditions. The transaction must constitute a transfer of 'branch of activity' (part of a business) or a 'universality of goods' (all assets and liabilities). The acquiring company must have its business seat or most important establishment in one of the member states of the Community. The transfer must exclusively be compensated with shares of the acquiring company. Finally, purpose of the transaction must be of a financial or economic nature.

37. **Cross-border transfers of assets** are not subject to more constraints than to domestic transactions. The condition that the acquiring company must have its business seat or most important establishment in Belgium has been extended to companies located in the European Union to be in accordance with the Directive.

4. 3. EXCHANGE OF SHARES

38. Capital gains taxation on shares transferred between EU-shareholders almost never occurs in Belgium. However, the 16.5% capital gains tax on substantial shareholdings has the inconvenience that it is triggered by having **foreign** shares as an exchange currency (*cfr. supra* no. 28). That provision may prove to be a violation of fundamental freedoms under EU treaty law.

Still, exchange of shares is a favourable option. After all, cross-border dividends are still far from being tax efficient. Exemptions for dividend withholding tax for parent-subsidiary situations are only possible for relatively large intra-European shareholdings by corporate shareholders, not for smaller, individually owned shareholdings.[80] Even in Europe, individual shareholders might still face double taxation, although the European Court of Justice now tends to challenge obvious unequal treatment between domestic and foreign shareholders under withholding tax rules.[81]

5. TAX FREE REORGANISATIONS

5. 1. MERGERS & DIVISION

39. As an exception to the general principle of taxation, a tax relief is available for **domestic mergers and divisions** if three conditions are met. Both the acquiring company and the acquired company are resident in

[79] TH. BLOCKERYE & J.F. LYCOPS, *Reorganisatie van Belgische naamloze vennootschappen. Juridische, boekhoudkundige en fiscale aspecten.*, 1994, ced.samsom, 398.
[80] Parent-Subsidiary Directive 90/435/EEC, July 23th, 1990.
[81] W. DEJONGHE & W. VAN DE VOORDE, *M&A in Belgium*, Kluwer law international, 2001, 172. [H.v.J., 6 June 2000, Case c-35/98].

Belgium; the transaction complies with the Belgian Company Code; the transaction is justified by a sound business or financial motivation (*cfr. supra* no. 30). Company reorganisations usually give rise to taxation as soon as one or more of the involved companies are dissolved and liquidated. The latter actions create corporate taxation on reserves of the acquired company, which have not previously been subject to taxation. Capital gains originating from the transaction are also subject to taxation.[82] It is most likely that capital gains will arise. Previously, every capital gain determined and realized following the distribution of the assets of a company used to be taxable in Belgium.[83] The introduction of article 211 of the Belgian Income Tax Code has modified this situation. When the relevant conditions are fulfilled, some of the capital gains realized through the merger will be exempted from taxation. This system is in fact obligatory, in the sense that there is no option for a taxable transaction. An exemption will be made as soon as all conditions are fulfilled. (*cfr. supra* no. 30) By not fulfilling one of the conditions for exemption however, one can escape the obligatory exemption.

40. The tax relief completely exempts all capital gains on the assets and liabilities of the acquired company.[84] The previously recognized, not yet realised capital gains (so-called 'gains from revaluations') and the effectively realized capital gains which will be reinvested, remain exempted from taxation.[85] An exception to this rule exists for determined gains on stock in trade and work in progress. The latter will immediately constitute a profit that will be taxed. Capital subsidies from article 362 of the Belgian Income Tax Code which are not yet indicated as profits at the moment of the transaction remain exempted from any taxation.

A broad category of capital gains originating from the transaction are equally exempted from taxation. This rule is however only valid for values present, but not for unrealised capital gains, in the dissolved company. An example here could be the clientele of the company built up over the years. All tax characteristics of these assets and liabilities are simply transferred to the acquiring company.[86] There is also a category of capital gains which is subject to taxation, but spread out over time. These capital gains, for which there is an obligation of reinvestment are realised on assets older than 5 years and for which a substitution reserve account is made.[87]

41. Whenever a company is dissolved and all property and capital of the company is distributed, it is likely that a liquidation bonus is paid to the

[82] C. AMAND, M. DE MUYNCK, G. DE NEEF, *Overdracht van ondernemingen*, 1999, Larcier, 357.
[83] Article 102, BITC.
[84] Article 211, § 1, 1°, BITC.
[85] Article 211, BITC.
[86] Article 212, BITC.
[87] Article 47, BITC.

shareholders. As above-mentioned these dividends are subject to a withholding tax of 10% on behalf of the liquidated company. (*cfr. supra* no. 20). However, if the three conditions for a tax exempted merger are fulfilled, the taxation as a result of the distribution of the company's equity[88] will be deferred to the extent that the transfer is compensated with the issuance of new shares.[89] In practice, this means that under the tax relief, only that part of the acquired company's equity that is not transferred to the acquiring company (because part of the consideration for the merger was cash or because of a pre-existing shareholding between both the companies), is treated as if it were distributed.[90] This may be very unsatisfactory in case of an acquired company that was already owned by the acquiring company and that has lots of previously tax-exempt reserves.[91]

In Belgium, the possible impact of art 211, §1, 2° of the Belgian Income Tax Code must not be underestimated. After all, the Belgian Company Code explicitly forbids the acquiring company to issue new shares with the intention to exchange the new shares for old shares of the acquired company which the acquiring company already owned.[92] This rule is most unfortunate for companies that have a 100 % participation in the company they wish to acquire. In this case, capital gains will be subject to taxation.[93] (*cfr. infra* no. 71)

42. Under the tax relief, each company's losses carried forward are transferable in the following proportion: net fiscal value of the target company / net fiscal value of both the target and acquiring company.[94] If these losses are located within a company with a low net fiscal value, a merger may cause a substantial portion of these losses to evaporate. There are also limitations for the carry-over when there is a substantial change in ownership.

