New exit levy on DRD Funds: much ado about nothing

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To generate a return on their excess liquidities, Belgian companies often turn to so-called DRD Funds, which offer a favourable tax treatment. Dividends and capital gains on shares in DRD Funds are in principle largely exempt from taxation. In order to reduce this tax advantage, the federal coalition agreement announced 'a 5% levy on capital gains on exit' of DRD Funds, as well as a conditional credit for the withholding tax on dividends distributed by such funds. Following the Easter Agreement, the outlines of this measure were further developed in the draft Program law, which was recently approved in first reading by the Council of Ministers. This draft law reveals, on the one hand, that the scope extends beyond traditional DRD Funds, and on the other hand, that the tax measure may in practice fail to achieve its intended objective.

DRD Funds: tax favoured investment product for companies

The 'DRD Fund' referred to in the federal coalition agreement is a regulated investment company with variable capital whose main objective is the collective investment in listed securities, generally with the status of an '*openbare bevek*'/*sicav publique*'. For tax purposes, such DRD Fund is subject to the special tax regime of article 185bis ITC 1992, on the basis of which it is only taxable on a very limited basis and can de facto avoid corporate income tax.

What makes the 'DRD Fund' attractive for corporate investors is that, in addition to its own tax-exempt status, dividends from DRD Funds and capital gains on exit remain largely tax exempt allowing a compounding of the return tax free in the hands of corporate investors. This is because the conditions for the application of the dividend received deduction (DRD) regime and the share capital gains tax exemption either do not apply or will usually be met:

- the classic holding period and minimum participation conditions do not apply in respect of dividends distributed by such 'DRD Fund', due to its tax status as an 'investment company' (art. 202, §2, third indent, 3° ITC 1992) (the 'holding period condition' normally requires that the shares have been or will be held in full ownership for at least one year; and the 'minimum participation condition' normally requires that the shareholder holds a participation (i) of at least 10% in the share capital of the distributing company, or (i) with an acquisition value of at least EUR 2,500,000 which, except for so-called 'small' shareholders, also qualifies as 'fixed financial asset'; both conditions however do not apply if the shares are held in an 'investment company').
- the 'DRD-taxation condition' (which normally requires a minimum level of taxation in the hands of the distributing company) can usually largely be met despite the DRD Funds' tax-exempt status. This condition is indeed considered met if the DRD Fund's articles of association provide for the annual distribution of at least 90% of the net income, and to the extent that this income consists of redistributed dividends or capital gains from 'good shares', ie from shares whose dividends themselves are eligible for the DRD regime or from capital gains on shares eligible for exemption under Article 192 ITC 1992 (art. 203, §2, second indent ITC 1992). This proportionality rule ('to the extent that') means that dividends paid by DRD Funds are often partly eligible for DRD and partly taxable, although in practice it often concerns a high percentage of DRD. The Belgian Ruling Commission has repeatedly issued rulings on how this 'coefficient' of exempt income should be determined when a DRD Fund distributes dividends, when the shares in the DRD Fund are sold, or in the event of a share buyback by the DRD Fund (see, eg, Advance Ruling 2024.0443 of 9 July 2024).

An investment in DRD Funds is therefore a fiscally interesting alternative to a direct investment in listed shares, where the corporate investor would be required to meet both the holding period and minimum participation conditions to benefit from the DRD regime. This is even more the case since successive legislative changes have fully aligned the conditions to benefit from the capital gains on shares exemption regime with those for the DRD regime (art. 192, §1 ITC 1992; full alignment since the 2017 'summer agreement', with effect from assessment year 2019).

Moreover, DRD Funds will become even more important now that the minimum participation condition for shareholdings of less than 10% but with an acquisition value of at least EUR 2,500,000 is further tightened, ie such shares must qualify as a financial fixed asset, unless the shareholder is a small company (this change is included in the Program Law adopted by the Belgian Parliament on 18 July 2025, yet to be published). However, this change has no impact on investments made through DRD Funds since, as mentioned, the minimum participation condition is not applicable here.

