Belgium’s De Facto Position on the Taxation of Trusts

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The Belgian Ruling Committee (the authority for advance rulings) issued three rulings in late 2009 relating to the tax treatment of payments made by a trust to a beneficiary during the life of the settlor. Those rulings, which have just been published on the committee’s website, offer insights into the position of tax authorities in a country that does not have a trust concept.

Trusts in Belgian Tax Law

As a typical civil-law country, Belgium does not have the concept of a trust. Moreover, Belgium has not signed the Hague Convention of July 1, 1985, on the Law Applicable to Trusts and on Their Recognition. The Private International Law Code adopted in 2004 dealt with the concept for the first time. (For prior coverage, see Tax Notes Int’l, Sept. 27, 2004, p. 1207, Doc 2004-17037, or 2004 WTD 189-10.)

To determine how a trust is to be treated under Belgian tax law, one has to analyze the trust arrangement under Belgian civil law. (Belgian tax law does, indeed, follow civil law.) The various transactions and legal relationships, as well as the rights and obligations of the settlor, trustee, and beneficiary, must be translated into civil-law terms before the Belgian tax rules can be applied. That can be a problem, however, because Belgian civil law does not make the distinction between beneficial and legal ownership.

The Belgian tax authorities have not made a complete analysis of the tax situation of trusts. Until now, the legal analysis made by commentators was an extrapolation of current rules combined with a single decision dating back to 2004.

That analysis was usually based on a simplified perception of the trust as being one of two extremes: the irrevocable and discretionary trust or the fixed-interest trust.

Irrevocable and Discretionary Trust

The general conclusion is that if the settlor has set up an irrevocable and discretionary trust, the settlor abandons any entitlements to the trust property and accepts that he loses the income of and control over trust property without any hope of recovering those assets, the income of those assets, or control over the way they are used. The settlor normally will no longer have to declare the income from the trust assets for income tax purposes, and because the trust assets have left his estate, he will not be subject to inheritance tax.

In an irrevocable and discretionary trust, the trustee is the legal owner of the assets, but he has a duty to use them on behalf of the beneficiary. When he acquires the trust assets, it is not the result of a donation that might be subject to the registration tax for donations. But when the trustee holds title to the trust assets and collects the income from those assets, he may be subject to income tax in his country of residence.

Moreover, it is the trustee who decides who gets what, and as long as the trust assets are held by the trustee, the beneficiary does not have any right to the trust assets or to the income of the trust assets. Nor does he have an obligation to declare the income of the trust assets or any benefits he receives from the trust in his income tax return. When the trustee assigns a trust asset or a sum of money from the trust assets to the beneficiary, it is not considered taxable income, but rather a gratuity. (Gratuities do not constitute taxable income.)
Fixed-Interest Trust

If the settlor has settled a fixed-interest trust, giving the beneficiary a fixed interest, the trustees have no power of discretion in the distribution of the trust property or the income from the trust property to the named beneficiaries; they must follow the settlor’s instructions. The beneficiaries are clearly given the right to receive a specific fixed interest in the trust. If the trust is fixed, some or all transactions or relationships may be treated as transparent for tax purposes. When the settlor transfers assets to the trustee, the trustee may receive them as a nominee for the settlor or in his own name with a personal duty to make payments to the beneficiaries, or in some cases, as a nominee for the beneficiaries.

The agreement between the settlor and the trustee will determine whether the trust assets must be deemed to have left the settlor’s estate; but even then the tax authorities can use an antiavoidance rule to consider that they are still held by the settlor. The relationship between the trustee and the beneficiary will determine whether the beneficiary has a right to the trust assets, a right to the income from the trust assets, or a right to income from the trustee.

In the most common situation, in which the beneficiary receives an income from the trust assets, the income will be considered investment income and will be subject to income tax at a rate of 15 percent in the same way as interest income.

A fixed-interest trust will usually be treated as transparent for tax purposes. This means that unlike an irrevocable and discretionary trust, a fixed-interest trust is of limited use for estate planning. There is, however, a gray area between both types of trust, and the oversimplification is that a discretionary trust that is not irrevocable or that can be modified by the settlor, or even an irrevocable and discretionary trust when the settlor is a beneficiary or the protector, must be transparent for tax purposes.

The Position of the Tax Authorities

The following is a summary of the position taken by Belgian commentators.

Only once, in 2004, did the tax authorities take a position on a trust structure to confirm that the settlement of an irrevocable and discretionary trust did not trigger any gift tax liability for the trustee or the beneficiary. Moreover, they confirmed that the beneficiary derives his entitlement to a benefit from the discretionary decision of the trustee. As long as the trustee does not decide that the beneficiary will receive a benefit and what the extent of that benefit will be, the beneficiary cannot be subject to inheritance tax.

Consequently, there is no inheritance tax liability at the time of the settlor’s death, because it remains uncertain whether the beneficiary will actually get any rights to the trust assets or the trust income. In other words, the beneficiary is subject to the trustee’s decision to grant him an entitlement. The inheritance can only be due when the trustee has made that decision and the beneficiary has accepted the benefit. (For prior coverage, see Tax Notes Int’l., Nov. 21, 2005, p. 685, Doc. 2005-22980, or 2005 WTD 218-6.)