43. As aforesaid, it is difficult to say much about possible exemptions for **cross-border mergers and divisions** in Belgium. Therefore a cross-border merger will, for now, be treated in Belgium for tax purposes as a taxable transaction (*cfr. supra* no.23).[95]

44. Still, we should have a closer look at the Directive. The Directive reflects the principle of continuity for companies, which corresponds to the

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[88] Article 209, BITC.
[89] Article 211, BITC.
[90] Article 211, § 1, 2° and § 2, BITC.
[91] W. DEJONGHE & W. VAN DE VOORDE, *M & A in Belgium*, Kluwer law internaional, 2001, 143.
[92] Article 703, §2 and 740, §2, Belgian Company Code.
[93] C. AMAND, M. DE MUYNCK, G. DE NEEF, *Overdracht van ondernemingen*, 1999, Larcier, 360.
[94] Article 206, § 2, second paragraph, BITC.
[95] W. DEJONGHE & W. VAN DE VOORDE, *M & A in Belgium*, Kluwer law internaional, 2001, 138.

tax-neutral regime in fiscal matters. The tax relief is only a postponement of taxation. Whenever the acquiring company realizes assets or liabilities afterwards, any capital gains shall be taxable in the state where the acquired company is located. After all, transferred assets do constitute a permanent establishment in that state.

Also for the maintenance of the neutrality principle, the Directive determines that losses of the disappearing company can be taken over by the fixed places of business of the receiving company that are located in the country of the acquired company.[96] This is only possible if domestic legislation of the member state of the acquired company allows for a similar regime for its domestic reorganisations. The Directive does however not mention the destination of the losses from the acquiring company.

Since October 1st, 1993 transfer of losses is allowed in Belgium, but only for national mergers and divisions. The reason for this is the same reason we have already mentioned several times before (*cfr. supra* no. 23 and 43). A takeover of a Belgian company by a foreign one will not allow the legal transfer of losses.[97] Thus once again, cross-border mergers will be treated less favourably than domestic ones.

5. 2. TRANSFER OF ASSETS

45. First, two remarks have to be made. Firstly, no distinction has to be made between a domestic and a cross-border transfer of assets. Belgian legislation has been modified so that transfers within the Community are entitled to the benefits of an exemption. Secondly, the exemption regime is optional (*cfr. supra* no. 36). The transferring company is thus free to choose between immediate taxation or postponed taxation (exemption regime) on the capital gains that might arise by occasion of the transfer.

46. Fiscal treatment in Belgium of a cross-border transfer of assets was adapted to the regulations of the Merger Directive by the law of July 28th 1992. This law expanded the existing rules for this type of reorganisations towards transactions within the Community.[98] Article 46 Belgian Income Tax Code was modified, so that the fiscal principle of neutrality applicable to transfers of assets between Belgian companies would also be applicable to similar transfers in a Community context.[99] When the company receiving the transfer is located in another member state of the Community than Belgium, the transferred assets are assumed to constitute a Belgian permanent establishment. Whenever

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[96] Article 6, European Merger Directive.
[97] TH. BLOCKERYE & J.P. LYCOPS, "Fusie en splitsing van vennootschappen. De wet van 6 augustus 1993 gezien in het licht van het gemeenschapsrecht", *A.F.T.,* 1993, 203.
[98] J.J. COUTURIER, "Inbreng van een algemeenheid of van een bedrijfstak", *A.F.T.* 1998, 139.
[99] TH. BLOCKERYE & J.F. LYCOPS, *Reorganisatie van Belgische naamloze vennootschappen. Juridische, boekhoudkundige en fiscale aspecten.*, 1994, ced.samsom, 383.

the company ceases its activities in the other member state, the assets transferred in the Belgian permanent establishment are considered to be realized, and by consequence subject to taxation in Belgium.[100]

47. Article 46 of the Belgian Income Tax Code does not allow for losses of the inserting company to be transferred to the acquiring company. This is not in conflict with the Directive which explicitly allows member states to derogate from this principle in the Directive. Article 6 of the Directive states that recoverable losses may be transferred but only insofar the Administration of the member state where the transferring company is located provides for this possibility for domestic transfers of assets.

48. If the exemption regime is chosen by the company, the following rules will apply. Revenues that were determined or obtained by occasion of a complete and definitive standstill of the activities of the company, and which originate from the gains on assets that were used for professional activities' sake, can be fully exempted from taxation.[101] The exemption, however, is only temporary and is given only insofar four conditions are fulfilled (*cfr. supra* no. 36).

For the company partially transferring its activity, the value of the received shares is equal to the fiscal value of the transferred assets. The capital gains realized through the transaction – this is the difference between the value of the received shares and the fiscal value of the transferred assets – are temporarily exempted from taxation only if they are credited and held on a separate blocked reserve account.[102] When the transferred assets are being realized later on, the realisation will give rise to taxation.

On behalf of the acquiring company, it is not necessary to make a difference between taxed or tax-exempted reserves. After all, contrary to the merger case, there is no transfer of exempted reserves, provisions and capital gains from one company to another because the transferor company remains in existence.[103]

49. Business loss carry forwards are only deductible in a certain proportion (*cfr. supra* no. 42).[104]

5. 3. EXCHANGE OF SHARES

50. As far as **exchange of shares** is concerned, we might state that Belgian legislation is in full accordance with the Merger Directive. Tax

[100] Article 46, §1, 2°, BITC.
[101] Article 28, first paragraph, 1°, BITC juncto article 46, §1, first paragraph, 2°, BITC
[102] they should remain 'unaffected' or 'untouched', article 190, BITC
[103] TH. BLOCKERYE & J.F. LYCOPS, *Reorganisatie van Belgische naamloze vennootschappen. Juridische, boekhoudkundige en fiscale aspecten.*, 1994, ced.samsom, 407.
[104] Article 206, § 2, BITC.

exemption in Belgium is in fact much broader than the one prescribed by the European Directive.[105] Firstly, the Belgian exemption is final whereas the Merger Directive implies a deferral of taxation[106], not a postponement. Secondly, the exemption is also valid for shares in non-European companies. On the contrary, the European Directive only concentrates on the exchange of shares in which companies from two or more member states are involved.[107] Thirdly, in Belgium tax exemption is granted according to Belgian national legislation regardless the amount of shares transferred (except for the capital duty exemption, *cfr. infra* no. 64/1). Instead, European law requires the acquiring company to obtain a voting majority in the target company through the operation of an exchange of shares.

