

# Expatriate News

**Special Edition** January 2005: Exit Charges



During the BDO Global Expatriate Conference that was held in Brussels in October 2004 a number of surveys helped to document the technical content of the conference. The BDO Global Expatriate Team has decided to use a series of special newsletter editions to share the information gathered in the surveys and at the conference.

We would like to thank everybody who shared the specific country information that made it possible for us to produce this newsletter and who made the Brussels 2004 Expatriate Conference a huge success.

Some of the information below may now be subject to change. In all specific cases you should check the current position with your BDO expatriate contact.

## **Exit charges**

### **1. Introduction**

Local governments, irrespective of whether the specific country is inside or outside the EU, tend to preserve what they claim to be their own. In that respect, many countries surrounding us have provisions in their national tax system that prevent a resident taxpayer from moving from one country to another without taxation on emigration. However, with the common market principle in mind, one may question whether it is in accordance with the four basic freedoms that are protected by the EC Treaty that on the occasion of his emigration from one EU Member State to another EU Member State a taxpayer should be obliged to pay tax on the basic movement of his residence from one country to another country.

## 2. Court of Justice case 'De Lasteyrie'

Recently, the European Court of Justice (ECJ) decided that France did not act in accordance with the basic principles of the EC Treaty on the occasion that a resident taxpayer moved from France to Belgium. In this so-called 'Hughes de Lasteyrie Du Saillant case' the taxpayer successfully claimed before the ECJ that he was obstructed by the French Government when he moved from France to Belgium. The Attorney General in this case stated that France is entitled to levy tax on the occasion of the alienation of the substantial interest that the taxpayer had according to French tax legislation. However, to levy tax on the mere movement of the residency of the taxpayer was concluded not to be in line with European legislation.

The French exit charge system equals the Dutch system in many ways. Under the French exit charge system persons who have resided in France for at least six years in the last ten years and who in the last five years prior to the moment of emigration owned more than 25 per cent of the shares of a company residing in France face an exit charge if they decide to emigrate to another country. The exit charge, which amounts to tax of 16 per cent, is levied on the fair market value of the shares minus their acquisition value. Deferral of the tax is possible, however very strict conditions apply, for example a fiscal representative must be appointed, the taxpayer should file an annual income tax return and a bank guarantee would have to be provided to the French tax authorities. The payment can be deferred until the moment the shares are actually sold. The French tax authorities provide for relief to avoid double taxation if the state of residence levies tax on the occasion of the sale of the shares as well. The assessment will not be collected after a period of five years.

The French government justified the tax regulations by pointing out that they aimed to prevent substantial shareholders from moving to another country to realise the capital gain free of tax or at a lower tax rate and subsequently emigrating back to France to resume their normal lives.

According to the ECJ the French tax regulation whereby unrealised capital gains are taxed on the moment of emigration to another EU Member State is not in line with EU legislation. The ECJ considered that it was not relevant that the taxpayer had the possibility to defer taxation. The deferral of taxation was subject to meeting strict conditions. The ECJ also ruled that the bank guarantee that the taxpayer

had to provide to the French tax authorities is of itself not in line with EU legislation.

Even if EU Member States' tax regulations are not in line with EU legislation, under certain conditions the regulations can be justified. As none of the French justifications was heard by the Court, we will not go into this deeper at this stage.

This so-called 'Lasteyrie' case led in many countries to changes to the national tax systems, e.g. the Netherlands. The 'Lasteyrie case' was brought before justice on 11 March 2004.

On 21 September 2004 it was announced that the French tax administration would await the final decision of the French Supreme Administrative Court before it would issue guidelines on the consequences of the decision taken by the ECJ. The most recent news is that the French Supreme Administrative Court on 10 November 2004 followed the decision taken by the ECJ. The Supreme Court ruled that the French regulation indeed was incompatible with EU law and therefore void when applied to French residents transferring their residence to an EU country for the purpose of exercising their freedom of establishment.

Questions that at this stage remain unanswered are:

- Will the provision be applied if it concerns an emigration to an EEA country; and
- Will the provision be applied if the emigration is not motivated by an economic reason, ie not to exercise the freedom of establishment?

With regard to this last item recent ECJ court rulings shed more light. That jurisprudence will not be dealt with at this stage.

## 3. Brussels 2004 expat questionnaires

For our survey we issued a questionnaire.

The questionnaire contained following questions:

- (i) In the situation that a resident of your country emigrates to another country, would an exit charge be levied?

(ii) If so, does the exit charge relate to:

- a. shares that the resident holds in a company, and if yes, is there a limit to the percentage of shares and does it make any difference where the company is resident? If so, please specify the exit charge
- b. pension rights and/or annuity insurances that have built up in the state of residence? If so, please specify the exit charge
- c. any other personal deductions? If so, please specify the exit charge.

(iii) Would the answer to question (ii) be different if the emigrant was an EU/EEA citizen?

Out of 44 countries that filled in the questionnaire 13 countries have exit charge provisions in their local tax system. These countries are both EU countries and non-EU countries. Most exit charges relate to shareholdings. Some exit charges relate to other items such as pension rights that have been built up during the period that the taxpayer was a resident of that specific country.

