



Laga Newsflash

Legislator closes Cayman Tax Loopholes Draft Program Law submitted to Parliament

The Cayman Tax, introduced in 2015, is essentially a look-through tax applicable to Belgian Personal Income Tax ("PIT") and Belgian Legal Entities Tax ("LET"). It targets income generated by qualifying legal arrangements, by attributing it to and taxing it in the hands of the founder or third-party beneficiary of such an arrangement, as if the latter had received this income directly. Next to this transparent approach, the Cayman Tax also aims at taxing liquidations of legal arrangements and certain transfers of (part of) the assets (for legal arrangements with legal personality, so-called 'Type 2 arrangements', as opposed to the Type 1 legal arrangements lacking legal personality). Apart from the effective taxation, there is (since 2013) also an obligation for founders and third-party beneficiaries of legal arrangements to report the existence of the legal arrangement in their annual tax return. The Cayman Tax was amended for the first time at the end of 2015 (see [previous newsflash coverage](#)).

On 6 November 2017, the draft Program Law was submitted to Parliament. The draft law implements several tax measures that were announced on 26 July 2017 (the so called 'Summer Agreement'). Below, the focus is on the measures aimed at reinforcing the Cayman Tax. The following analysis is based on texts that remain subject to parliamentary approval, expected before year-end.

Introduction of "Type 3" legal arrangements

The definition of "legal arrangement" will now also include a third type of arrangement (Type 3 legal arrangement), targeting instances where the link between the founder and the legal arrangement is 'cut loose' and packaged as an insurance contract. This broad definition should cover all instances whereby Type 1 or 2 arrangements are contributed, or where premiums are paid as investments in such arrangements.

Consequently, income obtained by a Type 1 or 2 legal arrangement packaged as a Type 3 legal arrangement will be taxed in the hands of the resident taxpayer who concluded the contract, and in whose name the contractual premium(s) has (have) been paid, as this person will be regarded as the “founder” of a Type 3 legal arrangement.

Abolition of the “third party beneficiary” definition

Going forward, the application of the Cayman tax will be limited to the legal arrangement’s founder. Any other beneficiary will be deemed to receive a dividend (more details below). Consequently, the tax will no longer apply in the hands of the legal arrangement’s third party beneficiary, and the “third party beneficiary” definition will be abandoned.

“Chain arrangements”

The look-through tax will also be applicable to so-called “chain arrangements”. Art. 2 ITC will contain a definition of the “chain arrangement”, “parent arrangement” and “subsidiary arrangement” notions.

If there is a parent arrangement holding all or part of the shares or economic rights of a subsidiary arrangement, the income received by the subsidiary will be considered as income directly received by the parent, in proportion to the participation it holds in the subsidiary.

To avoid double taxation, profit distributions from the subsidiary to the parent arrangement will not be subject to the look-through tax in the hands of the founder, to the extent that the taxpayer has demonstrated that this distribution consists of previously taxed income (FIFO rule). Furthermore, the income received by the subsidiary arrangement will not be considered as income from the parent arrangement if the founder of the parent is also the founder of the subsidiary.

Taxation of distributions by all legal arrangements

Under current Cayman Tax legislation, distributions by trusts or trust-like legal arrangements can be organised tax-free.

Article 18 ITC will be amended to reflect that each distribution by a legal arrangement that is not a repayment of contributed assets will be considered as a taxable dividend, regardless of the legal arrangement type.

An exception to dividend taxation will apply if the taxpayer demonstrates that the distribution triggers a decrease in the value of the legal arrangement’s assets to below the value of the assets originally contributed.

Similarly, an exception will continue to exist if the dividend relates to income that was already subject to its tax regime in Belgium in the hands of an individual or legal entity. A FIFO rule will also be introduced in this respect.

Moreover, the distribution of contributed assets will be deemed to occur after distribution of all reserved profits or income. If needed, the founder will need to prove the originally contributed assets' amount.

Economic activity exception

The economic activity exception will be clarified to better achieve its objective. It will only be possible to claim the substance exemption if the legal arrangement's genuine economic activity (or activities) does not relate to the management of the private estate belonging to (one of) its founder(s).

It can be questionable whether limiting the substance exemption further in such a way fully complies with the freedom of establishment principle, as interpreted by the EU Court of Justice in its 14 September 2017 decision in case C-646/15, Panayi.

Deemed liquidation

Two deemed liquidation scenarios will be included (as irrebuttable presumptions).

Consequently, upon the transfer of the arrangement's assets to another country that does not effectively exchange tax information with Belgium (based on a tax treaty, TIEA, etc.), or upon the contribution of a legal arrangement's economic rights, shares or assets, the "historic" reserves of a legal arrangement will be considered as paid or attributed to the arrangement's founder.

Upon subsequent dividend distribution, an exception will continue to exist if the dividend relates to income that was already subject to its tax regime in Belgium, in the hands of an individual or legal entity.

Sui generis tax transparency for entities without legal personality

Tax will also become applicable to income obtained on a foreign account held by an entity without legal personality and not subject to corporate or legal entities tax (such as trade unions and youth movements).

The tax will be assessed in the hands of the tax resident individual(s) who is (are) authorised to manage the account, unless the entity opts to be subject to the legal entities tax for at least 6 successive taxable periods.

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The current Cayman Tax contains a specific anti-abuse rule that allows Belgian tax authorities to disregard legal acts of Type 2 arrangements that are aimed at circumventing the application of the Cayman tax rules.

This specific anti-abuse rule will be amended. It will be rewritten for all legal arrangements and tied to the existing general anti-abuse rule (article 344 §1 ITC).

Entry into force

Certain provisions (such as the taxation of dividends of distributions by Type 1 legal arrangements) will already be applicable on income collected, paid or attributed by a legal arrangement as of 17 September 2017 or, with respect to withholding taxes, as of the first day of the month following the month of publication (likely 1 January 2018).

Other provisions of the Law will apply as of 1 January 2018.

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