For the discussion of the draft law, it is useful to already note that a similar tax regime applies to investments in certain regulated investment and real estate companies that nevertheless do not have the regulatory status of an '*openbare bevek*'/*sicav publique*'. This includes the following fund types:

- the *'Private Privak'/Pricaf Privée'* and the 'Publieke Privak'/'Pricaf Publique', both of which aim at investing in unlisted shares (venture capital or private equity).
  - As far as the '*Private Privak/Pricaf Privée*' is concerned, the above-mentioned redistribution condition is interpreted differently: it is deemed to be fulfilled if the redistributed income derives from 'good shares', without any distribution obligation (amounting to at least 90% of the net income) (art. 203, §2, third indent ITC 1992). However, note that a *Private Privak/Pricaf Privée* is only subject to the special tax regime (under aforementioned art. 185bis ITC 1992) if certain specific conditions are fulfilled (art. 185bis, § 3 and art. 192, § 3 ITC 1992); otherwise, the *Private Privak/Pricaf Privée* is subject to normal corporate income tax, in which case a corporate investor can still benefit from the DRD regime and capital gains exemption, based on the standard 'taxation condition' (but still without the 'holding period' and 'minimum participation conditions' having to be met, as such Private Privak/Pricaf Privée is also an 'investment company').
  - For the *Publieke Privak/Pricaf Publique*, on the other hand, a redistribution requirement does apply, although it is set at 80% of net income rather than 90% (cf. art. 203, §4 ITC 1992).
- specialised real estate investment funds (REIFs) and (public and institutional) regulated real estate companies (RRECs). These vehicles are also subject to an adapted redistribution requirement under the DRD-taxation condition: they must redistribute at least 80% (instead of 90% for DRD Funds) of their net income in order for the dividends and capital gains to be eligible for the DRD regime and capital gains exemption. Such re-distributed income will be eligible for the DRD regime if it arises, either from dividends or capital gains on 'good shares' or from property income normally taxed abroad. Since re-distributed rental income from (Belgian) real estate held by the company itself is exempt from tax on the part of the investment or real estate company and therefore, in any case, does not qualify for DRD regime on the part of the corporate investor, the DRD-coefficient here is generally much lower than for the DRD Fund.
- the European Long-Term Investment Institutions (**ELTIF**), whose purpose is to encourage long-term investment in the European economy. As in the case of the *Private Privak/Pricaf Privée*, the redistribution condition is deemed to be met if the redistributed income arises from 'good shares', without a redistribution obligation (art. 203, §2, second indent ITC 1992). Moreover, as in the case of the aforementioned real estate companies, the DRD regime can also be applied to the part of the dividend originating from real estate income normally taxed abroad (art. 203, § 2, sixth indent ITC 1992).

Moreover, in all these cases, they do not necessarily have to be Belgian regulated investment or real estate companies; dividends from shares of foreign companies with similar status can also fall within the scope (under certain conditions) of the abovementioned regimes.

Coalition agreement

In the federal coalition agreement, it was stated in relation to DRD Funds that 'a 5% tax will be imposed on capital gains at exit', and additionally, 'withholding tax will only be creditable against corporate income tax to the extent that the receiving company grants the minimum director's remuneration in the income year in which the distribution is received'.

Based on this paragraph, it could only be inferred that the scope of the new levy would be limited to the 'DRD Fund.' However, no details were provided regarding the practical modalities of its application or any possible exceptions. Concrete guidance was only expected with the publication of the draft law.

Draft Program law

In summary, the draft law provides for a separate tax of 5% '*in the hands of companies realising exempt capital gains in accordance with Article 192, §1 [ITC 1992]*' on shares in certain regulated real estate and investment companies and whose distributed income benefited from the DRD regime in one of the previous taxable periods (new Article 219sexies ITC 1992).

Companies only

For clarity, the separate tax applies only to domestic companies and foreign companies holding the said shares through a Belgian establishment.

For individuals, DRD Funds do not offer any specific tax advantages compared to other UCITS funds. The draft law does not provide for a separate tax on exempt capital gains for such individual investors. However, they will need to take into account the announced new general 10% capital gains tax when selling such shares as of 1 January 2026.

Targeted shares

According to the draft Program law, the scope includes '*the shares of an investment company referred to in Article 203, §1, first indent, 2°, or an investment company with fixed capital for investment in real estate referred to in Article 203, §1, first indent, 2°bis, a regulated real estate company or a foreign company, whose distributed income was deducted from profits in at least one of the previous taxable periods in application of Articles 202 and 203*' (new Art. 219sexies, second indent ITC 1992).

