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Global Tax Alert

The Netherlands publishes 2020 budget proposals

Executive summary

On 17 September 2019, the Dutch Government published the Dutch budget proposals (the Proposals) for fiscal year 2020.

The Proposals include, among other items: (i) a limitation in the reduction of the headline corporate income tax (CIT) rate; (ii) an amendment to the domestic dividend withholding tax exemption and controlled foreign corporation (CFC) rules; (iii) an amendment to the domestic definition of permanent establishment (PE); and (iv) minimum capital requirements for banks and insurance companies as of 2020. Also, a conditional withholding tax (WHT) on interest and royalties to low-taxed jurisdictions or countries put on the European Union (EU) list of non-cooperative jurisdictions and in abusive situations is proposed as of 2021. At the same time, an amendment to the liquidation loss rules is announced as of 2021.

Detailed discussion

Proposals that will enter into force as of 1 January 2020

CIT rate

As part of the 2019 Budget Plan, the headline statutory CIT rate would be reduced to 22.55% in 2020 and 20.5% in 2021. It is now proposed to limit the reduction and maintain the headline CIT rate of 25% in 2020 and reduce it to

21.7% in 2021. The CIT rate for the first €200,000 shall – in line with the 2019 Budget Plan – be gradually reduced to 16.5% in 2020 and to 15% in 2021.

Domestic dividend WHT exemption

It is proposed to amend the anti-abuse rules to apply the domestic dividend WHT exemption. Currently, meeting specific substance requirements is a safe harbor to determine that the arrangement is not abusive. Following recent EU Court of Justice case law,[1] meeting these substance requirements shall no longer function as a safe harbor, but rather as a presumption of proof for non-abusive arrangements as of 1 January 2020. Even if the substance requirements are met, the Dutch tax inspector can demonstrate that an arrangement is abusive. Please note that irrespective of the substance, the taxpayer can via other means demonstrate the non-abusiveness of arrangements.

CFC rules

Under the Dutch CFC rules, a subsidiary or PE in a low-taxed jurisdiction or country put on the EU list of non-cooperative jurisdictions shall not be considered a CFC if it performs substantive economic activities. This should for example be the case if specific substance requirements are met. For financial years starting on or after 1 January 2020, meeting these substance requirements shall no longer function as a safe harbor, but rather as a presumption of proof of substantive economic activities.

Definition PE and Permanent Representative

It is proposed that the domestic definition of PE and permanent representative shall be aligned with the respective bilateral tax treaty. It is important to note that the Netherlands made a reservation to Article 12 of the *Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting* (the MLI) that targets the artificial avoidance of PEs through commissionaire arrangements.[2] If no tax treaty applies, a domestic PE and permanent representative definition is proposed in line with the Organisation for Economic Co-operation and Development's MLI definition combating the artificial avoidance of a PE or permanent representative.

Minimum capital requirements for banks and insurance companies

A minimum equity rule is proposed that would restrict the deductibility of interest for banks and insurance companies that have a license issued under the *Dutch Financial Supervision Act* and are excessively leveraged (i.e., equity ratio less than 8%).

Other proposals

- The Netherlands shall implement the EU Anti-Tax Avoidance Directive 2 covering hybrid mismatches. These rules aim to limit the deductibility of payments by or to hybrid entities or on hybrid financial instruments that result in a double deduction or a deduction without an inclusion. An EY Global Tax Alert with a detailed discussion of the proposal is forthcoming.
- The unilateral decree under the Netherlands-United States tax treaty regarding hybrid entities (CV/BV Decree) shall be repealed as of 1 January 2020. As a result, dividend distributions by a Dutch resident entity to a reversed hybrid entity, such as CVs, may become subject to 15% Dutch dividend WHT.
- Under the EU Mandatory Disclosure Rules (DAC 6) that the Netherlands will also implement, EU intermediaries (for example, tax advisors, accounts, bankers) are required to report potentially aggressive tax arrangements to the Dutch tax authorities if they are involved in such arrangements.[3]
- The Dutch tax authorities shall no longer calculate tax interest if the CIT return is filed on time and the CIT assessment is in line with the CIT return filed. At the same time, no payment discount is granted for payments on preliminary CIT assessments.
- On 1 July 2019 the MLI entered into force with respect to the Netherlands. As a result, the MLI shall in general have effect on covered tax agreements as of 1 January 2020 provided the other jurisdiction also timely ratified.
- Dutch intra-group financing and licensing companies may need to comply with additional substance requirements to mitigate exchange of information with other jurisdictions.

