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VAT and Directors' Fees in the Benelux

The VAT Directive does not clearly address the question of the VAT treatment of directors' fees, and recent developments in Dutch, Belgian and Luxembourg VAT legislation have emphasized the lack of harmonization on that question among the EU Member States. In this article, the authors outline the VAT treatment of directors' fees in the Benelux. Using some real-life examples, they subsequently show how differences in the VAT treatment of directors' fees in practice result in an increasing level of legal uncertainty for companies and directors.

1. Introduction

The VAT treatment of company board members' activities ("company directors") differs across the EU Member States. This difference leads to situations in which the same (private or legal) person, when acting as a company director, as well as the company itself, are treated differently for the same activity in cross-border situations.

One of the many outstanding questions in this area relates to the VAT *status* of company directors. In particular, a key question is whether a company director should be considered to be a taxable person acting independently within the framework of an economic activity for the purpose of articles 9 and 10 of the VAT Directive,[1] or, by contrast, whether he should be considered an "instrument" of the company, who does not act independently and therefore remains outside the scope of VAT.

Another key concern, raised by many VAT practitioners, relates to the VAT treatment of the consideration received by company directors in the form of a percentage of a company's profits, as a payment depending solely on the arbitrary decision of the company's shareholders (so-called "tantièmes"). Here, the question is whether or not the consideration has a direct and immediate link with the activity of the company director for the purpose of article 2 of the VAT Directive.

2. The VAT Treatment of Directors' Fees in EU Legislation and ECJ Case Law

The VAT Directive remains silent on the issue of the VAT treatment of the management of a company. The VAT principles of "autonomy" and "neutrality" would probably call for a specific VAT definition – and therefore a specific VAT treatment – based on an analysis of the nature of the activity that the company directors perform. However, references made by the EU institutions to this question have been very limited.

In 1977, the European Council and the European Commission held, in statements recorded in the minutes of the meeting at which the Sixth VAT Directive[2] was adopted,[3] that the EU Member States are entitled not to subject to VAT those persons carrying out *honorary activities, as well as managers, directors, officers, receivers of companies in their relationships with the companies, acting as instruments*. However, the statement made on this occasion was not legally binding.[4]

In contrast, the report of the 53rd meeting of the VAT Committee on 4 and 5 November 1997 stated that "[a]ll delegations agreed that services supplied by a legal person as a member of a company's board of directors should be regarded as economic activities carried out independently within the meaning of Article 4(1) and (2) (of the Sixth European Directive 388/77/EC) and that they should therefore be subject to VAT."[5] But, again, this guideline, on which unanimity was reached amongst the delegations of the EU Member States participating in the meeting of the VAT Committee, had no legal force.

Recently, the European Commission has shown some concern about the VAT treatment of company directors in a number of EU jurisdictions, including the Netherlands and Belgium. In 2011, it initiated an infringement procedure against the Netherlands that sought to amend the rules applying to persons participating in the supervisory board of a company.[6] The result and consequence of this infringement procedure will be discussed in section 3.2. Likewise, in 2014, the European Commission was reported to have criticized the VAT treatment of company directors in Belgium and threatened Belgium's public authorities with an infringement procedure that sought to amend the VAT regime applying to legal persons acting as company directors. The amendment of the VAT regime applying to company directors in Belgium will be discussed in section 3.1.

Thus far, the case law of the Court of Justice of the European Union (ECJ) has remained silent on the issue of the VAT treatment of company directors, with the exception

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1. Council Directive 2006/112 of 28 November 2006 on the common system of value added tax, OJ L347/1 (2006), EU Law IBFD.
2. Sixth Council Directive 77/388/ECC of 17 May 1977 on the harmonization of the laws of the Member States relating to turnover taxes – Common system of value added tax: uniform basis of assessment, OJ L145 (1977), EU Law IBFD.
3. Document R/716/77 (FIN 151).
4. DE: ECJ, 22 Oct. 2009, Case C-242/08, *Swiss Re Germany Holding GmbH v. Finanzamt München für Körperschaften*, ECJ Case Law IBFD.
5. *See* http://ec.europa.eu/taxation_customs/taxation/vat/key_documents/vat_committee/index_fr.htm.
6. IP/11/1128, 29 Sept. 2011.