7. VAT AND CAPITAL DUTY

7. 1. VAT

7.1.1 Transfer of assets

51. In principle, Belgian VAT is due on the transfer of a business or a part of a business (other than land and old buildings). The transferred items (e.g. the stock in trade) fall within the scope of the VAT. If the transferee is a VAT taxpayer, the VAT incurred may be credited in the periodical VAT return of the acquiring company. However, the Belgian VAT code contains an exception to this principle and provides that if transferred assets qualify as a whole business or an independent branch of activity, the transfer is not considered to be a supply and is therefore not subject to VAT.[108] Because of this exemption the financial position of both the transferee and transferor is not needlessly burdened. In absence of this exception, the acquiring company would only be able to recuperate the charged VAT by the transferor through its periodical VAT returns.[109]

52. A transfer of a whole business or a branch of activity qualifies for the VAT exemption, provided that the following four conditions are met[110]:

[105] C. AMAND, M. DE MUYNCK & G. DE NEEF, *Overdracht van ondernemingen: fiscaal-juridische aspecten.*, 1999, 418.
[106] Member states are allowed to tax the gains arising out of the subsequent transfer of securities received in the same way as the gains arising from the transfer of securities existing before the acquisition (art. 8, 2° European Merger Directive).
[107] Article 1, European Merger Directive.
[108] Article 11, VAT Code.
[109] DE SPIEGELEER J., HERREMAN F., STAS D., THESIN K., VANDENDRIESSCHE P., *Fiscale basisbegrippen. BTW.*, Die Keure 1998, 62.
[110] J. POLLET, "Value Added Taxation in Europe", *International Bureau of fiscal documentation* mei 2000, Suppl. No 105, 29.

(1) The transfer must relate to a whole business or to a branch of activity. With respect to the transfer of a whole business, the exemption will only be granted if all elements of the business are being transferred at once. In the case of the transfer of a branch of activity, the exemption will only be granted if the transfer relates to all the goods invested in that branch of activity and if these goods constitute, from technical point a view, an independent company which can operate separately by its own means. In such a case, the transfer will generally include the immovable goods as well.[111]

(2) Both parties to the transaction are VAT registered entities.

(3) The acquiring company continues the business previously preformed by the seller. The acquiring company thus takes on all the rights and obligations with respect to VAT, because the transferee is assumed to continue the person of the transferor.

(4) The receiving company would have been able to deduct, wholly or partially, the VAT charged by the transferring country if the transfer had been subject to VAT. The entitlement of the acquiring company to deduct the VAT may be the result of the transfer itself.[112]

53. If the four above-mentioned conditions are met, the exemption is automatically applicable. The transfer of a whole business or a branch of activity needs to be concluded in an official document by the parties involved in the transfer. Each party has to be in possession of a copy of that document.[113] The document has to include in particular the following references: (a) the date of the transfer, (b) the name, address and VAT identification number of the parties involved in the transfer, (c) a detailed description of the transfer, and, (d) if applicable, the price of the transfer. Nevertheless, a transfer of a whole business or branch of activity that takes place free of charge can also enjoy the tax exemption if all the necessary conditions are fulfilled.

54. If the conditions for a VAT exemption are not satisfied, then each transferred item of the business or branch of activity will have to be examined separately for VAT purposes. The VAT rate will vary according to the nature of each transferred element. The transfer of each physical element will constitute a VAT taxable delivery. The transferring company then needs to declare officially the VAT due as a result of the transfer.
If the VAT exemption is not applicable, the previously deducted VAT for the goods part of the transfer will have to be revised for a 5 or 10 year period;

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[111] In some specific cases the tax administration will agree to an exemption although the immovable property is not being transferred. This is the case when the transferee will continue to use the immovable goods for the exploitation of the other branches of activities he keeps.
[112] F. BORGER & P. WILLE, *Handboek BTW*, Intersentia, 2002.
[113] Article 11, VAT Code, K.B. NR.1.

7.1.2 Mergers & divisions

55. Mergers are treated for VAT purposes in the same way as a transfer of a business (to be precise, a universality of goods). This implies that no VAT is due if two conditions are simultaneously fulfilled[114]:

(1) All assets of the acquired company need to be transferred to the receiving company
(2) The acquiring company has to be subject to VAT taxation, notwithstanding the fact that the company is taxed or exempted from tax for income tax purposes.

56. If the receiving company is not subject to VAT, a 5 or 10 year period revision of the tax relating to the transferred assets and of which the deduction was allowed will have to take place on behalf of the acquired company. Unlike usual the revision will not take place every year, but at once at the time the capacity of VAT taxpayer ceases to exist. The revision should be dealt with in the final VAT return.[115]

57. Divisions are also treated in the same way as a transfer of a business (to be precise, a universality of goods) for VAT purposes. This implies that no VAT is due if two conditions are simultaneously fulfilled.[116]

(1) All assets of the acquired company need to be transferred to the one or more receiving companies

(2) The one or more acquiring companies need to be subject to VAT taxation if they want to benefit from the VAT tax exemption. The fact that one receiving company is not registered for VAT purposes does not hinder the applicability of the tax exemption for the other receiving –and VAT paying- companies. A revision, for the goods transferred to the receiving company that is not subject to VAT, will have to take place on behalf of the devised company.

