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Belgium Requests CJEU Ruling on Write-Down of Shares

by Marc Quaghebeur

Marc Quaghebeur is a partner with Cabinet David in Brussels.

In this article, Quaghebeur examines *Bech NV*, a case involving the Belgian tax authorities' denial of a deduction for a reversal of write-downs that the taxpayer recorded before transferring to Belgium from Luxembourg.

On June 25 the Belgian Supreme Court issued a decision requesting a preliminary ruling from the Court of Justice of the European Union on the compatibility of the Belgian tax rules with the freedom of establishment.[1] The case relates to write-downs on shares recorded before a company transferred its registered office to Belgium and the reversal of those write-downs upon arrival in Belgium.

Background

The taxpayer, Bech NV (currently VP Capital), is the parent company of a Dutch company, VP Exploitatie NV, the investment vehicle of a Dutch family. The parent company was incorporated in Luxembourg in 1995. Its shareholding in VP Exploitatie NV was recorded in its accounts with an acquisition value of €249,011,513.99.

In 2008 the taxpayer sold 60 shares in the Dutch entity for €7,001,260.93 and recorded a write-down of €59,083,453.05 on the remaining participation. The following year — before moving its registered office to Belgium — it recorded a further write-down of €26,339,800, leaving the shares with a book value of €156,587,000 in the taxpayer's last financial statements in Luxembourg, which were dated April 30, 2009.

The taxpayer also held other participations in financial institutions and holding companies on which it took another write-down of €1,685,993. In its Luxembourg tax returns, the company added write-downs totaling €87,109,246.05 to its tax losses, resulting in a loss carryforward of €89,587,962.96.

On May 1, 2009, Bech NV transferred its registered office to Belgium and did not keep a permanent establishment in Luxembourg. Based on article 206, section 3 of Belgium's Income Tax Code 1992 (ITC), the company was not allowed to deduct the losses it had carried forward from Luxembourg against its Belgian taxable profits. It reversed part of its write-downs, amounting to €43,478,500 on the shares of VP Exploitatie NV and €497,833.94 on the other investments.

The Dispute

The Belgian tax authorities took the position that the reversal of the write-downs was liable to corporate income tax. It reasoned that because the write-downs had been tax-deductible costs in Luxembourg, the company was not entitled to the exemption for reversals of write-downs on shares.

Article 74, section 2, 1° of the royal decree implementing the ITC exempts the reversal of write-downs by allowing a deduction of the write-downs from the taxable reserves if the write-downs have not been deducted as business expenses under article 198, section 1, 7° of the ITC. Article 198 of the ITC provides that write-downs and capital losses on shares are usually not tax-deductible business expenses, although there are some exceptions.

The company argued that it could increase the book value of the participations at the time of the transfer to Belgium and that this reversal was not liable to tax.

The Belgian tax authorities responded that when an overseas company transfers its

[1] *Bech NV v. Belgian State*, F.19.0132.N (2021).

headquarters, main place of business, or executive or administrative office to Belgium, capital gains or losses on the assets allocated to its overseas establishment and on any assets that it owns abroad are determined based on their book value at the time of the transfer in accordance with article 184-*ter*, section 2 of the ITC.[2]

Article 44, section 1, 1° of the ITC provides that capital gains that are expressed but not realized are tax exempt. However, article 190 of the ITC clarifies that this capital gains exemption applies only if the gains are recorded and maintained on a separate equity account on the balance sheet that is unavailable for distributions. Because the company had not recorded the capital gain accordingly, the authorities maintained their position that the reversal was taxable.

The Rulings

Court of First Instance and Court of Appeal

The company contested the taxation before the Antwerp Court of First Instance and before the Antwerp Court of Appeal.

Before the court of appeal, the company issued a writ of summons against its Dutch tax advisers, PricewaterhouseCoopers Belastingadviseurs NV, and its Belgian tax advisers and chartered accountants, Ernst & Young Tax Consultants and Ernst & Young Bedrijfsrevisoren BV CVBA, which had advised and assisted the company with legal and tax issues regarding the restructuring and the transfer of its registered office to Belgium. The purpose of that writ is to oblige third parties (the defendants in the writ process) to intervene in the procedure. This ensures that any decision is binding on those third parties, and they cannot later claim that the decision was not res judicata as far as they are concerned. The intervention is not intended to condemn the third party but rather to extend the effect of res judicata for any decision in the underlying case to the third parties, which may be interested parties or the potential subjects of a subsequent claim based on the court decision.

The Antwerp Court of Appeal confirmed the position of the Belgian tax authorities.[3] The court held that the book value of the participation could not be increased retroactively when the company transferred its residence to Belgium. A decisive factor was that Luxembourg law — unlike Belgian law — does not disallow write-downs of participations as deductible business expenses.