of some particular positions that either it or its Advocates General have reached in some very fact-specific cases. For example in his Opinion in the *Polysar* case,[7] Advocate General Van Gerven indicated that private persons acting as company directors should be considered "instruments" of the company when they do not act independently, as opposed to service providers that are acting independently. Therefore, according to the Advocate General, the former should not be treated as taxable persons for VAT purposes (thus in contradiction with the VAT Committee guideline issued on that question). In 2000, Advocate General Fennelly's adopted the same position in his Opinion in the *Floridienne/Berginvest* case.[8]

As to the ECJ, it has neither ever expressly contradicted nor confirmed the position of these two Advocates General. At times, it seems to have at least considered this issue. In the *Heerma* case,[9] for example, the ECJ indirectly referred to the theory under which company directors could act as "instruments" of the company they manage, i.e. not independently. However, the facts on which the *Heerma* judgment is based are so specific that the ECJ's expressed position cannot be sufficiently relied upon for guidance. The indirect reference in the *Heerma* case aside, the ECJ has never confirmed that company directors should be considered "instruments" of the company that they represent. On the contrary, in a relatively recent judgment,[10] the ECJ seems to have confirmed that company directors should be considered to be acting within the framework of an economic activity for VAT purposes and therefore should be considered to be taxable persons for VAT purposes (in line with the VAT Committee guideline). However, the specific nature of the case and the ECJ's somewhat unclear conclusion on this point again prevents practitioners from reaching clear-cut principles.

For the sake of completeness, it should be noted that the ECJ made clear that a private person director remains outside the scope of VAT when this private person is bound by an employment agreement.[11] This follows from article 10 of the VAT Directive.

3. The VAT Treatment of Directors' Fees in the Benelux

3.1. Belgium

The VAT treatment of directors' fees has recently become a significant issue in Belgium. The reason is that the Belgian VAT authorities have changed their position on this subject, as a result of pressure from the European Commission (as indicated in the previous section, the European Commission was reported to have criticized the VAT treatment of company directors in Belgium and threatened Belgium's public authorities with an infringement procedure that sought to amend the VAT regime applying to legal persons acting as company directors).

In short, the Belgian VAT treatment depends on whether a director acts as a private or as a legal person, and whether the director supplies his services under a statutory mandate (as determined in the managed company's by-laws).

Directors acting as a private person are not deemed to act independently from the company in which they carry out their statutory mandate(s). This position is based on the theory that the director is considered as an integral part or "instrument" of the company itself. As a result, the remuneration received for services carried out within their capacity as a director is considered to be outside the scope of Belgian VAT. This reasoning applies to all types of fees and remuneration that are directly linked with the activities carried out as director (such as recurring fees, tantièmes, bonuses, etc.). However, services that are outside the scope of the statutory mandate (e.g. consultancy services) are, in principle, subject to VAT to the extent that these services are supplied in an independent manner (when acting under an employment agreement, such a director would, in principle, not be considered to be acting in an independent manner). However, a mere management agreement that is not covered by a statutory mandate is, in principle, subject to VAT according to the general principles of VAT law.

In contrast, legal entities operating as a director are deemed to carry out VAT-taxable transactions from a Belgian VAT perspective. In Belgium, entities with a separate legal personality are generally considered taxable persons for VAT purposes acting in an independent manner. In the past, Belgian administrative guidance[12] had established an optional regime under which legal entities, operating as a director, could choose whether or not to opt for VAT on the received directors' fees. In the case where directors had opted for VAT, all the fees linked with their activity as a director were subject to VAT. This decision also applied to the so-called tantièmes, although one could question whether there is or was a direct and immediate link between the activities carried out as a director. This issue raises the question of whether the profit share remains within or outside the scope of VAT. (*See* section 3.3. for comments from a Luxembourg perspective.) It should be noted that recent Belgian case law supports the qualification as a profit share outside the scope of VAT.[13] However, the official position of the Belgian authorities remains unchanged. In any case, this optional regime for *legal entity directors* was abolished with effect from 1 June 2016. This change had been decided and announced at the end of 2014, but its entry into effect was postponed several times in recognition of its major impact on the VAT position of legal entities acting as a director. In many industries which perform exempt transactions for VAT purposes (such as the medical, the financial and the real estate

