New Dutch government to scrap dividend withholding tax and lower corporate income tax rates

After more than 200 days of negotiations following the Dutch general elections in March 2017, a coalition of four political parties have agreed to form a new government. The coalition agreement, which contains the joint policy decisions that the incoming government intends to execute during its four-year term, was made public on 10 October 2017. Of particular interest in the field of corporate taxation are the following measures:

- abolition of the dividend withholding tax
- phased reduction of the headline corporate income tax rate from 25% to 21% between 2019 and 2021
- introduction of an "anti-abuse" withholding tax on dividends, royalties and interest paid to very low tax jurisdictions
- certain steps to protect the Dutch corporate income tax base.

Although the coalition agreement does not provide details of these measures, it does provide much food for thought on how these changes could possibly benefit or affect corporate structures and transactions. To give you some indication of the potential tax impact, we have prepared a Q&A. Further guidance will become available during the legislative process.

QUESTIONS & ANSWERS

What are the key implications of the abolition of the Dutch dividend withholding tax?

It will make Dutch companies more attractive, in particular because it will take away any Dutch dividend withholding tax leakage in relation to foreign retail shareholders and remove administrative burdens. Currently, all shareholders are, in principle, liable to 15% Dutch dividend withholding tax in respect of dividends paid by a Dutch resident company.
In practice, however, dividend withholding tax is borne almost exclusively by non-resident retail shareholders. These non-resident shareholders may be able to claim a full or partial refund or exemption of the Dutch dividend withholding tax (under either a tax treaty or Dutch domestic law) or they may be able to claim a credit for the tax in their country of residence. Frequently, however, a full home country credit is not available. In addition, for Dutch companies and their shareholders, the process of withholding and claiming reductions, exemptions and credits gives rise to administrative burdens. Abolition of the Dutch dividend withholding tax removes all of these disadvantages.

How will dividends be taxed until the abolition of the Dutch dividend withholding tax?

The coalition agreement does not specify the precise effective date of the abolition but seems to suggest that this measure will take effect as of 2020. The above timeline gives an overview of the treatment of dividends distributed by Dutch companies until abolition of the dividend withholding tax. The overview takes into account the proposed changes as of 1 January 2018 as laid down in the Dutch Tax Bill 2018 published on 19 September this year. These changes have not yet been passed by Dutch parliament, leaving open the question of whether these measures will still be implemented in the form presently proposed in light of the upcoming abolition of the Dutch dividend withholding tax. The coalition agreement does not provide any guidance in this respect.

Can distributions before abolition be made without Dutch dividend withholding tax?

Yes, if one of the current forms of relief or, if adopted, extended source exemptions apply. Alternatively, companies could opt to repay share capital or issue bonus shares out of recognised share capital or premium, if available, in order to mitigate Dutch dividend withholding tax. As of abolition, having recognised share capital or premium becomes irrelevant for Dutch dividend withholding tax purposes.

What are the key implications of the new "anti-abuse" withholding tax on dividends, interest and royalties?

The coalition agreement, and specifically the announced "anti-abuse" withholding tax clearly demonstrate an intention to reduce the attractiveness of the Netherlands as a passive flow-through jurisdiction, while also seeking to further improve the country's attractiveness for active business operations and headquarters. However, the coalition agreement does not offer guidance on the timing and details of the new withholding tax rules; for instance, it is currently unclear what the relevant tax rate(s) will be, when a jurisdiction will qualify as "low tax", and (only with respect to dividends) what situations will be regarded as abusive. The coalition agreement assumes that no revenues will be raised through this new withholding tax, apparently because the new Dutch government expects that the relevant companies will either restructure or relocate these activities.

In the context of countering tax avoidance through the use of tax havens, the coalition agreement also proposes the introduction of a blacklist of non-cooperative jurisdictions.
and a country-by-country reporting obligation for multinationals on their activities in blacklisted jurisdictions and EU member states, the latter presumably to facilitate transparency towards EU partners.