7.1.3 Exchange of shares

58. An exchange of shares does not cause a VAT-charge. No VAT is due for these types of reorganisations because only a transfer/delivery of physical goods is subject to VAT.[117]

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[114] TH. BLOCKEYRE & J.P. LYCOPS, *Reorganisatie van Belgische naamloze vennootschappen. Juridische, boekhoudkundige en fiscale aspecten.*, ced.samsom, 1994, 315.
[115] Article 11, §3, VAT Code, K.B. NR.3.
TH. BLOCKEYRE & J.P. LYCOPS, *Reorganisatie van Belgische naamloze vennootschappen. Juridische, boekhoudkundige en fiscale aspecten.*, ced.samsom, 1994, 316.
[116] TH. BLOCKEYRE & J.P. LYCOPS, *Reorganisatie van Belgische naamloze vennootschappen. Juridische, boekhoudkundige en fiscale aspecten.*, ced.samsom, 1994, 315.

7. 2. CAPITAL DUTY

59. The rules concerning indirect taxes levied upon the collecting of capital have been harmonised on community level by the Directive 69/335/EEG from 17th July 1969. The Directive stipulates that the contribution to capital may enjoy relief of capital duties, or be subject to proportional capital duties up to a maximum of 1%. Except for this duty tax, member states cannot impose any other taxation upon the raising of capital. Some exceptions to this rule have however been included in article 12 of the Directive.[118]

60. According to the Belgian registration tax code, the transfer of immovable and movable assets to a company which has its effective place of management in Belgium or otherwise to a company which has it statutory seat in Belgium and its effective place of management outside the EU, is subject to a capital duty of 0,5%. This percentage is levied over the total amount of the transfer or capital increase.[119] It can be concluded that the Belgian registration tax is consistent with the above-mentioned EU Directive.

7.2.1 Transfer of assets

61. Nonetheless, the transfer of a universality of goods or a branch of activity is not subject to the above-mentioned capital duty of 0,5% on the condition that the transferring company has EU nationality and that the transfer is almost exclusively compensated with the shares representing the capital of the company receiving the transfer. When the conditions are fulfilled, there is a lump sum tax of only 25 euros. Hence, the first requisite for an exemption is that the transferring company has its effective place of management or statutory seat situated on the territory of a EU Member State. Secondly, it is required that the transfer comes to pass in exchange for the shares representing the nominal capital of the acquiring company, possibly increased with a mark-up in cash up to 10% of the nominal value of the assigned shares.[120]

7.2.2 Mergers and divisions

62. Transfers of a universality of goods, by way of merger or division, are treated in a similar way as a transfer of assets by the Belgian Registration Tax Code. This implies that mergers and divisions will equally be exempted from capital duties as a transfer of assets, as long as the 2 relevant conditions for tax exemption are met. Only the lump sum tax will be due.

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[117] Article 9, paragraph 1, VAT Code.
[118] C. AMAND, M. DE MUYNCK, G. DE NEEF, *Overdracht van ondernemingen*, Larcier, 1999, 437.
[119] Article 115, 115 bis, 116, Belgian Registration Code.
[120] Article 117, §1, 2, Belgian Registration Code.

63. The notion of merger under the Belgian Registration Tax Code is different from the notion under Belgian company code. A transaction whereby the receiving company acquires its subsidiary of which it already owns a 100% of the capital, is not considered to be a merger under the Belgian Registration Tax Code. This transaction will therefore not benefit from the 0,5% capital duty (and the 12.5% or 10% real estate transfer tax when the transfer involves immovable property).

7.2.3 Exchange of shares

64. Since 15th January 1999 no registration duties are applied anymore to an exchange of shares, as long as both the material and formal requirements are fulfilled.[121]

The material conditions for a tax exemption are[122]:

(1) the transfer of shares representing nominal capital should have as a result that the receiving company acquires at least 75% of the nominal capital of the transferring company.

If the 75% criterion is obtained on account of several transfers, the exemption will only be applied to the transfer resulting in the acquisition of the 75% participation, as well as any subsequent transfer. The 75% criterion corresponds to the notion of capital participation and not the notion of voting rights. Thus with respect to the 75% norm, the Belgian legislator unambiguously deviates from the definition given to the concept of exchange of shares by the EU Merger Directive.

(2) both the transferring as receiving company ought to have their place of effective management or their statutory seat in a EU member State.

(3) the transfer has to be compensated exclusively with newly issued shares or securities receiving company, possibly increased with a mark-up in cash up to 10% of the nominal value of the assigned shares

The formal conditions for a tax exemption are[123]:

(1) the deed of transfer needs to mention that the transfer resulted in the acquisition by the receiving company of at least 75% of the nominal capital of the transferring company.

[121] Y. BILLIET, 'Fusie à l'anglaise: de aanschrijving', *Fiscale Actualiteit* 1999, 27-29.
[122] Article 117, § 3, Belgian Registration Code.
[123] Article 117, § 3, Belgian Registration Code.

(2) an attestation of an auditor, confirming the attainment of the 75% criterion, has to attached to the deed of transfer.

All these conditions ought to be fulfilled no later than the moment when the deed is formally handed over. Otherwise the deed will be registered at the normal rate of 0,5%.

8. SPECIAL QUESTIONS

8. 1. SITUATION WHERE THE TRANSFEROR COMPANY POSSESSES OWN SHARES

65. If the acquired or split company has own shares, then these shares have to be destroyed for the purpose of the merger or division. These shares cannot be exchanged for shares of the acquiring or receiving company.[124] As a result, the blocked reserve accounts created by the acquired or split company perish and are not being transferred to the acquiring or receiving company.[125] If no reserve was created for these shares, the available reserves have to be diminished with the book value of these shares. Insofar this reduction originates from tax exempt reserves, taxation will occur. If no such reserves exist, that value will have to be deducted from the capital account.