7. NL: ECJ, 20 June 1991, Case C-60/90, *Polysar Investments Netherlands BV v. Inspecteur der Invoerrechten en Accijnzen*, ECJ Case Law IBFD.
8. BE: ECJ, 14 Nov. 2000, Case C-142/99, *Floridienne S.A. and Berginvest S.A. against the Belgian State*, ECJ Case Law IBFD.
9. NL: ECJ, 27 Jan. 2000, Case C-23/98, *Staatssecretaris van Financiën v. J. Heerma*, ECJ Case Law IBFD.
10. DE: ECJ, 13 Mar. 2014, Case C-204/13, *Finanzamt Saarlouis v. Heinz Malburg*, ECJ Case Law IBFD.
11. NL: ECJ, 18 Oct. 2007, Case C-355/06, *J.A. van der Steen v. Inspecteur van de belastingdienst Utrecht-Gooi/kantoor Utrecht*, ECJ Case Law IBFD.
12. Administrative decision E.T.79.581, 27 Jan. 1994.
13. Court of Appeal Brussels, 4 May 2016, 2013/AF/105.

industries), the optional regime for director companies was indeed often used to reduce the VAT cost on management fees. As a result of the abolition of the optional regime for legal entities operating as a director, companies with no right to deduct input VAT are now facing an additional cost of 21%[14] on the incurred directors' fees paid to legal entities. Accordingly, this change is having an important negative impact on those industries.

To limit the impact of this decision, the Belgian VAT authorities have included a number of concessions in the administrative guidance, in which they outlined their final position on this subject.[15] First, it should be noted that *legal entity directors* can qualify under the "franchise"[16] regime if their annual turnover does not exceed EUR 25,000.

Second, the most obvious method of avoiding an additional VAT cost on directors' fees is to create a VAT group between the operating company and the management company. To do so, the companies must be closely bound to one another by financial, economic and organizational links. This requirement particularly causes difficulties in the case where an operating company is managed by several management companies, as these mutual links usually do not exist between the management companies. In this respect, the Belgian VAT authorities have made a concession in which they accept that, under certain circumstances, a VAT group can be created between an operating company and different management companies. This is an important relief from VAT where one company, such as an insurance agency (performing exempt transactions), is managed by several management companies. However, this concession's compatibility with EU VAT principles remains open to debate.

If management companies carry out both services within and outside the scope of their legal mandate as a director, then each service should, in principle, follow its own VAT treatment, unless it concerns a single supply from an economic perspective that should not be artificially split.[17] In practice, it has been argued that many management companies in the financial services sector are supplying both VAT-taxable management services as well as exempt intermediary services (negotiation in share transactions, credit, insurance, etc.). In this respect, the Belgian VAT authorities accept that a distinction should be made between services carried out within and outside the scope of the statutory director mandate. Services that are outside this scope might be exempt from VAT and, hence, reduce the amount of non-deductible VAT in the hands of an operating company with an exempted main activity. However, the Belgian VAT authorities consider that at least 25% of the fees cover the remuneration for the director services subject to VAT when no clear distinction can be made by referring to the factual situation and contracts. Companies are, of course, free to prove otherwise on the basis of contracts or any other evidence. But again, this is a concession that the Belgian VAT authorities have made that can be called into question when referring to the ECJ's extensive case law on single and composite supplies.

It has also been confirmed that directors' fees paid to management companies of special investment funds can remain exempt under the VAT exemption for the management of special investment funds.[18]

In conclusion, the VAT treatment of directors' fees in Belgium has changed significantly as a result of the abolition of the optional regime for directors operating as a legal entity. Taxable persons carrying out exempt transactions are still struggling with the impact of this change in Belgian VAT law.

It should also be highlighted that the VAT position of *private person directors* has not yet been questioned in Belgium. They remain outside the scope of VAT. However, it cannot be excluded that this position could be changed in the future in light of the developments at the EU level (*see* section 3.3. regarding Luxembourg).

3.2. The Netherlands

In the Netherlands, *legal person directors* are considered to be taxable persons for VAT purposes if they receive any remuneration for their managerial activities. As to *private person directors*, a distinction must be made between directors and members of supervisory boards.

Based on article 10 of the VAT Directive, individuals with an employment agreement are explicitly not considered taxable persons. In the Netherlands, *private person directors* having an employment agreement with a company are not taxable persons for VAT purposes and as such any remuneration will be considered outside the scope of VAT.

