Belgian Commission Recommends Anti-Tax-Fraud Measures

by Marc Quaghebeur

The Belgian Parliament's Tax Evasion Commission in a May 7 report recommended strong measures to fight tax fraud and held tax advisers responsible for devising fraudulent transactions.

Also, on June 18 the Constitutional Court upheld a rule allowing tax authorities to recover evaded tax and penalties from tax advisers if they are condemned as accomplices of tax offenders.

Parliamentary Commission

The commission in charge of investigating major tax evasion cases was established a year ago to investigate why tax evasion cases worth billions of euros have petered out after protracted proceedings in court. The commission's goal was to find out why those cases failed systematically and to propose remedies for the problems. The commission investigated in particular three major fraud cases: the foreign tax credit cases, the cash company tax avoidance schemes, and the case involving the Beaulieu textile group. (For prior coverage of the foreign tax credit cases, see *Doc 2003-19342* or *2003 WTD 167-5*; for prior coverage of the cash company tax avoidance schemes, see *Doc 2004-20956* or *2004 WTD 210-2*.)

After about 70 closed-door hearings with tax experts, magistrates, and a law professor, the commission on May 7 published its 417-page report describing the mechanism of the fraud and the facts and dysfunctions it found.[1] The report lists several general problems the commission uncovered. The report describes the rules relating to Belgian bank secrecy vis-à-vis the tax authorities[2] with a summary of the doctrine and the case law, and it provides a comparison of the bank secrecy rules in France, Germany, the Netherlands, and the United States. Another general issue is the protection in law against the penalties the tax authorities can impose (the right to a fair trial as guaranteed by article 6 of the European Convention on Human Rights, its consequences for the right to remain silent, and so on).

Administrative Recommendations

The commission recommends a relaxation of the "bank secrecy rules." It should be noted that the Belgian rules are not banking secrecy rules but rather banking confidentiality rules. Under Belgian law, Belgian banks cannot give information about their clients to the tax authorities. In practice, however, this fiscal bank confidentiality

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[1] Parl. Doc. House of Representatives, 2008-2009, nr. 52-0034/004.

[2] Article 318, Income Tax Code 1992.

is being eroded by new money laundering rules and the U.S. qualified intermediary system. In 2006, Parliament adopted a law that stopped banks from invoking client privilege in dealings with the tax collector. Finally, the double tax treaty with the United States made the benefit of the zero withholding tax rate on dividends dependent on compliance with the exchange of information provisions. To this effect, Belgium adopted a law empowering the Belgian tax authorities to request the disclosure of tax information and to conduct investigations and hearings, even if that contradicted Belgian domestic tax law. (For prior coverage, see *Doc 2007-11206* or *2007 WTD 99-10*.)

Nevertheless, the parliamentary commission finds that the banking confidentiality rules hinder the fight against tax fraud. It recommends that the tax administration be granted the power to ask the banks to disclose information when it has one or more indications that income has not been declared. Currently, the administration must have tangible evidence indicative of tax evasion.

The public prosecutor's office must inform the tax authorities of any indications of tax evasion, but that does not give the tax administration access to the public prosecutor's investigation files. They can get access if authorized by the head of the public prosecutor's office. To avoid wasting time, the commission suggests that Ministry of Finance officials be allowed to access the files of the public prosecutor in cases that have indications of tax evasion.

A basic principle of the Belgian income tax system is that an individual is not taxed on capital gains realized on his private assets consisting of securities, tangible assets, or real property if those gains are realized on transactions that are within the limits of the "normal management of a private estate."[3] A sale of shares in a privately owned company usually constitutes normal management, so the resulting capital gains are generally tax free. In the late 1990s, the tax authorities worked out a different reading of what constitutes normal management in order to tax so-called internal capital gains. Those are transactions in which a shareholder exchanges the shares in an entirely controlled company for those of a holding company. The tax authorities held that this did not constitute normal management of a private estate. (For prior coverage, see *Doc 2006-5832* or *2006 WTD 75-5*.) The commission finds the notion of "normal management of a private estate" vague, leading to problems of interpretation. It suggests adding more precise and objective criteria to the law that would allow the introduction of a presumption of abnormal estate management.

The commission finds that the right of the taxpayer to choose the route of lesser taxation is a fundamental principle of Belgian tax law. This is the so-called *Brepols* doctrine.[4] The commission wants to require taxpayers to report any transactions

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[3] Article 90, I°, Income Tax Code 1992.

[4] The Supreme Court has repeatedly held that parties are free to conclude any agreements in the way they want, provided they accept all the consequences and do not infringe any legal provision even if the form they choose is not the most common one and even if they only do so to reduce the tax burden on the transaction. *See* Cass. June 6, 1961, *Brepols*; *Pasicrisie*, 1961, I, 1082: "There is no prohibited simulation and hence, no tax evasion, if, in order to enjoy a more favorable tax regime, and without

involving a tax haven and to submit tax constructions that are justified by the *Brepols* doctrine to the Ruling Committee (tax shelter disclosure).