Proposals that will enter into force as of 1 January 2021

Conditional WHT on interest and royalties

As of 1 January 2021, a WHT is proposed on interest and royalty payments to group companies that are resident in a jurisdiction with:

- A statutory tax rate lower than 9%
- A jurisdiction that is included on the EU list of non-cooperative jurisdictions

  Or
- In certain abusive situations

Under the proposed WHT, accrued, imputed or paid interest and royalties by Dutch resident entities are subject to a WHT equal to the headline CIT rate (21.7% in 2021) irrespective of whether these payments are deductible for CIT purposes. Note that having (relevant) substance in either the Netherlands or in the receiving jurisdictions does not provide for an exception to the proposed rules.

Anti-abuse rules combat interposing conduit companies in non-low taxed jurisdictions if these intermediate conduit companies do not meet certain substance requirements or in the absence of actual economic activities. As discussed above under the Domestic dividend WHT exemption, the Dutch substance requirements shall become a presumption of proof that an arrangement is not abusive.

With respect to low-taxed jurisdictions with whom the Netherlands has concluded a bilateral tax treaty, a three-year grandfathering rule shall apply. Within this grandfathering period, the Netherlands shall approach the treaty partner to amend the respective tax treaty.

Liquidation loss

Currently, liquidation losses with respect to subsidiaries and PEs are deductible under restrictive conditions. Amendment of the liquidation loss rules as of 2021 is announced in the Proposals. Potentially, a liquidation loss may only be claimed as of 2021 regarding subsidiaries and PEs in EU/European Economic Area jurisdictions, in which the Dutch taxpayer has a qualifying interest of at least 25% and must in general be taken within three years after the operations cease or the decision to cease the operations is made. Such amendment was also announced previously, and actual draft legislation will be forthcoming during 2020.

Innovation box

The proposals announce that the effective tax rate under the innovation box shall be increased from the current 7% to 9% as of 1 January 2021.

Endnote

1. See EY Global Tax Alert, *CJEU rules on application of Danish withholding tax on dividends and interest payments*, dated 26 February 2019.
2. See EY Global Tax Alert, *Dutch House of Representatives approves MLI*, dated 15 February 2019.
3. See EY Global Tax Alert, *The Netherlands publishes draft proposal on Mandatory Disclosure Rules*, dated 26 July 2019.

For additional information with respect to this Alert, please contact the following:

Ernst & Young Belastingadviseurs LLP, International Tax and Transaction Services, Amsterdam

- Danny Oosterhoff danny.oosterhoff@nl.ey.com
- Dirk Stalenhoef dirk.stalenhoef@nl.ey.com

Ernst & Young Belastingadviseurs LLP, International Tax and Transaction Services, Rotterdam

- Michiel Swets michiel.swets@nl.ey.com

Ernst & Young LLP (United States), Netherlands Tax Desk, New York

- Simone Admiraal simone.admiraal1@ey.com
- Rik Jansen rik.jansen@ey.com
- Tim Clappers tim.clappers@ey.com
- Annelien Dessauvagie annelien.dessauvagie@ey.com
- Max t Hart max.t.hart1@ey.com

Ernst & Young LLP (United States), Netherlands Tax Desk, Chicago

- Sebastiaan Boers sebastiaan.boers1@ey.com
- Martijn Bons martijn.bons2@ey.com
- Henrik Stipdonk henrik.stipdonk2@ey.com

Ernst & Young LLP (United States), Netherlands Tax Desk, San Jose/San Francisco

- Dirk-Jan (DJ) Sloof dirkjan.sloof@ey.com
- Laura Katsma laura.katsma2@ey.com

Ernst & Young (China) Advisory Limited, Netherlands Tax Desk, Beijing

- Yee Man Tang yeeman.tang@cn.ey.com

Ernst & Young Tax Services Limited, Netherlands Tax Desk, Hong Kong

- Miranda Baas miranda.baas@hk.ey.com
- Joost Huisman joost.huisman@hk.ey.com

Ernst & Young LLP (United Kingdom), Netherlands Tax Desk, London

- Randall Hornberger randall.hornberger@uk.ey.com
- Celeste Krens celeste.johanna.krens@uk.ey.com

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