The position of *private person directors* who are the major or sole shareholder of a company (*directeur-grootaandeelhouder*) is a special issue in the Netherlands. According to the Dutch Supreme Court's earlier case law, such directors were considered to be acting as taxable persons, meaning that their directors' fees were subject to VAT.[19] However, in the *J.A. van der Steen* case, the ECJ has held that a *director sole shareholder* acts as an employee, outside the scope of VAT.[20] The ECJ referred to the following elements: the director depends on the company to determine his remuneration; the director acts on behalf and under the responsibility of the company; and the director does not bear any economic business risk in acting as the manager.

Since this ECJ judgment, it is generally accepted that *private person directors* who are the major or sole shareholder of a

14. Standard VAT rate in Belgium.
15. Administrative decision E.T.127.850, 30 Mar. 2016.
16. Special scheme applicable for small businesses.
17. DK: ECJ, 2 May 1996, Case C-231/94, *Faaborg-Gelting Linien A/S v. Finanzamt Flensburg*, ECJ Case Law IBFD; UK: ECJ, 25 Feb. 1999, Case C-349/96, *Card Protection Plan Ltd v. Commissioners of Customs and Excise*, ECJ Case Law IBFD; NL: ECJ, 27 Oct. 2005, Case C-41/04, *Levob Verzekeringen B.V, OB Bank N.V, v. Staatssecretaris van Financiën*, ECJ Case Law IBFD; and SE: ECJ, 29 Mar. 2007, Case C-111/05, *Aktiebolaget NN v. Skatteverket,* ECJ Case Law IBFD.
18. Art. 135(1)(g) VAT Directive.
19. *Hoge Raad*, 26 Apr. 2002, 35.775.
20. *See Van der Steen* (C-355/06).

company are deemed to have an employment agreement with that company and therefore remain outside the scope of VAT. However, if a director operates through a personal holding or management company, then the services will be subject to VAT as such a company cannot act within an employment agreement.

Directors of companies who do not have shares in the company can have an employment agreement and, as such, their remuneration is outside the scope of VAT under article 10 of the VAT Directive. However, if a company director agrees to a management agreement with the company, which is not an employment agreement, then this arrangement will always be a taxable service.

Executive directors of entities incorporated under Dutch Law that are listed in the stock exchange have a special position. Since 1 January 2013, they are no longer allowed to enter into an employment agreement with such entities.[21] As a consequence, such an executive director needs to enter into a type of management agreement with the listed company. If the executive director enters into such an agreement personally (i.e. not through a personal holding company), then the consequence will be that the executive director could qualify as a taxable person. In this respect, it should be assessed whether the executive director acts in an independent manner. Under article 2:162 of the Dutch Civil Code (DCC), executive directors are appointed by the supervisory board. Furthermore, executive directors represent the company and are autonomous in managing the company within the limits set by the law and the company's by-laws. This situation could be an argument for justifying that such an executive director is acting in an independent manner. By contrast, article 3(1) of the Dutch Income Tax Act[22] stipulates that an executive director is considered to have a deemed employment agreement with the company and therefore income tax is equally owed on his remuneration. While this situation can be used as an argument to conclude otherwise, it should be noted that a similar assumption was made for members of supervisory boards until 1 January 2017 (*see* below).

In conclusion, at the moment it is still unclear whether an executive director of a Dutch stock exchange-listed company, when acting as a private person, could be considered a taxable person.

The VAT position of the members of supervisory boards should also be mentioned. In the Netherlands, members of supervisory boards are appointed by the annual shareholders' meeting (article 2:132 of the DCC). The role of the supervisory board is to supervise the acts and decisions of the board of directors, the general affairs of the corporation and its affiliated undertaking(s), and to advise the board of directors. In carrying out its duties, the supervisory board is guided by the general interests of the company and the companies affiliated with it (article 2:140 of the DCC). Furthermore, only private persons can be part of a supervisory board and hence not legal entities. As a consequence, it is not possible for a supervisory board member's personal holding company to engage in an agreement with the legal entity. The annual shareholders' meeting determines the remuneration of the supervisory board members.

Until 1 January 2017, members of the supervisory board were also considered to have a deemed employment agreement for income tax purposes in the Netherlands. Since that date, this fiction has been deleted from the Dutch Income Tax Act. In general, a lot has been written about the VAT position of members of supervisory boards in the Netherlands. The European Commission is of the opinion that a member of a supervisory board does indeed qualify as a taxable person and has asked the Netherlands to amend its favourable policy on this point.[23] The Netherlands have changed the VAT treatment without challenging the European Commission's approach at the ECJ. In the authors' view, the European Commission's position is correct when referring to the ECJ case law that applies VAT to activities that are performed in one's own name, for one's own account and under one's own responsibility, such as a person who will qualify as a taxable person.[24] Given its independent role, a member of a supervisory board will indeed have the characteristics of a taxable person. In the end, such a person is independent, receives remuneration for his work and performs his activities in a sustainable manner.