The reversal of the write-downs constituted an expressed but not realized capital gain, which would normally be tax exempt. However, because the gains were not recorded in a separate equity account on the balance sheet that was unavailable for distributions, the company was not entitled to the exemption.

The court also rejected the taxpayer's argument that because the write-downs had taken place before the transfer of the company to Belgium, the taxation of their reversal was incompatible with the freedom of establishment set forth in article 49 of the Treaty on the Functioning of the European Union.

Supreme Court

The Belgian Supreme Court observed that the reversal of the write-downs, which had been recorded in Luxembourg, after the transfer of the registered office to Belgium constituted the realization of a capital gain within the meaning of article 184-*ter*, section 2, 2° of the ITC. Therefore, the realized capital gain must be based on the book value that the assets had when the registered office transferred to Belgium. It was irrelevant to the Supreme Court that the gain was not effectively realized and had not been received at that time. The Court found that for Belgian tax purposes, the reversal of the write-downs must be regarded as an expressed but not realized gain in the sense of article 44, section 1, 1° of the ITC. Thus, the capital gain could be exempt only if it was recorded in a separate equity account on the balance sheet.

The Supreme Court then examined the taxpayer's claim that this Belgian legislation is not

[2] In 2019 the text of article 184-*ter*, section 2 of the ITC was amended to refer to the "real value" — that is, the market value — of the assets rather than their book value. Corporate Tax Reform Act of Dec. 25, 2017, implementing Council Directive (EU) 2016/1164 laying down rules against tax avoidance practices that directly affect the functioning of the internal market.

[3] Antwerp Court of Appeal, *Bech NV v. Belgium*, 2016/AR/2064 (2018).

compatible with the freedom of establishment enshrined in article 49 of the TFEU.

The taxpayer argued that the obligation to record capital gains in a separate equity account on the balance sheet to benefit from the exemption implies that the gains cannot be distributed or added to a statutory reserve, and the gains may not be used for the calculation of a remuneration or allocation.

The write-downs of shares were recorded when the company was established outside Belgium, and they were not deducted because the company was loss-making at that time. Thus, the taxpayer argued and the Supreme Court agreed that the restrictions regarding the obligation to record and maintain the gain from the reversal on a separate account constitute a restriction of the freedom of establishment.

These restrictions do not apply to Belgian companies that reverse a write-down of shares under Belgium's ITC. Because Belgian companies do not have to book the increases in value, which lie behind the reversals, to an unavailable equity account — although the write-downs must not have previously been deducted from the Belgian taxable result — the Court found discrimination existed.

The question becomes whether the CJEU's judgment in *AURES Holdings*[4] applies to this situation. In *AURES Holdings,* the Court held, *inter alia*, that article 49 of the TFEU must be interpreted as meaning that a company incorporated under the laws of one member state that transfers its place of effective management to another member state without that transfer affecting its status as a company incorporated under the laws of the first member state may rely on article 49 of the TFEU to contest the second member state's refusal to defer losses incurred before that transfer.

The taxpayer also argued that *AURES Holdings* is incompatible with the CJEU's judgment in *Bevola*.[5] In that case, the CJEU held that the freedom of establishment precludes legislation of a member state under which it is not possible for a resident company that has not opted for an international joint taxation scheme to deduct from its taxable profits the losses incurred by a PE situated in another member state when there is no longer any possibility to take those losses into account in the other country.

The Belgian Supreme Court decided to stall the proceedings and seek a preliminary ruling from the CJEU on the following question:

> Does freedom of establishment, as guaranteed by Article 49 TFEU, preclude national legislation, such as that at issue here, where it results in a Luxembourg company which records write-downs on shares in Luxembourg and which, although deducting those write-downs in principle from its taxable income, cannot actually deduct them from its taxable income because of the existence of a tax loss position, being taxed on the write-back of those write-downs in Belgium following the transfer of its registered office to Belgium, unless the increases in value masked by that write-back are allocated to a liability account not available for distribution, whereas a Belgian company which has recorded write-downs on shares in Belgium is not taxed on the write-back of those write-downs, provided that the write-downs had not been previously deducted from its Belgian taxable income, without needing to allocate the increases in value masked by that write-back to a liability account not available for distribution?[6] ■

[4] *AURES Holdings AS v. Czech Republic*, C-405/18 (CJEU 2020).

[5] *A/S Bevola, Jens W. Trock ApS v. Denmark*, C-650/16 (CJEU 2018). For discussion, see Tom O'Shea, "CJEU Says Denmark Must Grant Loss Relief for Final Cross-Border Losses," *Tax Notes Int'l*, Nov. 26, 2018, p. 911.

[6] Belgian Hof van Cassatie, Request for a preliminary ruling in *VP Capital NV v. Belgische Staat*, C-414/21 (July 7, 2021).