In this special edition newsletter we would like to take a closer look at the exit charges in following countries:

EU:

**Austria**  
**Belgium**  
**Denmark**  
**France**  
**Germany**  
**Norway**  
**The Netherlands**  
**The United Kingdom**  
**Spain**  
**Sweden**

Non-EU:

**Australia**  
**Canada**  
**South Africa.**

## 4. Definition of exit charges

First we should identify what an exit charge actually does. An exit charge in the meaning of this newsletter is a charge levied on unrealised capital gains in assets or on unrealised income that is levied only due to the taxpayer deciding to move from one country to another. An exit charge could also take the form of tax benefits being reclaimed at the moment the taxpayer decides to leave the country.

### 4.1. Exit charge on shares in companies

Exit charges on the unrealised capital gain on substantial shareholdings are commonly used in Germany, Austria, the Netherlands, Denmark and France. In Germany, unlike in the other jurisdictions under investigation, taxation cannot be deferred. Exit charges that are implemented by means of the claw back of taxable benefits (pension) on the occasion of transfer of residency have been found to exist in Belgium and in the Netherlands.

The German tax system implies that German tax residents who have been subject to unlimited taxation during the ten years before the date of emigration and who within the five years prior to the emigration owned at least one percent of a German corporation, are taxable on the occasion of the emigration of the taxpayer out of Germany. The tax rates can go up to 45 per cent. The German tax claim vanishes in the case of re-immigration to Germany within five years after the moment of emigration. The period of five years may be extended to ten years if certain conditions are met.

After the Lasteyrie case was brought before justice the European Committee issued a press release on 19 April 2004. The press release contained the request from the EC Committee to the German government to abolish the exit tax regulation as outlined above. At the end of November 2004 BDO contacted the German Ministry of Finance to find out the current status. The Ministry of Finance indicated that the German government had no intentions to abolish the exit tax regulations completely. However, it was admitted that the exit tax regulations may violate EU legislation to a certain extent and that the German government was dealing with the request from the European Committee. It is possible that the German government were negotiating with the European Committee in order for the German tax regulations to be more in line with EU Legislation and to avoid facing an ECJ case. It was indicated that it could take months before the adjustments of the German exit tax regulations would be made public.

The Danish tax system also contains an exit tax charge. The percentage of shares does not appear to be relevant and neither is the place of residence of the company. The tax rates vary between 28 per cent and 43 per cent.

The Austrian tax system is also an interesting tax system to explore more closely. Under the Austrian tax system there is an exit charge on the unrealised capital gains on shares. An individual who owned more than one percent of the shares during the last five years before emigrating from Austria to another country in principle is subject to the exit charge. If the company in which the shares are held is residing outside Austria then the exit charge will be implemented at the moment of emigration. If the company resides in Austria, then the position as to whether the exit charge is implemented or whether the exit charge taxation would be deferred depends on the regulations as outlined by the Double Tax Agreement concluded between Austria and the country of residence. If under the Double Tax Agreement Austria would lose the right to levy tax, then the exit charge is effected. If Austria maintains its right to levy tax, then taxation can be deferred.

After the Lasteyrie case was brought before justice the Austrian government implemented changes to the above system. It was decided that at the request of the taxpayer taxation could be deferred until the moment the shares are actually sold. The possibility to request the deferral of taxation is only possible for emigrants that emigrate to EU or EEA Member States, provided that between Austria and the future state of residence an administrative and legal enforcement agreement is in place. A subsequent emigration to a non-EU or non-EEA state will be regarded as a sale of the shares. At the moment of taxation the tax assessment of the year of emigration will be altered. If the value of the capital gain is decreased between the moment of emigration and the moment of sale, taxation will take place on the lower value. It is uncertain what will happen if the value does not decrease, but increases. The ECJ decided that EU Member States were allowed to levy tax on the capital gain that originated during the period the tax resident was a resident of a certain country. However, the ECJ decided that if the taxable moment would be the moment of emigration that would be a breach of the basic freedoms as safeguarded by the EC treaty. The fact that the French regulation made it possible to defer taxation on request was not considered relevant according to the ECJ. It is surprising that the altered Austrian regulation indicates that at the request of the taxpayer taxation can be deferred. Interestingly from an EU point of view, it is not yet known, how the request must be made by the taxpayer and whether

the request can only be made if certain conditions are met.

## **4.2. Reclaim of tax benefits**

Another source of income some countries focus on when implementing exit charges is pension benefits. Some countries reclaim the tax benefits claimed in the period in which the taxpayer was a resident. These exit charges exist amongst other countries in the Netherlands (reclaim of amounts deducted) and in Belgium (depending on the type of pension right and the age of the beneficiary, the pension benefits would still be taxable in Belgium at progressive rates, unless fixed rates of 10 per cent, 16.5 per cent or 33 per cent apply). It is commonly understood that the exit charge as it exists in Belgium is not in conformity with EU law.