66. The merger directive does not provide rules concerning the result achieved by the acquired company on own shares which are possessed by the acquired company.

8. 2. SITUATION WHERE THE TRANSFEROR COMPANY OWNS SHARES IN THE TRANSFEREE COMPANY - DOWNSTREAM MERGER

67. A merger by acquisition by which the transferor company owns shares in the transferee company causes the acquiring company to receive its own shares. The acquiring company reimburses all the transferred assets and liabilities of the transferor company with newly issued shares, including the shares held in the acquiring company.

68. Generally these 'own shares' are destroyed by the receiving company immediately after the tax exempted merger. As a consequence the positive difference, between the fiscal value of these 'own shares' and the paid-in capital corresponding to these shares, will be considered as dividends.[126] No

[124] Article 19, 2, Third European Directive
Article 703,§2 Belgian Company Code.
[125] Article 78, §3, 2° K.B. Belgian Company Code.
[126] Article 186 BITC.

withholding tax will be levied upon these dividends.[127] If this destruction of shares is completely assigned to previously taxed reserves, then the occurring dividend distribution will be compensated by a decrease of these taxed reserves and no corporate income tax will be due. In addition a taxed reserve is booked equivalent to the decrease of the fiscal capital representing the destroyed shares.[128] Consequently no taxable basis will arise due to the destruction of the own shares.

If the difference between the fiscal value of the 'own shares' and the fiscal capital corresponding with these shares is negative, no dividend is considered to be distributed. When the destruction of shares is assigned to the previously taxed reserves and a taxed reserve is booked equivalent to the decrease of the fiscal capital representing the destroyed shares, an increase in reserves will arise.

If the destruction of the shares corresponds with a reduction of the tax exempted reserves, a taxable base will appear to that extent.

69. When the shares are not immediately destroyed after the merger, a special reserve has to be created for these shares. Twelve months after the merger the acquiring company can maximally posses an amount of own shares of which the total nominal value does not exceed 10% of the fiscal value of the capital after those twelve months. The amount of shares above the 10% criterion has to be sold within that twelve month period.[129] Legal doctrine has however accepted that these excess hares (or all received shares) can be destroyed.

70. The Merger Directive does not regulate the situation where the transferor company realises a result on the shares that it possesses of the acquiring company.

8. 3. MERGERS, DIVISIONS AND EXCHANGE OF SHARES WHERE THE TRANSFEREE COMPANY OWNS SHARES IN THE TRANSFEROR COMPANY

71. According to the Belgian corporate tax code a transferee company cannot issue new shares in exchange for its participation in the transferor company.[130] This implies that the whole transfer will not be compensated by newly issued shares. Part of the transfer will be compensated by the disappearance of the share participation of the transferee company in the capital of the transferor. The assets and liabilities of the transferor company are reduced for the amount of the participation that the receiving company

[127] Article 264, first paragraph, 2° BITC.
[128] Article 188 BITC.
[129] Article 622, §2, second paragraph, 4°, Belgain Company Code.
[130] Article 703, §2 and 740, §2, Belgian Company Code.

possesses.[131] This reduction is done proportionally to the paid-in capital on the one hand and the reserves on the other hand. The reduction of the reserves will first be allocated to the already taxed reserves. If these reserves are insufficient then the reduction of the equity of the transferor company will be allocated to tax exempt reserves[132] and taxation will take place.[133]

This proportional rule is not applied when the merger is not fully compensated with shares by reason of a mark-up in cash. In this case the reduction originates first from the taxed reserves, then the tax exempted reserves and finally from the paid-in capital.[134]

72. The situation in which the receiving company has a participation in the transferring company before the reorganisation is dealt with in the Merger Directive. Where the receiving company has a holding in the capital of the transferring company, any gains accruing to the receiving company on the cancellation of its holding shall not be liable to any taxation. The Member States may however derogate from this rule where the receiving company's holding in the capital of the transferring company does not exceed 25 %.[135] (*cfr. infra* no. 81)

8. 4. THE ANTI-ABUSE CLAUSES AND THE RE-CHARACTERIZATION OF MERGER TRANSACTIONS

73. A tax motivated merger may face the obstacle not only of the ‘legitimate needs’ requirement of article 211 but also of article 344 §1 of the Income Tax Code. That article provides that the tax authorities can re-characterize a transaction, or an integrated series of transactions, where the characterization given by the parties had a tax avoidance motive, unless the parties can justify their characterization by ‘legitimate needs of financial or economic character’.[136] It is, however, difficult to conceive of a situation

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[131] TH. BLOCKERY & J.P. LYCOPS, “Fusie en splitsing van vennootschappen”, *A.F.T.* 1993, 276.

[132] Article 211, §1, 1° BITC states however that taxation never takes place for the capital gains in article 44, §1, 1° and article 47 BITC, for the capital gains realised through the reorganisation and for capital subsidies in article 362 of the Belgian Income Tax Code which are not yet indicated as profits at the moment of the transaction.

[133] C. AMAND, M. DE MUYNCK, G. DE NEEF, *Overdracht van ondernemingen,* Larcier, 1999, 359.

[134] C. AMAND, M. DE MUYNCK, G. DE NEEF, *Overdracht van ondernemingen,* Larcier, 1999, 361.

[135] Article 8 European Merger Directive.