The draft law thus generally targets investment and real estate companies that benefit from a special tax regime. This includes, on the one hand, domestic '*beveks/sicavs*' and '*bevaks/sicafs*', REITs, RRECs and ELTIFs and, on the other hand, foreign investment and real estate companies with similar regimes that benefit from a special tax regime in their tax jurisdiction. As such, the scope of the new separate tax is significantly broader than what the federal coalition agreement initially suggested, which only referred to the 'DRD Funds' described above.

Excluded shares

As mentioned above, *Private Privaks/Pricafs Privée* may also be subject to a special tax regime. However, capital gains on shares in *Private Privaks/Pricafs Privée* will not be subject to the new separate tax, as these shares are explicitly excluded (new Art. 219sexies, third indent ITC 1992).

Furthermore, capital gains on shares in investment and real estate companies that do not benefit from a special tax regime are also not subject to the new tax. This eg includes the *Private Privak/Pricaf Privée* that is subject to the normal corporate income tax (see above), as well as non-regulated investment and real estate companies. Capital gains on these shares remain fully exempt, provided the standard DRD-conditions are met (with respect to 'investment companies', this only concerns the standard 'taxation condition', given that the 'holding period' and the 'minimum participation condition' do not apply; see above).

Only on exempt capital gains

- *Exemption regime of article 192, §1 ITC 1992*

The separate tax only applies to an 'in accordance with Article 192, §1 [ITC 1992] exempt' realised capital gain. Based on this Article, a capital gain can be exempt to the extent that the dividends on those shares are eligible for the DRD regime. As mentioned above, the fulfilment of this condition depends on whether the investment company itself realises 'good income', which generally leads to only a partial capital gain exemption in accordance with a certain coefficient (see again Advance Ruling 2024.0443 which also explains how this 'exempt capital gain' coefficient is calculated). The part of the realised capital gain that is not exempt (and thus included in the taxable basis for corporate income tax purposes) is not subject to the separate assessment.

- *No dividends*

Dividends distributed by the aforementioned investment and real estate companies fall outside the scope of the new separate assessment.

Interestingly, redemption and liquidation bonuses – which arise when investment or real estate companies buy back their shares from the investor or are liquidated – are therefore also excluded from the scope of the separate assessment (which the explanatory memorandum moreover explicitly confirms). The reason is that such redemption and liquidation bonuses do not qualify as capital gains, but as dividends from a tax perspective (art. 18, 2°ter ITC 1992).

This is noteworthy, especially given that 'classic' DRD Funds are generally not listed and are of indefinite duration, meaning that investors usually exit by having their shares redeemed by the DRD Fund. Since the DRD Fund usually cancels these shares immediately, the discussion regarding the potential qualification as a 'capital gain on shares' for redeemed shares that are not cancelled within the same taxable period does not arise here (cf. Circular 2017/C/12 of 14 March 2017).

It therefore appears that this measure completely misses its original purpose, at least based on the current draft law. Companies investing in DRD Funds do not seem to be affected by the separate tax. And yet, the coalition agreement seemed specially aimed at reducing the tax benefit linked to such DRD Funds.

This is different for non-listed investment companies with fixed capital (such as the REIFs), as well as (public and institutional) regulated real estate companies and the ELTIF. Shares in these entities are typically disposed of through a 'regular' sale, meaning that the new separate tax on realized capital gains may effectively apply. The separate tax therefore clearly mainly targets investments in such companies. However, as mentioned above, these real estate companies usually have a low DRD-coefficient, and therefore a relatively low basis for the separate tax of 5%, which makes the measure come across as 'much ado about nothing'.

The same applies moreover to *Publieke Privaks/Pricaf Publique*. However, since such *Publieke Privaks/Pricaf Publique* tend to have a high DRD-coefficient, the separate assessment may have a more significant impact in that case.

It is somewhat ironic that a measure announced to reduce the favourable tax treatment of indirect investments in listed shares ultimately ends up mainly targeting real estate, infrastructure projects, and private equity investments.

- *Retrospective effect*

Contrary to the announced new general capital gains tax, the draft law on the 5% tax does not provide for an exemption for historical capital gains. The separate tax will thus apply to the entire capital gain realised from its entry into force, even if it accrued before that time.

