International Tax | 6 June 2018

Netherlands tax alert

Legislative proposal contains broad changes to fiscal unity regime

On 6 June 2018, the Netherlands Ministry of Finance published a legislative proposal that contains measures to bring the Dutch fiscal unity regime in line with the "per element" approach taken by the Court of Justice of the European Union (CJEU) in its decision issued on 22 February 2018 (for prior coverage, see ***World Tax Advisor***, 9 March 2018). According to the proposed measures, certain tax rules would be applied ignoring the existence of a Dutch fiscal unity. Most provisions are intended to apply retroactively as from 25 October 2017.

Background

The Dutch fiscal unity regime allows members of a Dutch group (only Dutch taxpayers may be part of the group) to be treated as a single entity for corporate income tax purposes. The regime entails an attribution of income, assets, liabilities and activities of a Dutch taxpayer to its Dutch parent company (provided there is a legal and economic relationship of at least 95% between the companies and certain other requirements are met). As a result of this attribution ("consolidation"), certain "tainted" loans and tainted transactions and participations held by fiscal unity members are disregarded.

In its February 2018 decision (involving two joined cases), the CJEU held that the Netherlands may not deny certain benefits ("elements") of the fiscal unity regime in EU situations simply because EU-resident companies are not allowed to be included in a fiscal unity.

The Dutch State Secretary of Finance already released a letter (in October 2017, following the issuance of the opinion of the advocate general of the CJEU) announcing that emergency remedial measures would be taken to eliminate specific discriminatory advantages of forming a fiscal unity in domestic situations, rather than extending the benefits of the regime that apply in domestic cases to comparable EU cases. These measures would resolve the discriminatory aspects of the fiscal unity regime by denying the fiscal unity benefits in domestic situations.

Emergency remedial measures

According to the legislative proposal, a fiscal unity would be deemed not to exist for purposes of the application of specific provisions in the Corporate Income Tax Act (CITA) and the Dividend Withholding Tax Act (DWTA). Specifically, the following rules would be applied as if no fiscal unity exists:

- Related party financing rules (article 10a CITA);
- Excessive participation financing rules (article 13l CITA);
- Portions of the participation exemption (article 13 (paragraphs 9-15 and 17) CITA);
- Mandatory revaluation of low-taxed portfolio investments (article 13a CITA);
- Limitation of loss compensation rules (article 20a CITA); and
- Specific withholding tax reduction (article 11 DWTA).

Due to the retroactive nature of the proposed rules, the emergency remedial measures would affect existing fiscal unities.

Related party financing rules

Article 10a CITA provides that interest expense on related party debt is nondeductible if the debt is connected with certain “tainted” transactions (i.e. dividend distributions, repayments of capital, capital contributions or acquisitions), unless the taxpayer can demonstrate that there are business reasons for the transaction or the corresponding interest income is sufficiently taxed according to Dutch standards. Under the proposed measures, if a loan is obtained from a related party outside the fiscal unity to finance a tainted transaction within the fiscal unity, the transaction would become regarded for tax purposes and the loan would fall within the scope of article 10a CITA. The same would apply to a loan obtained from a related party within the fiscal unity if the loan is linked to a tainted transaction within or outside the fiscal unity.

It should be noted that the proposal specifically states that even though, due to the consolidation, the interest expense, in effect, would not be taken into account at the level of the fiscal unity, the nondeductible interest expense would be added to the results of the fiscal unity, unless the taxpayer is able to invoke one of the exceptions to the application of the article 10a rule. An exception could apply if, with respect to loans obtained from related parties within the fiscal unity, the taxpayer can show that a sufficient compensating levy exists, provided no loss carryforward can be applied. Article 10a also can be avoided by eliminating the tainted loan, such as through a legal merger or capitalization of the tainted loan, although it should be noted that there is no guidance on whether it is possible to “untaint” a tainted loan where the tainted transaction is eliminated in these situations.

A “grandfathering” rule would apply for purposes of article 10a, but only if the overall interest expense of the fiscal unity did not exceed EUR 100,000 during a 12-month period.

Participation financing rules

Article 13l CITA limits the deductibility of interest expense on all debt that is deemed to finance investments in subsidiaries. In many cases, the effects of the rule are limited if the taxpayer can demonstrate that the acquisition of a subsidiary was made in the context of expanding the group's operational activities. However, this "safe harbor" rule does not apply in the case of a tax planning structure.

In many cases, a Dutch holding company has debt, and Dutch operating activities may be structured in another group company. Until the emergency remedial measures become effective, interest expense on such debt may be fully deductible because the debt is deemed to first finance the business assets of the operating group member. The remedial measures would require the taxpayer to ignore the fiscal unity when applying article 13l, with the result that interest expense could become nondeductible. This result also could apply to loans obtained from related parties in the same fiscal unity (as with article 10a). One benefit, however, is that the threshold of deductible interest of EUR 750,000 would be applied per entity.

Future of fiscal unity regime

Other aspects of the Dutch fiscal unity regime potentially may be contrary to EU law, so further remedial measures may be announced in the future. It is not yet clear how the per element approach will apply to the EBITDA that will be included in the CITA as from 1 January 2019 as part of the Netherlands' implementation of the EU anti-tax avoidance directive. Given the possible challenges to fundamental features of the fiscal unity regime, the government is considering the introduction of a new regime.

Comments

The proposed remedial measures are unprecedented in terms of their potential impact in conjunction with the retroactive effective date, and likely will adversely affect all Dutch fiscal unities in some (potentially significant) way. Despite criticism by businesses, practitioners and members of parliament, the government has chosen to pursue the route of denying fiscal unity benefits to Dutch taxpayers to eliminate the breach of EU law, since granting the elements of the fiscal unity as benefits to non-Dutch persons would create an unacceptable monetary burden for the treasury.

Although it is possible that the parliamentary process to approve the proposed measures may take some time, the proposals are likely to be enacted within the next few months.

Contacts

If you have any questions or would like additional information on the topics covered in this alert, please email one of the following Deloitte professionals:

Corina van Lindonk
cvanlindonk@deloitte.nl

Jasper Korving
jkorving@deloitte.nl

Marie Oudemans
moudemans@deloitte.nl

Additional resources

Global Tax Alerts subscription page

Global Tax Alerts archive

World Tax Advisor

Deloitte International Tax Source (DITS)

Deloitte tax@hand app

Dbriefs

www.deloitte.com/tax