[136] It should be noted that the ‘legitimate needs’ test of a Articles 211 and 344 §1 differ in that: (a) In article 211 the test applies to the operation itself (i.e. the merger or division) whereas in article 344 §1, the test applies to the characterization given by the parties to an operation or a series of operations. (b) In article 211, the burden of proof is on the taxpayer to establish that the test is met, whereas in article 344 §1, the tax authorities first have the burden of proof of establishing that the operation or operations are tax motivated, and the taxpayer then has the burden of proof of justifying its characterization of the operation or operations under the ‘legitimate needs’ test. [J.

where article 344 §1 would be invoked. Article 211 should be sufficient to resolve the issue, and it is difficult to see how the merger or division could be re-characterized except as a liquidation, which is the result of disqualifying the operation under article 211. However, one of the principal purposes of article 344 §1 is to permit a step transaction analysis of integrated transactions, and article 344 §1 may therefore be invoked where the merger or division is merely one part of an integrated series of transactions.[137]

74. The 'legitimate needs' test of article 211 and article 344 §1 can both be viewed as legislative reactions to the victory before Belgian courts of the principle that a taxpayer is free to choose the transaction(s) which have the most favourable tax consequences for him over the efforts of the Belgian tax Administration to attack tax motivated transactions.[138] Until the introduction of the general anti-abuse income tax statute by the Law of 22 July 1993, the legal world of the Belgian tax planner was reasonably simple and liberal. A tax saving structure was either legal tax planning – being an application of taxpayer's free choice of the least taxed route – or it was illegal – being an ordinary violation of the Belgian tax law or a sham (simulation).[139] Illegal sham thus traditional constituted the only general limitation to tax avoidance.

The world of the Belgian tax planner became even better when the Supreme Court, in its decision of 6 June 1961 in the *Brepols case*, provided a strictly legalistic and conservative interpretation to illegal sham:

"There is no illegal sham vis-à-vis the tax authorities, and therefore no tax fraud, when the parties, in order to achieve a more favourable tax treatment and using their freedom of contract without infringing the law, accomplish acts of which they assume all legal consequences, even if the form which they choose for such acts would not be the most common one."

This interpretation was confirmed and further articulated in subsequent case law of the Supreme Court.[140] The taxpayer's victory can best be illustrated by quoting from the decision of Belgium's highest court in the *Au Vieux Saint Martin* case decided in 1990:

"There is neither prohibited simulation with respect to the fiscal or tax fraud when, for purposes of benefiting from a more favourable tax regime, the

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STURTEVANT, "Tax Free Mergers and Divisions: The business Purpose" Test under Belgian Tax Law', *Intertax* 1994, 506.]

[137] J. STURTEVANT, "Tax Free Mergers and Divisions: The business Purpose" Test under Belgian Tax Law', *Intertax* 1994, 506.

[138] J. STURTEVANT, "Tax Free Mergers and Divisions: The business Purpose" Test under Belgian Tax Law', *Intertax* 1994, 506.

[139] L. HINNEKENS, "Tax avoidance in Belgium", *European Taxation* 1999, 95.

[140] Its most outspoken decisions were those of 27 February in the case of *Maas International* and of 29 January in *Mortsels Accountants Kantoor*. [L. HINNEKENS, 'Tax avoidance in Belgium', *European Taxation* 1999, 95.]

parties, using their freedom to contract without however violating any legal obligation, enter into transactions for which they accept all of the consequences, even if these transactions are accomplished for the sole purpose of reducing taxes." [141]

75. The new anti-abuse provisions in the Belgian Income Tax Code differ greatly from this former legal doctrine, to which they were a reaction (*cfr. Supra* no. 74). The statute provides for a number of specific anti-avoidance measures which limit the scope of the taxpayer's free choice of the least taxed route[142]. Contrary to the new anti-abuse articles, according to the doctrine illegal sham is not dependent on the intention of the parties but on the objective test of the true or untrue nature of the transaction; this true nature referred to legal truth and not to economic reality. On the contrary, article 344 §1 explicitly mentions the tax-motivated intentions of the parties as the principal argument for exemption of tax relief. The articles 211 and 344 §1 both refer to the 'legitimate needs of a financial or economic character'.

There have been practically no cases clarifying the meaning of the terms 'legitimate needs of a financial or economic character' used in article 211. Their obvious purpose is to require a non-tax motive, but that concept could be better expressed.[143]

76. It has been suggested that the 'legitimate needs' test of article 211 should be interpreted to have the same meaning as the provision of the Directive[144]. However, textually, there is an important difference between the Directive and the provision in article 211. The Directive requires that there be a tax avoidance motive and then creates a presumption that such motive exists if there is no valid economic reason for the transaction.[145] Article 211 requires a legitimate economic reason for the transaction, whether or not tax avoidance is involved. This leaves open the possibility that favourable tax treatment will be denied even though the transaction is not tax motivated. On the other hand, if the transactions is tax motivated, one could argue that the 'legitimate needs' test is met when a – secondary – economic reason is present. But this argument has little chance of being accepted. The Belgian legislative history indicates that tax avoidance must be the exclusive motivation to exclude tax free treatment, thus implying that a secondary economic motive will be sufficient to preserve tax free treatment.[146] Moreover, we feel that there can only be one true purpose of a transaction, tax-motivated or economic.

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[141] Cass. 22 March 1990 (*Pas, I, 853*).
[142] Articles 46(1)(2), 211, 54, 207, 344 §1 and §2 BITC
[143] J. STURTEVANT, "Tax Free Mergers and Divisions: The business Purpose" Test under Belgian Tax Law', *Intertax* 1994, 507.
[144] J. KIRKPATRICK, *Le régime fiscal des Sociétés en Belgique,* Première Partie, Chapter II, Bruylant, 1992, 33.
[145] Article 11 (1) (a), European Merger Directive
[146] J. STURTEVANT, "Tax Free Mergers and Divisions: The business Purpose" Test under Belgian Tax Law', *Intertax* 1994, 508.

Such an interpretation would be contrary to the legislative history of the 'legitimate needs' test in article 211. In first introducing that test for mergers and divisions, the government stated to the Parliamentary Commission considering the bill that the test was founded on article 11(1)(a) of the Directive, that it would not have the effect of making the tax authorities the censors of the soundness of economic decisions, and that the text of the bill was only intended to refuse the benefit of tax exemption with respect to operations the clear objective of which is tax avoidance. The same assurances were given by the government to Parliament in connection with the bills establishing the same test in the same language for tax free assets transfers.[147] It is to be hoped that the tests will only be used in conformity with the governments repeated assurances to the legislature.