Only when the DRD regime was actually applied

According to draft Program law, the separate tax is only applicable to the extent that the dividends distributed on the relevant shares were, 'in at least one of the previous taxable periods', deducted from profits under the DRD regime. Given that this is a subjective criterion, it must be assessed whether the company in question actually claimed DRD on (the eligible part of) the dividends received from the regulated investment or real estate company in its corporate income tax return (or non-resident corporate tax return).

It follows that the separate tax will not apply if no DRD was applied to the dividends from the transferred shares. Given the annual distribution obligation of the companies concerned (see above), this exception will probably only be relevant in practice in cases of short-term capital gains (where no dividends have been distributed yet), or if a corporate investor forgot to claim the DRD, or failed to do so due to a lack of knowledge about the DRD-coefficient. It also appears that any dividends received *during* the taxable period in which the capital gain is realized are not taken into account (since the draft Program law explicitly refers to 'one of the previous taxable periods'). Hence, it seems that the separate tax can be avoided if the DRD was only applied to dividends received in the same year as the sale (but not earlier).

Separate assessment

The new 'levy' thus takes the form of a separate tax assessment equal to 5% of the total amount of realised capital gains (to the extent exempted under Article 192, §1 ITC 1992; cf. supra).

The nature of a separate tax assessment means that these gains will always be taxed — regardless of the taxable result of the corporate investor or the presence of tax attributes, such as carry forward losses.

Capital losses incurred on (other) shares in the relevant investment or real estate companies are not deductible from the tax base for this separate tax assessment.

Conditional withholding tax credit

In addition to the new tax of 5%, the Program law also provides for a change to the withholding tax credit system for corporate investors receiving dividends from the investment- or real estate companies referred to in the draft Program law (new art. 282/1 ITC 1992).

Currently, withholding tax on these dividends is in principle fully creditable.

Going forward, the corporate investor will no longer be able to offset withholding tax against corporate tax on the portion of dividends that 'is deducted' from profits as DRD (cf. aforementioned DRD-coefficient). However, this non-creditability is not applicable in case, during the relevant taxable period, the company paid to at least one director the minimum remuneration required under Article 215, third indent, 4° of the ITC 1992. This refers to the minimum remuneration that 'small' companies should pay in order to qualify for the reduced corporate income tax rate (20% on the first tranche of EUR 100,000 of profit). The current amount is EUR 45,000 (although a lower amount is allowed, provided that it is at least equal to the result of the taxable period). However, this threshold would be raised to EUR 50,000 and would also become subject to indexation going forward.

Since the current withholding tax rate is 30%, the non-credibility of this withholding tax (if the aforementioned exception does not apply) results in a higher tax rate than the corporate income tax rate applicable to the taxable portion of the dividends (ie 25%, or possibly the reduced rate of 20%).

Granting the minimum director's remuneration may therefore become relevant not only for companies that qualify as small companies (cf. the scope of application for the reduced corporate income tax rate; Art. 215, second indent ITC 1992), but also for other companies that invest in the aforementioned investment and real estate companies.

An exclusion is provided for recognised cooperative companies (new Art. 281/1, §2 ITC 1992): they may continue to credit the withholding tax, without any requirement to grant the minimum director's remuneration. The explanatory memorandum justifies this by noting that these companies are not subject to the minimum remuneration condition to qualify for the reduced tax rate (Article 215, third indent, 4° ITC 1992). However, the reduced rate only applies to recognized cooperatives that qualify as small companies, whereas the exemption to the non-creditability of withholding tax applies generally (and therefore also applies to 'large' cooperative companies).

Since this conditional withholding tax credit applies to dividends from the aforementioned investment and real estate companies, this measure — contrary to the separate tax assessment (see above) — will have a significant impact on investments in classic DRD Funds, if the corporate investor does not grant the minimum director's remuneration.

Entry into force

The draft Program law stipulates that the new separate assessment and conditional creditability of withholding tax will apply 'from assessment year 2026'.

Consequently, for most companies a quick sale will not provide relief from the separate tax. However, companies whose financial year ends before 31 December 2025 (and is therefore linked to assessment year 2025) may still be able to avoid the new tax by selling their shares within the current financial year.

Note that any change made from 3 February 2025 to the closing date of the financial year is rebuttably presumed to be intended to avoid the application of the new assessment. Such change will therefore remain without effect unless the taxpayer can justify the change by motives other than avoiding the separate assessment.

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