The latest news in that respect is that the European Commission sent a reasoned opinion on 17 December 2003 requesting the amendment of the Belgian tax legislation by which persons emigrating from Belgium are still taxable in Belgium on pension benefits received, even if Belgium under its Double Tax Agreements has ceded taxation rights to other countries. However, no Belgian tax would be due if the taxpayer can prove that he is actually taxed abroad on the pension benefits. Belgium agreed to make the necessary changes to its tax legislation at the latest by September 2005, on which date the Pension Fund Directive should be implemented. In the Netherlands the Dutch government for the time being pertains that the reclaim of benefits is in line with EU legislation.

## **4.3. Unlimited or limited extended tax liability**

Exit charges could also take the form of an unlimited extended tax liability, under which the emigrant is deemed to remain a resident of the country he emigrates from. Deemed residency regimes are common in Spain, Norway, Germany, Sweden and the UK.

According to the Norwegian tax system, a person who has been a Norwegian tax resident for a period of ten years will be regarded as such during a three year period after the emigration. An emigrant is still considered to be a Norwegian tax resident after emigration if during the Norwegian income tax year this person spends 61 days or more in Norway. This is also the case if his spouse and/or under-age children maintain a home in Norway. A Spanish tax resident who emigrates to a tax haven (e.g. the Antilles) for the full tax year and the preceding four tax years is regarded as remaining a tax resident. The question of residence is not dependent on the fact of

whether the emigrant has Spanish income or not after the emigration. The unlimited residency regulations are subject to Double Tax Agreement regulations.

The UK, Germany and Sweden have exit charge regulations that are generally characterised as 'limited extended tax liability regulations'. In the UK capital gains tax is levied on certain assets on re-entry in the UK within five years after emigration. German nationals who emigrate to low tax jurisdictions and who have a substantial economic interest in Germany during a period of ten years are taxed more heavily than regular non-resident taxpayers. Swedish tax residents after emigration from Sweden are liable for capital gains tax on, for example, shares in Swedish companies and so-called financial instruments issued by Swedish companies (convertible debt instruments, futures, warrants etc.) for a period of ten years. The Swedish exit charge regulations are subject to the Double Tax Agreements concluded by Sweden. In most cases the ten year period is limited. We feel that the UK exit charge regulations may be in line with EU law. UK non-residents that re-emigrate to the UK are taxed on the same assets and in the same manner as UK residents that did not emigrate from the UK. We fail to see any discriminatory elements in that. It is doubtful whether the unlimited or limited extended tax liabilities in other countries are in conformity with EU law. We suggest checking on a case-by-case basis whether the regulations may be conflicting with EU law.

## **5. Emigration to non-EU / non-EEA Member States**

Up to now we focussed on emigrations from one EU Member State to other EU Member States. On emigration of EU citizens to non-EU or non-EEA Member States the provisions that regulate the exit charges are governed by the arrangements made in the Double Tax Agreements concluded between the various countries. In principle most Double Tax Agreements do not conflict with the exit charges levied, as in most cases they are levied during the period the taxpayer is still a resident and thus before the Double Tax Agreement applies. In the Netherlands the principles of the exit charge on emigration to non-EU and non-EEA Member States still stand. Consequently, the Dutch tax authorities will issue a conservatory assessment at the moment of emigration and in order to defer taxation the taxpayer should provide for certain financial guarantees. Most Double Tax Agreements that the Netherlands has concluded stipulate that capital

gains on the alienation of shares in a company that is established in the Netherlands by a person that has been a tax resident of the Netherlands in the past five years prior to the alienation, are taxable in the Netherlands. The Double Tax Agreement limits the period of taxation to five or, in recent Double Tax Agreements, to ten years.

Finally, we have looked more closely at some exit charge regulations in non-EU or non-EEA Member States, in particular Australia, Canada, and South Africa.

The South African tax system implies that at the moment of emigration capital gains tax is levied on all assets. South African immovable property and business assets of a South African permanent establishment are not subject to the exit charge. The exit charge includes shares in a South African company. The applicable tax rate amounts to 25 per cent. The effective rate amounts to approximately 10 per cent. A more or less similar system can be found in Canada. From Canadian perspective the exit charge also relates to shares in a company, whereby in general it is irrelevant where the company is resident. In Australia on emigration one is subject to taxation on the deemed realised capital gain on all assets, unless the asset has a necessary connection with the territory of Australia. The latter relates to Australian real estate and shares in an Australian company. The deemed capital gain can be delayed until the moment the assets are actually sold. There is an exit charge on shares unless the departing resident owns more than ten percent of shares in an Australian public company or owns any shares in an Australian private company. The applicable capital gains tax rate for individuals is 24.25 per cent provided the shares are held for more than one year. There is no taxation on departure of any pension rights that have been build up during the period of residency.

## More information

For more information, please contact your local BDO expatriate contact or in the Netherlands contact Armand Lahaije via email at [armand.lahaije@bdo.nl](mailto:armand.lahaije@bdo.nl) or by telephone on **+31-10-24 24 600**.

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This newsletter aims to provide general information etc. For completeness' sake we mention that if a particular country was not mentioned in this newsletter; the conclusion cannot be drawn that in that particular country an exit charge does not exist. We have mainly focused on the countries that submitted documentary information for our Brussels 2004 expat conference.