In their practice note relating to the implementation of the EU savings tax directive, the tax authorities had to address the issue of the trust regarding the beneficial owner. “Beneficial owner” means any individual who receives an interest payment or any individual for whom an interest payment is secured, unless he provides evidence that it was not received or secured for his own benefit. The question then is who the beneficial owner is in fiduciary arrangements or trusts. Tax authorities’ definition of a trust is as follows: The trust relationship results from an agreement in which the settlor transfers an asset or a set of assets. The trustee undertakes to manage the assets for the benefit of a third party (the beneficiary) in accordance with the provisions that are clearly described in an official document (the trust deed).

The legal status of the trust is determined by the legislation of the country where the trust is established. The bank paying the interest must determine the capacity of the receiver of the interest payment in accordance with the legal status of the trust. The beneficial owner is then not the trustee but the settlor or, alternatively, the beneficiary if that is not the same person and if it appears from the agreement that the payments are definitively acquired by the beneficiary with no possibility of the payments returning to the settlor.

The Three Rulings

A Trust With a Belgian Foundation as a Trustee

In the first decision (no. 900.189, dated July 7, 2009), a Belgian private foundation was to be set up to act as a trustee.

The shareholdings in the trust fund would never go back to the estate of the settlors; the settlors would not receive any dividends or realize any capital gains. The trustee would hold shares of two British companies that, it appears, would settle the trust. The administration of the shareholdings would be entrusted to an external professional manager.

The committee found that the trust would be discretionary and irrevocable: Only the foundation/trustee would have the authority to manage and administer the assets (that is, to collect the dividends and sell the shares, and to decide how the income is distributed, to

from the shares immediately, the certifying entity is shares in return. As long as it distributes the income foundation receives shares of a company and issues the trustee determines which assets go into which trust.

Time the surviving spouse dies. surviving spouse receives a distribution of the principal or at the will be subject to estate tax. U.S. estate tax is due at the time the surviving spouse free of estate tax; distributions of principal marital deduction. However, the QDOT can only pay income to in his own name the unlimited marital deduction to offset the interest instead of dividends.

A U.S. Marital Trust (Qualified Domestic Trust) The second decision (no. 700.112, dated December 8, 2009) relates to a marital trust set up by the trustee of a family trust that was set up by a U.S. citizen living in Belgium who is married to a citizen of a third country and has children from a first marriage who are U.S. citizens and residents. The settlor will settle his private estate with an independent U.S. limited liability company, and the beneficiaries are likely to be himself, his wife, and his children. Upon his death, the trustee will make some donations and, if the settlor’s wife is still alive, split the trust into a bypass trust (the family trust) and a qualified domestic trust (QDOT) (the marital trust). The trustee determines which assets go into which trust. The value of the assets in the family trust is determined in accordance with the U.S. rules. The remain-

A QDOT is a solution to the rule under U.S. tax law that when the surviving spouse is a non-U.S. citizen, he cannot claim in his own name the unlimited marital deduction to offset the inheritance tax. A QDOT allows any property left to the trust of the noncitizen surviving spouses to qualify for the unlimited marital deduction. However, the QDOT can only pay income to the surviving spouse free of estate tax; distributions of principal will be subject to estate tax. U.S. estate tax is due at the time the surviving spouse receives a distribution of the principal or at the time the surviving spouse dies.

The settlor also wanted the committee to confirm that any distribution of capital by the trustee, or any decision to distribute capital, does not trigger an income tax liability, regardless of whether the trust qualified as a discretionary trust or as a fixed-interest trust.
The committee agreed that distributions of capital cannot constitute taxable income. Income recharacterized as capital by the trustee does, however, remain income.

The settlor asked the committee to confirm that any payments by the trustee of the marital trust to the beneficiary (the surviving spouse) would not be taxable income (whether the payments constituted investment income or any form of miscellaneous income). The committee found that the income received by the spouse from the marital trust qualifies as investment income relating to receivables and is taxable in Belgium at the fixed rate of 15 percent.

The settlor also wanted to make sure that article 344, paragraph 2 of the Income Tax Code (ITC) did not apply. That article allows the Belgian tax authorities to ignore some transactions involving low-tax jurisdictions, including the sale, transfer, or contribution of shares, bonds, debts, intellectual property, or cash to persons in jurisdictions whose tax regime is significantly more advantageous to taxpayers than Belgium’s tax system. The burden of proving that the transaction in question has a genuine financial or economic purpose is shifted to the taxpayer.

**Conclusion**

The relevance of these rulings is limited to the cases at hand. Nevertheless, they give an indication of the
Ruling Committee’s analysis and reasoning, and because the committee is on the front line faced with demands relating to many new issues, it often has to break new ground.

In particular, the second and third decisions show that the tax authorities are making a serious effort to understand the concept of a trust and are making sure they do not get it wrong. Fortunately, the situation is relatively simple: There are only one or two factors (the beneficiary and/or the settlor) that link the trust to Belgium; the trustee and the trust assets remain outside Belgium. What is important is that the Ruling Committee accepts that a trust can be irrevocably discretionary while still looking for any indications that the trust would be partially influenceable and therefore not entirely discretionary. Unfortunately, the committee takes a rather limited view of the notion of “discretionary.” It seems to assume that if there is only one beneficiary, the trustee does not have full discretionary powers, even if he can decide whether to make any distributions or payments to the beneficiary.

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