

Modifications to the Belgian Stock Option Regime: Practical Issues

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The Act of 24 December 2002 has modified provisions of the 1999 Belgian tax regime for stock options granted under an employee stock option plan (ESOP). (For prior coverage, see *Tax Notes Int'l*, 6 Jan. 2003, p. 20, 2002 WTD 247-2 [📄](#), or *Doc 2002-28005 (3 original pages)* [\[PDF\]](#).) These modifications were necessary because the new tax regime did not account for the possibility that the economic climate might deteriorate as much as it has in recent years.

Since the new tax regime was introduced by the Act of 26 March 1999, numerous stock option plans have been set up; over 60 percent of all listed Belgian companies have set up ESOPs for their employees. To minimise the income tax due, most of these plans were drafted so that the options were limited to five years and the beneficiaries would be unable to exercise their stock options before the end of the third calendar year following the year of the grant.

Under such a plan, the only tax due is the individual income tax due when the stock option is granted; the tax is calculated on a percentage of the value of the shares, which for most ESOPs is 7.5 percent. There is no further tax when the employee exercises his option or when he sells the shares. Moreover, no social security is due on this benefit.

When the employee exercises his option, he can realise a tax- exempt capital gain. There is only one snag: Without knowing if he will even make a profit, the employee must pay tax in advance at a marginal rate of about 53 percent on this fringe benefit, calculated in function of the current value of the current price of the stock.

In a bull market, granting stock options is tax-effective and can be very profitable for the employee. When stocks tumbled, it became apparent that the economy's possible deterioration had not been considered, and that the beneficiaries might not even be able to recover the tax they had paid when they were granted the stock options.

As most ESOPs were set up in 1999 and 2000, they will expire in 2004 or 2005. It would take a miracle for the stock market to pick up enough to make exercising the options worthwhile.

At the end of 2002, the legislation was patched up with the following measures:

- **Verbal offers of stock options are excluded.** To avoid any confusion, stock options can only be granted in writing.
- **The beneficiary must explicitly accept the extension.** Some employees, in particular when they were made redundant, felt that their employers had taken advantage of them. Many claimed that the stock options had been imposed on them and that they had not accepted them. Some even claimed damages from their employers to cover the loss they had

incurred, in particular the tax they had paid. Therefore, stock options must be accepted in writing by the beneficiary with effect from 10 January 2003.

- **Extension of the exercise period.** To give the stock market time to recover, ESOPs set up between 1 January 1999 and 31 December 2002 can be extended for a period of up to three years, even if that means the exercise period of warrants would exceed 10 years (which is, in principle, prohibited by article 499 of the Company Code). The grantor and the beneficiary of the stock option plan must agree to extend the period for exercising the option. It is specifically provided that such agreement would not constitute a grant of a new stock option. Indeed, under the existing legislation, the tax authorities tend to regard any change to the terms and conditions of an existing ESOP as the grant of a new stock option benefit that is liable to tax again.

The last measure, in particular, has raised a number of questions, as most ESOPs qualify under the legislation governing the public offering of securities. The Banking Commission issued a set of instructions on 4 March to ensure the market's transparency and the protection of the investors. The Belgian tax authorities also explained their view on the modifications in a 28 April administrative note.

Which ESOPs?

The tax authorities explain that ESOPs can only be extended if they are still current -- that is, their exercise period must not have lapsed, and the beneficiary may not have exercised his options yet.

Moreover, for practical reasons, they will accept that the exercise period can be extended for all ESOPs issued between 2 November 1998 and 31 December 2002. Because stock options are deemed to have been granted on the 60th day, stock options granted in the last 60 days of 1998 are deemed to have been granted in 1999 and had not been refused within 60 days.

The same rule applies to stock options granted in the last 60 days of 2002, even if they were only accepted in 2003.

Form of the Decision to Extend the Exercise Period

The Banking Commission distinguishes contractual stock options from stock options issued in the form of warrants.

For contractual stock options, the board of directors will have to make a formal decision for the extension of the exercise period.

Warrants are securities that represent a right to subscribe to a delayed capital increase. For those, the Banking Commission requires the board of directors to attach an explanation of the interest of the extension of the exercise period for the company (for example, an explanation that the employees are not able to exercise the warrants in due time and, therefore, the objectives of the ESOP (namely, motivation of the employees) will not be achieved).

In particular, the board of directors must be careful to justify only extending the exercise period for those employees who are liable for the Belgian individual income tax. In principle, this constitutes an infringement of the rules relating to the equal treatment of the owners of securities issued at the same occasion.

Formalities for the Employer

The Banking Commission suggests that the employer seek the approval of each individual beneficiary involved so that the refusal by one beneficiary would only affect his own situation. From a strictly legal point of view, even a tacit acceptance could be taken into account if it is undeniable. However, the commission recommends that the employer require a written acceptance within 60 days, with a presumption of refusal if the acceptance has not been given in writing.

Any ESOP that is offered to 50 or more beneficiaries is considered a public solicitation of investments and normally requires a prospectus or an addition to the prospectus. The commission notes that an addition to a prospectus is only required during the issue period, and a new prospectus must be published for a new issuance of securities. In the case of an extension of the exercise period, neither is required.

Although the employer must inform the beneficiaries, the Banking Commission need not approve the notice to the beneficiaries. Nevertheless, the commission appreciates being informed of such notices.

Finally, as the decision is relevant for the stock market, it must be made public. This can be done in the report of the board to the annual accounts.

The Beneficiary Must Have Accepted the Extension

The minister of finance had suggested before Parliament that this condition meant that all the beneficiaries had to approve the extension, preferably in one written and signed document.

The Banking Commission considered this condition to be too stringent. It suggested that the employer contact each of the beneficiaries directly to inform them of the suggested change, the corporate body that would enact the change, the justification and the tax implications, and how the beneficiary could approve the modification of the ESOP.

The tax authorities admit the employer only needs to seek the acceptance of those beneficiaries who are affected by the extension. He does not need to obtain the approval of all the beneficiaries of the ESOP. The fact that not all the beneficiaries have explicitly agreed cannot block the extension of the exercise period for those beneficiaries that have accepted in time.

Before 30 June 2003

The extension of the exercise period must be agreed before 30 June and notified to the tax authorities before 30 July. The information to be provided must include:

- a precise identification of the ESOP and all relevant information relating to the options granted (underlying shares, exercise price and period, and the major terms and conditions of the ESOP);
- the terms and conditions of the extension; and
- the identification of the beneficiaries for whom the ESOP has been extended.

The tax authorities confirm that it is the company that has offered the stock options that must notify the extension to its own tax office. A foreign company, without an establishment in Belgium, that has offered the stock options to the staff of its Belgian subsidiary must notify the extension to the subsidiary's tax office.

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