**How will the CIT rate reduction be implemented?**

The table below provides an overview of the phased reduction of the headline corporate income tax rate in the period between 2018 and 2021:

<table>
<thead>
<tr>
<th>Year</th>
<th>Taxable income &gt; EUR 200,000</th>
<th>Taxable income &lt; EUR 200,000</th>
</tr>
</thead>
<tbody>
<tr>
<td>2018</td>
<td>25%</td>
<td>20%</td>
</tr>
<tr>
<td>2019</td>
<td>24%</td>
<td>19%</td>
</tr>
<tr>
<td>2020</td>
<td>22.5%</td>
<td>17.5%</td>
</tr>
<tr>
<td>2021</td>
<td>21%</td>
<td>16%</td>
</tr>
</tbody>
</table>

**What will change on the corporate income tax base rules?**

The coalition agreement provides for the following changes to the Dutch corporate income tax base rules:

- as was known already, a new earnings stripping restriction on deduction of interest, implementing the mandatory EU Anti-Tax Avoidance Directive, will be introduced as of 1 January 2019. Under this new restriction, net interest costs will not be deductible to the extent that they exceed 30% of the EBITDA for tax purposes. The coalition agreement states that the incoming government will apply a de minimis threshold of EUR 1m and will not provide for a group ratio exception. According to the coalition agreement, certain existing statutory restrictions will be repealed;
- the introduction of a thin cap rule for banks and insurers affecting interest deduction for debts in excess of 92% of the aggregate assets on the commercial balance sheet, because these institutions are generally not captured by the earnings stripping restrictions;
- carry forward of tax losses will be limited to 6 years as opposed to 9 years;
- profits derived from intangibles that qualify for the innovation box will be taxed at an effective rate of 7% rather than the current 5% rate;
- the duration of the "30% regime" for incoming skilled expats will be reduced from 8 to 5 years. This regime allows for a fixed 30% allowance for Dutch wage tax and income tax purposes and an effective base exemption from Dutch net wealth tax for investments held outside the Netherlands;
- the depreciation floor for real estate used for group operations will be increased from 50% to 100% of the WOZ value.

**What about the tax treatment of Dutch fiscal investment institutions?**

Although abolition will generally increase the attractiveness of investing in Dutch companies and Dutch funds, it also raises two other points. First, Dutch fiscal investment institutions (FBIs) are widely used as investment funds for Dutch retail investors because they facilitate a tax-neutral treatment through a 0% corporate income tax rate, combined with a remittance discount regime, which allows an effective and neutral treatment of withholding taxes on underlying portfolio investments. This remittance discount regime entails that, although FBIs are currently required to withhold 15% Dutch dividend withholding tax, they can set off Dutch and foreign withholding taxes on dividends and interest (up to 15%) paid to the FBIs against the Dutch dividend withholding tax that they withhold from distributions to investors and they would otherwise have to remit to the Dutch revenue. Dutch retail investors receive a full credit or refund of the Dutch dividend withholding tax, including for the part that was actually not remitted pursuant to the
remittance discount. Abolition of the Dutch dividend withholding tax would, in principle, render the remittance discount regime ineffective. The coalition agreement does not provide any guidance regarding a solution for Dutch retail investors in this respect. We would, however, expect that alternative measures with similar effects will be put in place as part of the legislative proposal abolishing the Dutch dividend withholding tax.

Second, FBIs - listed and private - are also widely used as Dutch real estate investment funds. According to the coalition agreement, FBIs will no longer be allowed to directly invest in real estate, which could have a major effect on, in particular, widely-held listed and non-listed Dutch real estate investment companies or funds currently applying the FBI regime. These would become subject to Dutch corporate income tax unless they restructure into tax transparent vehicles, which will be challenging for listed or other widely-held FBIs.

What are the next steps?
The coalition agreement published yesterday represents the joint policy decisions of the four parties that will form the new government. The new government will have to submit legislative proposals to adopt the measures set out in this Legal Alert, including the abolition of the Dividend Tax Act 1965, to the Dutch parliament. It is at this stage, however, not clear when the legislative proposals will be submitted.

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