3.3. Luxembourg

3.3.1. Context

Until very recently, the Luxembourg VAT administration had not publicly taken a position on the VAT treatment of services supplied by company directors. Its position had only been set out in a few individual decisions. Under these decisions, directors, acting in their capacity as private individuals or legal persons within the framework of a social mandate (as opposed to an employment contract), were considered taxable persons. All types of directors' fees were considered subject to VAT, including the percentage fees calculated as a share of the profits of the company.

However, the VAT administration never officially communicated this position. Therefore, in practice, the activity of a company director was generally considered outside the scope of VAT and the consideration paid to directors (whether natural or legal persons) was not subject to VAT.

To bridge the gap between the unofficial position of the Luxembourg VAT Administration and common practice, a parliamentary question was submitted to the Finance Minister on 10 February 2016.[25] In his answer, the Finance Minister indicated that a working group would be set up

21. Art. 2:132 sub 3 Dutch Civil Code (*Burgerlijk Wetboek*).
22. Wage Tax Act 1964 (*Wet op de Loonbelasting* 1964).
23. IP/11/1128, 29 Sept. 2011.
24. NL: ECJ, 26 Mar. 1987, Case 235/85, *Commission of the European Communities v. Kingdom of the Netherlands*, ECJ Case Law IBFD; ES: ECJ, 25 July 1991, Case C-202/90, *Ayuntamiento de Sevilla v. Recaudadores de Tributos de La zone primera y segunda*, ECJ Case Law IBFD; and NL: ECJ, 27 Jan. 2000, Case C-23/98, *Staatssecretaris van Financiën v. J. Heerma*, ECJ Case Law IBFD.
25. Parliamentary question 1799, 10 Feb. 2016, L. Mosar.

to clarify these issues and an official position would be made public in the near future.

3.3.2. Circular letter 781

On 30 September 2016, the VAT administration published its much-awaited circular letter on the VAT treatment of company directors (Circular letter 781). While less detailed than expected, Circular letter 781 has confirmed that independent directors have the status of taxable persons in Luxembourg and that directors' fees are, in principle, subject to VAT at the current standard rate of 17%. Circular letter 781 should be read in the light of the "Frequently Asked Questions" and answers (FAQ) published on the same date on the Luxembourg VAT administration's website. According to the Circular letter, as completed by the FAQ, directors' fees paid by Luxembourg-based companies might be subject to VAT even where the director is established in a jurisdiction where he is not considered to be a taxable person for his mandate as director. This would, for example, be the case if a private person established in Belgium acted as a company director of a Luxembourg-based company.

Circular letter 781 only addresses the VAT treatment applying to the activity of company "directors". However, it is expected that principles laid down by Circular letter 781 will be applied similarly to managers of private limited liability companies (*sociétés à responsabilité limitée*) and all legal and private persons in charge of the management of all types of companies, within the framework of a social mandate (such as in limited partnerships (*sociétés en commandite*)).

Circular letter 781 also highlighted that employees exercising the functions of company directors "in representation of their employer" do not act independently and should therefore not be considered taxable persons for VAT purposes. In this case, the employer (represented by one of its employees) would be considered the taxable person supplying the service.

Although Luxembourg VAT should generally apply to all services supplied by directors and located in Luxembourg, it will not apply in the following situations:

- if the company director falls under the "franchise" regime applying to small businesses (which only applies to directors established in Luxembourg with a qualifying turnover of maximum EUR 30,000);
- if the company director benefits from the "honorary activities" exemption of article (44)(1)(w) of the Luxembourg VAT Law of 12 February 1979.[26] However, according to circular letter 781, the activity of a director will only be considered "honorary" if the consideration (attendance fee/*jetons de presence*) is paid as a contribution towards the expenses of the member. Circular letter 781 remains silent with regard to the notion of "contribution towards the expenses" (*défraiement*). In practice, it is to be expected that this exemption will only be accepted by the Luxembourg VAT administration in a limited number of situations, where the amounts involved correspond to a lump-sum reimbursement of the expenses that are incurred in practice by the director. In addition to the fact that the administrative interpretation of the exemption differs significantly from the text, it is likely to generate much discussion in the future; or
- if the services can be characterized as management services of an investment fund.

