

## Brazil Desk Email Bulletin

*This email bulletin is issued by the Brazil Desk of Loyens & Loeff. It is intended to provide you on an ad hoc basis with news flashes or background information on topical corporate, finance and tax law issues in the Benelux.*

### Year End Tax Bulletin: Belgium

#### Content:

- Administrative Circular on ECJ's Cobelfret Case
- Maximum rate of notional interest deduction
- Protocol to the UK-Belgian Tax Treaty

#### Administrative Circular on ECJ's Cobelfret Case

On 12 February 2009, the European Court of Justice ("ECJ") rendered its decision in the Cobelfret case (C-138/07) on the Belgian dividend participation exemption regime. Belgian legislation provides that dividends received by a parent company from its subsidiary are first included in the taxable basis of the parent company and are subsequently deducted from this taxable basis up to 95% (Dividend Received Deduction or "DRD"). However, this DRD is limited to the positive taxable base of the parent company after deduction of the other exempted profits or deductible costs. Article 4 (1) of the EU Parent-Subsidiary Directive leaves the Member States the choice between the exemption method and the credit method to prevent economic double taxation of dividends. By implementing the dividend participation exemption regime, Belgium opted for the exemption method. However, the Belgian system of the dividend participation exemption regime only allows a parent company to benefit from a full exemption if it has neither realised any losses nor borne deductible costs exceeding 5% of the dividend received during the same tax period. As the Member States cannot unilaterally introduce restrictive measures, the ECJ decided that the Belgian participation exemption regime was not compatible with the terms and objectives of the EU Parent-Subsidiary Directive.

In a response to this ruling, the Belgian tax administration sets out its interpretation of the Cobelfret case in an administrative circular published on 29 June 2009:

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Loyens & Loeff is an independent Benelux law firm with over 900 lawyers and offices in the main financial centres around the world. Loyens & Loeff combines an integrated corporate law, regulatory and tax practice.

In order to be able to give the best advice possible to our clients, Loyens & Loeff formed the Brazil Desk.

The members of the Brazil Desk strongly focus on Brazilian clients that invest or trade in Europe or other regions, as well as on international companies and financial institutions that want to expand their businesses to Brazil. In many cross border (including cross Atlantic) transactions, benefits can be derived by investing through the Benelux (Belgium, Netherlands and Luxembourg).

The team comprises members from various Loyens & Loeff practice groups. Members of the Brazil Desk visit Brazil three to four times a year.

Members of the Brazil Desk speak the Portuguese language.

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- The “unused DRD” can now be carried forward to subsequent tax periods. At the moment the taxpayer makes use of it by offsetting taxable profits, it has to demonstrate that, at the time this “unused DRD” was built up, it met all legal requirements to benefit from the participation exemption for dividends received.
- The circular also specifies that the “unused DRD” to be carried forward has a specific nature, different from the carry forward tax losses. In other words, this “unused DRD” is not subject to the limitations set forth in the Income Tax Code with respect to carry forward tax losses, e.g. corporate reorganisations and change of control.
- The “unused DRD” to be carried forward in principle only concerns the dividends distributed by companies located at the time of the distribution in the EU (including Belgium) or - since 1994 - in the EEA.

### **Maximum rate of the notional interest deduction**

The Notional Interest Deduction regime entitles Belgian companies and establishments to annually calculate a deemed interest expense on their aggregate (adjusted) equity amount, reducing their taxable basis accordingly. The exact amount of the deductible interest expense results from applying an interest rate to the adjusted base amount. This interest rate corresponds to the interest rate for 10-year government bonds. As part of the State Budget for 2010, the Minister of Finance has proposed fixing the maximum rate of the notional interest deduction at 3.8% for the financial years 2010 and 2011 (4.473% for 2009). For small businesses, this rate would be increased by 0.5%. This measure confirms once again that it is not the intention of the Government to fundamentally change the Notional Interest Deduction regime.

### **Protocol to the UK-Belgian Tax Treaty**

On 24 June 2009, the UK and Belgium signed a Protocol to the 1987 UK-Belgian Tax Treaty (the “**Protocol**”). The Protocol has not yet entered into force. One of the interesting features of this Protocol is that the current Article 11 of the treaty (on interest) is deleted and replaced by a completely new provision. The new Article 11 provides an exemption from withholding tax on interest paid on a loan of any nature granted or a credit extended by an enterprise to another enterprise (compared to the current limit of 15%).

Another interesting feature of this Protocol is certainly to treat the “pension schemes” as resident of the Contracting State where they are established. The Protocol defines a “pension scheme” as any plan, scheme, fund, trust or other arrangement established in a Contracting State, to the extent that it is operated to administer or provide pension or retirement benefits or to earn income for the benefit of one or more such arrangements and provided that this “pension scheme” is:

- in the case of Belgium, an entity, including pension funds, or a pension scheme arranged through an insurance company, organised under Belgian law and regulated by the Banking, Finance and Insurance Commission or registered with the Belgian tax administration; or
- in the case of the United Kingdom, a pension scheme (other than a social security scheme) registered under Part 4 of the Finance Act, including pension funds or pension schemes arranged through insurance companies and unit trusts where the unit holders are exclusively pension schemes.

In the case of Belgium, the Pension Vehicles (organismes de financement de pensions / organismen voor de financiering van pensioenen) shall therefore qualify as “pension schemes” and thus as Belgian residents for the purposes of the Tax Treaty.

Finally, the Protocol also amends the exchange of information clause in order to bring it in line with the current OECD model.

We trust to have fully informed you. Should you have any questions, please do not hesitate to contact us.

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