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Law & Tax

Weil

Tax in Distressed Situations

BELGIUM

GENERAL

1. Does debt have a specific meaning for tax purposes?

Debt is not separately defined for Belgian tax purposes, hence in principle the civil law definition prevails.

In the Belgian civil code, a loan is defined as a contract whereby one party (the lender) delivers to the other party (the borrower), either an asset (which the recipient can use under an obligation to return it after use) or a certain quantity of consumable goods (under the obligation for the lender to return the same quantity of goods of an equal type and quality).

By contrast, equity in the framework of a company contract is defined as a contribution of funds or assets with a view to sharing the profits (and losses) that may arise therefrom.

The main criteria used by the Belgian courts to decide whether an instrument should qualify as debt or equity are as follows:

- Debt obligation (loan/bond):
 - The holder is entitled to return of its investment after a specified period;
 - In most cases, the loan carries a predetermined, fixed return, which is not per se linked to the company's result;
 - In the event of the debtor's liquidation or bankruptcy, the investor ranks above the shareholders (i.e. has the right to be repaid before any funds are made available to shareholders).
- Equity:
 - Fully exposes the investor to the risk of the business (no assurance with respect to reimbursement of the original investment or the return);
 - The right to receive part of the liquidation surplus vests in its holders;
 - Provides shareholders rights to the investors (e.g. voting rights, rights of supervision, etc.).

Next to this, interest for Belgian (withholding) tax purposes is defined as "income from loans, including in rem security agreements, deposits and any other receivables". Absent a definition of "loan" under Belgian tax law, the qualification under Belgian civil law applies. Under Belgian civil law, a loan may arise when one party (the lender) makes available to another party (the borrower) capital, and is entitled to the repayment thereof. In other words, the qualification of a financial transaction as a loan requires the deployment of capital by the lender.

2. Do derivatives have a specific meaning for tax purposes?

The concept of a derivative is not expressly defined in Belgian tax law. Nevertheless, other administrative sources shed further light on the tax treatment of payments made under derivatives such as swaps or futures in Belgium.

The Belgian tax authorities are of the opinion that swaps essentially provide coverage against risks and future uncertainties such as interest rate fluctuations. As a consequence, the Belgian tax authorities deem that payments under swaps in principle do not qualify as interest for tax purposes (cf. supra). It is recognised that swaps are generally not entered into for the purpose of providing financing. It follows that payments under swaps not accompanied by a deployment of capital, cannot be considered interest payments given the absence of an underlying loan. Moreover, even in case (part of) the principal is transferred under a swap (as might be the case under foreign exchange swaps), the tax authorities take the view that the payments will not qualify as interest payments because it is generally not possible to determine accurately the amount of profit derived from swaps beforehand given the level of uncertainty. In this respect, swaps differ from loans, deposits and other receivables with the same nature as loans. The fact that payments under a credit default swap do not qualify as "interest" for Belgian withholding tax purposes is also confirmed by the Belgian ruling commission. However, in case of a "fake swap" (e.g. sale and repurchase contract over a fixed term with predetermined pricing), the Belgian tax administration takes the position that the realized surplus on the fake swap should be considered as interest.

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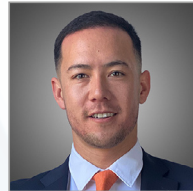
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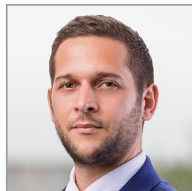
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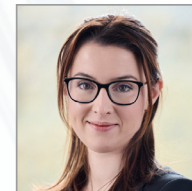
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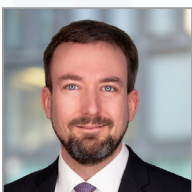
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