Company directors established in Luxembourg should effectively comply with all the Luxembourg VAT obligations for all services carried out from 1 January 2017.

The VAT applying to services supplied by non-established directors must be self-reported by the Luxembourg-based company through the reverse charge mechanism, provided that the Luxembourg-based company is a taxable person for VAT purposes. In the opposite case, the services supplied by a non-established director will continue to remain outside the scope of Luxembourg VAT.

According to Circular letter 781, the taxable amount on which the Luxembourg VAT will be calculated comprises all consideration paid for the services supplied by the company directors, i.e. everything that constitutes a consideration obtained or to be obtained by the company directors from customers or third parties. The withholding tax retained on directors' fees for income tax purposes is part of the taxable basis for VAT purposes.

It can be inferred from the FAQs that percentage fees (or "tantièmes") paid to company directors are considered to be part of the taxable amount. In the authors' view, however, this position should have received a more detailed explanation. To consider that the amount paid to the supplier is part of the taxable amount, it must have a direct and immediate link with the service provided.[27] In the case of percentage fees, such a link might not be so obvious. In addition, to fall within the scope of an economic activity, a service must be supplied for the purposes of obtaining income from it.[28] In the case of a company director, the function may be exercised for reasons that are foreign to receiving income (such as setting the political orientation of a company, pressing the interests of a specific shareholder, etc.). In the authors' view, it is therefore very debatable whether there is a direct and immediate link between the payment of a percentage fee and the activities carried out by a company director. This is certainly the case when a company director is also a shareholder.

26. Law of 12 February 1979 amending and completing the law of 5 Aug. 1969 concerning value added tax, Mémorial A no. 11 of 19 Feb. 1979, p. 186. Art. 44(1)(w) of the law provides that: "services supplied within the framework of an honorary activity by members of public bodies, groups and professional chambers, company boards or management committees or other similar instruments and remunerated by attendance fees, should be exempt from VAT".

27. CZ: ECJ, 10 Nov. 2016, Case C-432/15, *Odvolací finanční ředitelství v. Pavlína Baštová*, ECJ Case Law IBFD.

28. AT: ECJ, 26 June 2007, Case C-284/04, *T-Mobile Austria GmbH v. the Republic of Austria*, point 44, ECJ Case Law IBFD, and DE: ECJ, 13 Dec. 2007, Case C-408/06, *Landesanstalt für Landwirtschaft, Abteilung Förderwesen und Fachrecht v. Franz Götz*, point 18 and following, ECJ Case Law IBFD.

Since the taxable amount includes all taxes, duties, levies and charges, excluding the VAT itself, withholding taxes on directors' fees should also be considered part of the taxable amount for VAT purposes.

Whether the one-page Circular letter 781 really answers all the issues raised, including in the parliamentary question submitted to Finance Minister on 10 February 2016, is, therefore, open to debate.

3.3.3. Open question: Impact on the investment fund industry

Neither Circular letter 781 nor the FAQs clearly address the question of how the application of the VAT to directors' fees could in practice have an impact on the investment funds industry. Accordingly, fees paid to the directors of investment funds should probably continue to benefit from the exemption applying to the "management of investment funds", provided that the services in question can be characterized as management services of a qualifying investment fund (within the meaning of article 44(1)(d) of the Luxembourg VAT Law, as interpreted in the light of the ECJ's case law and Circular letters 723, 723bis and 723ter of the Luxembourg VAT administration).

In practice, the Luxembourg VAT administration would accept that the consideration paid to the directors of an investment fund is fully exempt from VAT on the basis of article 44(1)(d) of the Luxembourg VAT Law, when the investment fund is self-managed. However, this position might be different if the investment fund were managed by a third-party management company. Directors of third-party management companies would be obliged to make a split between that portion of the work that would be VAT exempt (being specific and essential to the management of the investment fund) and the (corporate) management of the management company itself that would subject to VAT.

4. Cross-Border VAT Implications

From the previous section it appears that the VAT treatment of directors' fees differs within the Benelux area. Although the trend is to broaden the scope of VAT for directors' fees, the different EU Member States still apply different approaches and interpretations. This situation complicates the VAT treatment in a cross-border context.