77. The interpretation of the general anti-abuse rule of article 344 §1 is still uncertain. The controversy will continue to exist until legal practice has clarified it, which is not expected to happen in the first years to come.[148] In any event, one or the principal problems which will surely be involved in the application of article 211 is whether the benefits of tax exemption will be denied in circumstances where there are mixed tax and economic reasons for carrying out the merger or division. In each case, the question will be whether the tax reason or the economic reason was the principal motivation for the transaction.[149]

At least three interpretations are being proposed.[150] In order of being more stringent:

Transactions are re-characterized as soon as their is a discrepancy between its form and the economic reality. This interpretation will maximize the effectiveness of the tax rule. Being maximalist, this interpretation is favoured by many tax inspectors.
The second interpretation is that of abuse of legal form or *fraus legis* in Dutch doctrine. It permits a reclassification of the documented transaction into another transaction that it would frustrate the object and purpose of the tax law if it were not taxed accordingly. This strikes a balance between tax effectiveness on the one hand, and the rule of law and of strict interpretation on the other hand.
According to the third interpretation, the change does not relate to the act or transaction as such, but to its legal characterization which may always be replaced by another legal characterization of the same act or transaction. It

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[147] *Contra* J. STURTEVANT, "Tax Free Mergers and Divisions: The business Purpose" Test under Belgian Tax Law', *Intertax* 1994, 507.
[148] L. HINNEKENS, "Tax avoidance in Belgium", *European Taxation* 1999, 96.
[149] J. STURTEVANT, "Tax Free Mergers and Divisions: The business Purpose" Test under Belgian Tax Law', *Intertax* 1994, 508.
[150] L. HINNEKENS, "Tax avoidance in Belgium", *European Taxation* 1999, 96.

follows that the statute can only be applied when at least two alternative legal characterizations are available for the same transaction, which situation is extremely exceptional in the legal world. This interpretation is minimalist in its effects and favored by many tax lawyers.

9. IMPLEMENTATION OF THE MERGER DIRECTIVE IN BELGIAN CONTEXT

78. In order to be in agreement with the merger Directive some changes to the Belgian tax law will have to be made. In the foreseeable future the Belgian Income Tax Code will enable cross-border mergers and divisions to take place. The Belgian tax rules which are inconsistent with the concept of a Societas Europeae will have to be modified. The most crucial amendment will be the one of article 211, §1, second paragraph, 1° of the Belgian Income Tax Code which states that a tax exempted merger/division is only possible if the acquiring company is a Belgian one.[151] The existing tax exemption regime for domestic mergers and divisions will be extended to the situation where a Belgian company is acquired by a EU company by way of merger or division.[152,153] In addition, the condition which states that the realization of the merger/division must be in accordance with Belgian Company Code will be extended.[154] Hence, the exemption regime will also be valid when the transaction occurs according to equivalent rules of the company law of the EU member state where the acquiring or receiving company resides.[155] The ultimate condition which requires that the motives of the merger/division should be of a financial or economic nature will remain unchanged. Question is, since we have a European anti-abuse rule, do we still need national anti-abuse rules?

9. 1. DISCREPANCY BETWEEN BELGIAN LEGISLATION AND THE MERGER DIRECTIVE

79. The Merger Directive gives the tax payers the option to make use of the regime of tax deferral.[156] According to the Belgian regime (so far only applicable to domestic mergers/divisions) the tax exemption is automatically

[151] TH. BLOCKERY & J.P. LYCOPS, "Fusie en splitsing van vennootschappen", *A.F.T.* 1993, 212.
[152] C. VANDERMEERSCHE, "Worden ook grensoverschrijdende fusies en splitsingen neutraal?", *Fisc. Act.*, 2001, 43/3.
[153] Analogously the article about transfer of losses will have to be modified in the Belgian Income Tax Code by extending its applicability to a cross-border situation (Article 206, paragraph 3 BITC)
[154] Article 211, §1, second paragraph, 2°, BITC.
[155] C. VANDERMEERSCHE, "Worden ook grensoverschrijdende fusies en splitsingen neutraal?", *Fisc. Act.*, 2001, 43/3.
[156] Article 3 (2), European Merger Directive.

applicable as soon as the three relevant conditions are fulfilled (*cfr. supra* no. 30).[157] An important remark is however that, even if the merger/division fulfils all three conditions of the exemption regime, the merger/division will still be subject to effective taxation if, and to the extent that, the transfer is not exclusively compensated with shares.[158]

80. The Merger Directive allows a mark-up in cash (up to 10%) in the name of the shareholder receiving the cash payment.[159] According to Belgian legislation the additional cash payment brings about taxation on behalf of the acquired company on the subject of paid capital and reserved profits.[160]

81. The first part of article 7 of the merger directive states that, where the receiving company has a holding in the capital of the transferring company, any gains accruing to the receiving company on the cancellation of its holding shall not be liable to any taxation. Belgian tax law is not in accordance with this rule and needs a dual change with reference to the capital gains that arise due to the cancellation of the shares at the moment of the merger.

