Tax consolidation: the first steps.

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With effect from the tax year 2020, more specifically for financial years starting on or after 1 January 2019, Belgian group corporations may apply a limited form of fiscal consolidation. With this reform, Belgium finally adopts what is common practice in most other EU member states. In the Netherlands, for instance, the principle of the fiscal unit has existed since the 1950s. So, under the banner 'better late than never', Belgium now also is trying to charm companies with the new '*group contributions*' tax deduction scheme.

Limited fiscal consolidation

This limited system of fiscal consolidation in the area of corporate tax allows companies to set off profits against losses. In other words, it does not involve full-grown consolidation but rather a loss transfer technique, defined as group contributions, between affiliated companies.

The Belgian fiscal legislator often excels at writing the most complex texts. And they haven't disappointed this time (section 205/5 of the 1992 Income Tax Act). The conditions for the group contributions are quite strict and their method of operation complicated.

How It Works

Tax losses over the taxable period can be transferred between two companies by means of an agreement. The 'group contribution' scheme consists of a tax deduction for the company paying the contribution and an offset against tax losses for the company receiving the contribution. As an attentive reader you will have noticed that the rule can only be applied to the losses of the financial year involved. Tax losses incurred in the past do not qualify.

Contrary to the fiscal consolidation in terms of VAT through a VAT unit, the individual tax return procedure for each company does not change. Corporate tax does not provide for joint tax returns. Each company has to process the group contribution through its own tax return. The profitable company enters the group contribution in the tax return as a new deduction item in the box *Uiteenzetting van de winst* ('profit statement'). The lossmaking company enters the group contribution in the box *Aanpassingen in min van de begintoestand van de belaste reserves* ('negative adjustment to the opening balance of the taxed reserves').

The following example may serve as an illustration: Company A has made a profit of 1,000; company B reports a loss of -400. Using the group contribution system, company A (user) may transfer part of its profit in an amount of 400 to company B (beneficiary). As a result, B does not incur any fiscal losses and A is taxed for an amount of only 600.

Compensation scheme

Use of the loss setoff scheme implies payment of compensation equalling the tax advantage. In our example this means that user A pays compensation to beneficiary B in an amount of 400 multiplied by the corporate tax rate.

The compensation scheme provides for an equity-neutral system: it does not involve any transfer of capital. This means that creditors or minority shareholders are not affected by the scheme. The user pays the compensation to the beneficiary in the next taxable period. The compensation does not qualify as a dividend, nor as an exceptional and favourable advantage.

The compensation is tax-neutral. For the profitable company it therefore constitutes a non-deductible professional expense (rejected expense). On the beneficiary side, it is exempt from the tax base (increase of the opening balance of the reserves).

Agreement

A key condition for application of the scheme is that the companies involved each year enter into a civil-law agreement. Such agreement can cover no more than one taxable period. A model agreement is in the making and will be published by Royal Decree. The agreement must be appended to the corporate tax return.

Among other things, this group contribution agreement must define the height of the group contribution. Said contribution may not exceed the loss that the beneficiary would have incurred in the taxable period if it had not received the group contribution. Beneficiary companies may be a party to more than one of such agreements. Under no circumstances may the sum of the group contributions included in the agreements exceed the stated loss.

Furthermore, the profitable company undertakes to compensate the beneficiary. As stated earlier, said compensation equals the tax surplus that would have been payable had no group contribution been in place.

For which companies?

The agreement may be entered into by Belgian companies (or EU/EEA companies with a permanent office in Belgium) who are subject to the common rules of Belgian corporate tax and who are affiliated via:

- a direct shareholders' relationship of at least 90% (parent company and subsidiaries); or

- a common parent company (a Belgian or EU/EEA company) directly holding at least 90% of the shares of the companies involved (sister companies).

Indirect participations are explicitly excluded.

Prior to any arrangement about a group contribution, the minimum shareholding condition must have been met for a continuous period of 5 years. Period commencing on 1 January of the fourth calendar year prior to the calendar year named after the assessment year. Except in the case of liquidation, another requirement is that the affiliated companies' financial years coincide.

Some companies are excluded explicitly, such as companies that put immovable property or any real right to immovable property at the disposal of the manager; investment companies; maritime shipping companies and diamond merchants.

Conclusion

The new fiscal consolidation is a bright light for Belgian groups of companies and multinationals. However, in view of the strict participation conditions its success is not guaranteed. Time will tell ...

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