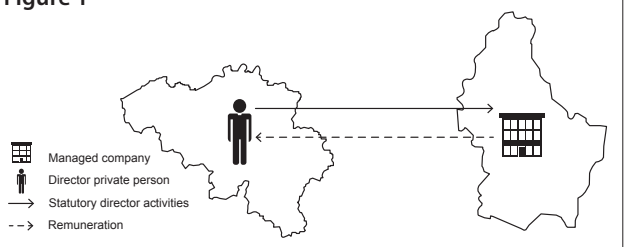
This will be illustrated in the next section with a commentary on specific VAT issues arising in connection with cross-border invoicing within the Benelux.

4.1. Belgium-Luxembourg

4.1.1. Belgian-based director/Luxembourg-based company

In this scenario (*see* Figure 1), a Belgian-based director, acting as a private person, carries out activities within the statutory mandate of a Luxembourg-based company. Assuming that the Luxembourg-based company is a taxable person for VAT purposes, the transactions carried

Figure 1



out by the Belgian-based director will be subject to VAT in Luxembourg.

However, from a Belgian VAT perspective, the transactions are considered to be outside the scope of VAT. In the case where the Belgian director does not carry out any other transactions for which he would be deemed to have to register for VAT purposes, the Belgian director will, in principle, not have a Belgian VAT number. This situation will trigger, among other things, the following concerns:

- Will the Luxembourg-based company be entitled to deduct input VAT without a compliant VAT invoice from the Belgian-based director? Although the Luxembourg-based company can rely on article 219a of the VAT Directive and on ECJ case law to defend its right to deduct input VAT,[29] this situation could give rise to discussions with the Luxembourg VAT administration.
- Will the Belgian director be able to register for VAT purposes in Belgium in the situation where this activity would be his only activity, and if so, is he required to file EC Sales Lists? In principle, Belgian VAT legislation only allows taxable persons to register for VAT purposes and file EC Sales Lists. A director private person that is not a taxable person for VAT purposes in Belgium should therefore not register in Belgium and comply with VAT reporting obligations. However, the recent changes in the Luxembourg VAT legislation might trigger further guidance from the Belgian VAT authorities.
- If the Belgian director did have to register for VAT in Belgium because of the VAT-taxable director services in Luxembourg, would he be able to recover input VAT in Belgium? This question is open for debate but, in practice, the Belgian authorities will in principle rely on article 169(a) of the VAT Directive to deny input VAT recovery (no input VAT deduction if the activities were carried out within Belgium).
- From which moment will the Belgian-based director be deemed to have a fixed establishment in Luxembourg if the director were to actually carry out his activities at the physical premises of the Luxembourg-based company? For example, if the Belgian director were to have an office in Luxembourg, the assessment should be made of whether or not there is a fixed establishment for VAT purposes in Luxem-

29. DE: ECJ, 1 Apr. 2004, Case C-90/02, *Finanzamt Gummersbach v. Gerhard Bockemühl*, ECJ Case Law IBFD.

bourg. If yes, then this situation would mean that the Belgian director should register for VAT in Luxembourg and issue invoices with Luxembourg VAT.

If the Luxembourg company was not a taxable person (i.e. a mere passive holding company), then the services supplied by a Belgian director, acting as a private person, will be deemed to take place in Belgium and thus fall outside the scope of VAT. This situation could be different if the Belgian director were to supply his services from a work place in Luxembourg to the extent that this work place qualified as a fixed establishment for VAT purposes.

4.1.2. Luxembourg-based director/Belgian-based company

In this scenario (*see* Figure 2), a Luxembourg-based director, acting as a private person, carries out activities within the statutory mandate of a Belgian-based company. Assuming that the Belgian-based company were a taxable person, the transactions would be deemed to take place in Belgium and hence not subject to VAT. The Luxembourg-based director should not have to suffer adverse VAT consequences due to the fact that his services will not be subject to VAT in Belgium. However, the question arises of whether the Luxembourg-based director, supplying services to a Belgian-based taxable person, must file an EC Sales List, since the services supplied would be considered beyond the scope of VAT in Belgium (while the legislation only provides solutions for services subject to or exempt from VAT).

In the case where the Belgian-based company is not a taxable person (i.e. a mere passive holding company), services supplied by a director established in Luxembourg will be subject to Luxembourg VAT at the standard rate of 17%, even if the director is a private person. This situation means that the Belgian holding company will be in a less favourable situation than if it had a Belgian-based director.