The capital gains realized by the acquiring company is the positive difference between the fiscal value of the shares of the acquired company (possessed by the acquiring company) and the net transfer value represented by those shares. This positive difference (capital gain) is treated for tax purposes as following:

- The fraction of the capital gains that will be taxed as a dividend on behalf of the acquired company, will theoretically qualify for participation exemption[161] on behalf of the acquiring company.[162] This rule implies that a tax free merger will not always be fully tax exempted on behalf of the acquiring company. The participation exemption (of 95% of the amount of the gross dividend) implies that 5% of the capital gains will be taxed.[163] This rule is thus in conflict with the merger directive which states that any gains accruing to the receiving

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[157] D. BEECKMAN, D. PIENS, W. VANDENBERGHE, E. DE LEMBRE, *Van ontbinding tot fusie*, ced.samsom, 1999, 386.
[158] J.-P. LAGAE, *De nieuwe fusiewetgeving 1993; 'Fusies en splitsingen – Fiscaal regime – Algemene bespreking'* Kalmthout, ,Biblo, 1994, 135.
[159] Article 8 (4), European Merger Directive.
[160] Article 211, §2, BITC.
[161] In order to avoid double taxation of dividend income (once on behalf of the issuing company and once on behalf of the receiving company) the Belgian income tax code provides a so-called DBI-deduction. This implies that under certain conditions and up to a certain threshold (95%) these dividends income will be deducted from the taxable base. [J.-P. LAGAE, *Vennootschapsbelasting*, Diegem, Ced.Samsom, 1998, 53]
[162] TH. BLOCKERY & J.P. LYCOPS, "Fusie en splitsing van vennootschappen", *A.F.T.* 1993, 213.
[163] C. VANDERMEERSCHE, "Worden ook grensoverschrijdende fusies en splitsingen neutraal?", *Fisc. Act.*, 2001, 43/1.

company on the cancellation of its holding shall not be liable to any taxation.[164]
The residual fraction of the capital gain that is not taxed as a dividend is deemed to be a no-realized capital gain[165], which will be exempted from tax if the 'condition of unavailability' is fulfilled.[166] This fraction of the capital gain will become taxable as soon as the condition of blocked reserve account ceases to be fulfilled or at the latest when the acquiring company is liquidated. This provisional tax exemption should be converted in a final tax exemption to be in compliance with the merger directive.[167]

82. According to the Merger Directive member states do not have to grant a tax exemption for a reorganization if there exists a presumption that the operation has tax evasion or tax avoidance as its principal objective or as one of its principal objectives.[168] According to Belgian legislation the motive of the reorganization should be of a financial or economic nature.[169] The question to which extent this 'legitimate needs' test of article 211 should be interpreted to have the same meaning as the provision of the Directive has been examined above. (*cfr. supra* no. 33 and 76)

10 CONCLUSION

83. For decades the Belgian merger legislation has been fairly stable. Since the nineties however, things have changed. After a conviction of the European Court of Justice, the Belgian legislator has finally implemented the third and sixth EU Directive regarding domestic mergers and divisions. With these Directives, the EU Council expressed its will to harmonize merger & acquisition legislation[170]. On 23 July 1990 the Council has accepted the Merger Directive 90/434/EEG. Again, the purpose was to avoid fiscal constraints in transnational reorganizations and to strive for a uniform law on cross-border reorganisations. The preamble of the Directive states that it is not possible to attain this objective by an extension at the Community level of the systems presently in force in the Member States, since differences between

[164] Belgian tax law is only in conflict with article 7 of the Merger Directive when the acquiring company cancels a holding of more than 25% in the acquired company. The member states may derogate from the Merger Directive where the receiving company's holding in the capital of the transferring company does not exceed 25%.
[165] Article 45, BITC.
[166] C. VANDERMEERSCHE, "Worden ook grensoverschrijdende fusies en splitsingen neutraal?", *Fisc. Act.*, 2001, 43/1.
[167] TH. BLOCKERY & J.P. LYCOPS, "Fusie en splitsing van vennootschappen", *A.F.T.* 1993, 215.
[168] Article 11 (1) (a), European Merger Directive.
[169] Article 211, §1, second paragraph, 3°, BITC.
[170] T. TILQUIN, *Traité des Fusions et Scissions,* Brussel, Kluwer Editions Juridiques, 1993, V.

these systems tend to produce distortions.[171] The Council of the European communities believes that only a common tax system is able to provide a satisfactory solution in this respect.[172] The Merger Directive forced member states to modify domestic legislation so that cross-border reorganizations could occur under the tax exemption regime at least before 1 January 1992.

84. In the light of these events, it seems unacceptable that cross-border reorganizations are still not possible in Belgium. On the grounds of article 211 of the Belgian Income Tax Code, it is impossible for cross-border mergers/divisions to qualify for a tax-relief. From the last update of Belgian corporate legislation, the underlying argument for this has lost most of its strength. After all, the concept of nationality constitutes no more hindrance for cross-border transactions because nationality does no longer represent an essential element of a company. Ever since, cross-border mergers are technically possible. Recently a proposal of law was made for the further implementation of the Directive, in order to change article 211. That's why it is most likely that very soon cross-border mergers will be perfectly, legally possible.[173]

85. After settlement of the tenth Directive the Member States will be obliged to regulate the legal form of a cross-border merger/division in their national legislation. If the tenth EU Directive would not be implemented, than the realization of the cross-border merger/division according to the rules of the Societas Europeae could be the second best alternative.[174] This structure will sometimes not be the most preferred one, because the Merger Directive states that the transferring company has a permanent establishment in the state where the transferred company was located. But a SE often tries to locate operational activities in one single country. A SE thus causes the opposite problem: according to the Belgium Income Tax Code it is perfectly acceptable, but from the fiscal point of view one should be aware that a permanent establishment is required in the state of the acquired company, to enjoy relief from taxation.

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[171] D. BEECKMAN, P. DAMIEN, W. VANDENBERGHE, E. DE LEMBRE, *Van ontbinding tot fusie,* Diegem, ced. samsom, 1999, 362.
[172] See preamble of the Merger Directive p1.
[173] B. PEETERS and M. OLISLAEGERS, "De Europese Naamloze Vennootschap (SE): Een nieuwe vennootschapsvorm met een Europees en nationaal karakter", *T.F.R.* 2003, Gent, Larcier, 164-165.
[174] G. VAN SOLINGE, *Grensoverschrijdende juridische fusie*, Kluwer, 1994, 336.