The commission also takes offense at tax doctrine. Articles written by tax specialists take an approach that systematically legitimizes or even encourages the choice for the route of lower taxation. Tax administration officials do little to counter this. The commission suggests creating a new tax magazine that would offer a contradictory explanation of the tax cases -- that is, one that defends the position of the tax authorities.

Tax Advisers

Finally, the commission gives tax consultants a rap on the knuckles. It observed that large-scale tax fraud is systematically organized with the collaboration of consultants who think up fraudulent transactions and put them into practice. The commission recommends greater criminal sentences for financial and tax advisers who devise fraudulent constructions and specific "non-optional" punishment for tax consultants who advise fraudulent constructions to their clients. It also wants to impose an obligation for consultants (such as accountants, lawyers, notaries, and banks) to cooperate in the fight against tax evasion and to inform tax authorities when their clients set up tax constructions in a tax haven.

The commission also advocates introducing an obligation for consultants to inform the Financial Intelligence Processing Unit of any cases of tax and organized fraud. Currently, banks, notaries, auditors, external accountants and tax consultants, and, under some conditions, attorneys at law already have an obligation to report to the money laundering authorities. However, as far as tax evasion is concerned, that applies only when those professionals are faced with money laundering originating in "serious and organized tax evasion using particularly complicated mechanisms or methods on an international scale" or when they notice 1 or more of the 13 indicators listed by royal decree. (For prior coverage, see *Doc 2007-18828* or *2007 WTD 159-3*.) The commission proposes removing the serious tax evasion requirement.

It should be noted that the government has recently proposed a bill to release those professionals from their reporting obligation in some situations -- that is, when they determine their client's position in law -- similar to what is already the case for attorneys at law. However, the law would include a restriction: The exemption would not apply if those professionals participate in the activities of money laundering or financing of terrorism, provide the legal advice for those activities, or know that their client is seeking legal advice for such purposes.

Constitutional Court

On June 18 the Constitutional Court handed down a decision that could be very expensive for tax advisers.

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infringing any statutory obligation, parties conclude agreements of which they accept all the consequences, even if the form which they give to these agreements is not the most common."

Last year the criminal courts in Brussels and Antwerp suspended two cases relating to cash company tax avoidance schemes to request a preliminary ruling from the Constitutional Court regarding article 458 of the Income Tax Code.

In the 1990s several companies with large taxable profits and few possibilities to cancel out the profits with deductions were lured by cash company schemes. The scheme is simple: If a company reinvests the proceeds from the sale of its assets in other qualifying assets within three years, rollover relief is available for capital gains on the fixed tangible (and some intangible) assets that the company held for at least five years before the sale.[5] If the company sells its business assets to a sister company, that company can depreciate the purchase price of the business assets. And if it finances the purchase, it also has the possibility to set off the interest against its taxable profits. The owners of the first company, which is now cash-rich, can then sell the shares of the company at a discount and legally escape the capital gains tax completely. There is no problem if the purchaser arranges for the company to reinvest the cash into assets that qualify for the rollover relief.

However, mala fide purchasers failed to reinvest or pay the capital gains tax that is then due by the cash company. Instead, they drained the cash from the company to repay the loans they had taken out to acquire the shares. There are about 440 companies involved in such tax avoidance schemes, some of which are quite well known, such as Douwe Egberts and Fortis Insurance Belgium. The public prosecutor's office initiated proceedings not only against the purchasers of 196 companies but also against the vendors of these companies and their advisers. The Belgian state has taken part in the proceedings to recover the tax evaded and has also started civil proceedings against another 87 companies. The advisers are often banks (Fortis, KBC, Deutsche Bank) or tax advisers (Ernst & Young).

Article 458 of the Income Tax Code states that whoever is condemned as an offender or an accomplice of one of the crimes listed in the income tax code is jointly and severally held liable to pay the tax evaded. Moreover, their employers or the companies of which they are a director can be held liable for the penalties and costs. The advisers pointed out that the tax evaded is often many times the amount of their fees and that the court does not recognize the financial impact a condemnation has on them. They argued that this provision was incompatible with articles 10 and 11 of the Belgian Constitution (equality and nondiscrimination) and article 6 of the European Convention on Human Rights (the right to a fair trial), particularly because article 458 does not allow the courts to examine the case without full powers of jurisdiction.

The Constitutional Court on June 18 confirmed that article 458 is compatible with the aforementioned articles. The court stated that the liability is a consequence in civil law of a criminal condemnation and cannot be likened to a criminal sentence and that the judge does not have to take account of attenuating circumstances. The tax authorities can therefore recover the tax from the accomplices. However, the court pointed out that the tax authorities will always initially recover the tax from the offender.

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[5] Article 47, Income Tax Code.

And if they hold the advisers liable to recover the tax from them, the advisers will always be able to recover the tax from the offender or the other accomplices.

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