On the basis of the above scenario, it appears that in many situations, the lack of harmonization between the Luxembourg and the Belgian interpretations will create potential VAT "leakages", specifically where the director is a private person. Therefore, correctly determining the place of establishment of the director is of paramount importance. In this respect, some clarification of the criteria to determine the place of establishment of a physical person exercising a taxable activity would be very important, especially where the director is in a frontier situation (with his/her domicile in Belgium and work place in Luxembourg). This place of establishment will determine where and if a director should have to register for VAT purposes, and should have compliance obligations.

4.2. Belgium-Netherlands

4.2.1. Belgian-based member of supervisory board/company based in the Netherlands

In this scenario (*see* Figure 3), a private person living in Belgium carries out supervisory activities within a supervisory board of a company established in the Netherlands.

Figure 2

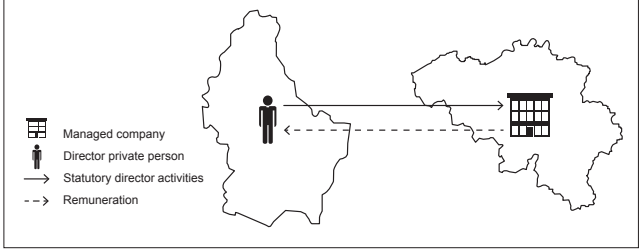
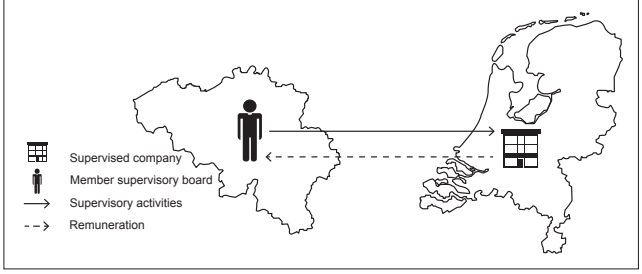


Figure 3



This situation could give rise to the same problems as outlined in section 4.1.1. (Belgian-based director/Luxembourg-based company).

From a Dutch VAT perspective, the payment made by the Dutch company will be considered to be payment for a service performed by the Belgian director. As a consequence, the Dutch company will need to apply the reverse charge mechanism to this payment to the extent that the Dutch company is a taxable person.

From a Belgian perspective, it should be determined whether the private person, being member of the supervisory board, is considered a taxable person or if the activities of this person are equal or similar to a director acting as an "instrument" of the Dutch company, and outside the scope of VAT. The problem is that under Belgian company law the concept and the content of the activities of a supervisory board are different and that it is not fully clear how to qualify supervisory services "Dutch style" from a Belgian perspective.[30]

Depending on the Dutch entity's right to deduct input VAT, the self-accounted VAT on the directors' fee is (partly) deductible. In the event that no VAT number should be granted to the Belgian private person, this will in general not lead to negative consequences on the right to deduct input VAT. However, questions could be raised by the Dutch tax authorities if, from a Belgian perspective, the person were not considered a taxable person. From the Dutch tax authorities' perspective, this is not an ideal situation, since the Belgian director will not list his service in the EC Sales List (VIES system). As such, there would be a lack of control from a European perspective on these payments.

30. In practice, the authors have seen that the Belgian authorities allow a VAT registration and the right to deduct input VAT for private persons that are member of a Dutch supervisory board. The exact VAT status of Belgian members of a Dutch supervisory board should, however, be determined on a case-by-case basis.

If the Dutch company is not a taxable person (e.g. a passive holding company), Belgian VAT should in principle be due unless it can be argued that the Belgian private person is acting as an "instrument" of the Dutch company, and thus outside the scope of VAT.

5. Conclusion

There are significant differences in the way directors' fees are treated from a VAT perspective in the Benelux. This is particularly the case when it comes to activities carried out by a private person within his statutory mandate as a director of a company or as a member of a Dutch company's supervisory board. These differences give rise to a number of unresolved concerns regarding the VAT position of the directors and the companies.

Moreover, the lack of harmonization might lead to a distortion of competition between the different EU Member States. This is especially the case for the management of mere passive holding companies. It goes without saying that in an area which is known in particular as being attractive for holding companies and where cross-border commuting is widespread, the lack of harmonization in this field causes significant legal uncertainty for businesses.