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Dutch Tax Plan 2022

Tax Plan 2022: Initial observations

On 21 September 2021, the Dutch government announced its Tax Plan 2022, which includes proposals for certain amendments in Dutch tax law. Since the current government is demissionary and in negotiation to form a new coalition government after the general elections last March, the demissionary government is restricted from making major political decisions. Consequently, the proposals in the Tax Plan 2022 are less controversial in nature and most of the more impactful proposals seem to have been pushed to the next government. Notwithstanding, we have outlined the most relevant developments in this alert and flagged items that have been tabled for now.

As a next step, the measures announced today will be discussed in Parliament in the coming weeks and, when approved, most of the new rules will be implemented effective 1 January 2022 (unless indicated otherwise). In addition to the plans announced today, we note that a limitation on offsetting tax losses was adopted earlier in the year and will also become effective 1 January 2022.

Should you be interested to learn more about any of these developments, please reach out to your Baker McKenzie contact.

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Excess Dutch dividend withholding tax no longer refunded

Refunds of Dutch withholding tax limited after EU Sofina Case

The Dutch government acknowledges that Dutch corporate taxpayers are treated more beneficially in comparison to foreign corporate investors when it comes to crediting Dutch dividend withholding tax, typically levied on their portfolio investments (<5%).

Currently, when applicable, Dutch corporate taxpayers can credit Dutch dividend withholding tax levied against their Dutch corporate income tax due. Any excess Dutch dividend withholding tax is refunded to the Dutch corporate taxpayer. Such refund is typically not available for foreign corporate taxpayers who own a less than 5% shareholding or who cannot otherwise invoke the Dutch dividend withholding tax exemption, though reference is made to the temporary measure in the decree referred to below.

Sofina Case

Following the European Sofina case law, the Dutch government now proposes to limit the credit of Dutch dividend withholding tax to the Dutch corporate income tax due. Any excess is no longer refundable but will instead be carried forward indefinitely. Certain limitations to the utilization of such carried forward excess dividend withholding tax are proposed with respect to the Dutch fiscal unity regime or in case of reorganizations such as a legal merger. If adopted, these rules will apply per 1 January 2022.

The Dutch government had already acknowledged the potential infringement with EU law before. Hence, in November 2020 the Dutch government published a decree based on which EU/EEA corporate shareholders can under conditions temporarily receive a refund of excess Dutch dividend withholding tax. Contrary to this decree, the current proposal seeks a balanced treatment by instead limiting these refunds also to Dutch taxpayers. Therefore, that decree will be abolished when the new rules enter into force.

Practical impact assessment

The change in rules was expected and it will further align the tax treatment of Dutch and foreign corporate investors investing for less than 5% interest in Dutch companies or in case the Dutch dividend withholding tax exemption does not apply.

R&D-Wage Tax Reduction Simplified

Clarification and simplification of the R&D-Wage Tax reduction application system

If your business carries out research and/or development projects you may be able to make use of the research and development tax credit, the so-called R&D-wage tax reduction. The R&D-wage tax reduction entitles companies to pay lower wage tax and lower national insurance contributions if certain conditions are satisfied. Furthermore, self-employed entrepreneurs can deduct an (annually set) fixed amount for R&D when filing their income tax return. The proposed changes will make the application system more user-friendly. A decision on material changes to the R&D-wage tax reduction scheme (e.g. rates and brackets) is deferred to the next Dutch government.

Simplifications and Clarifications

The Dutch Tax Plan 2022 includes the following changes to simplify and clarify the R&D-wage tax reduction system as of 1 January 2022:

i. A taxpayer will be permitted to apply for the R&D-wage tax reduction facility applicable for the next calendar month, even if that same calendar month has already been included in a previous R&D declaration. This change allows the taxpayer to better anticipate to new R&D projects and to include additional expected hours, costs and expenses for R&D projects that are already granted. The maximum of four applications per year has not changed.

ii. All issued R&D declarations will relate to the remaining calendar months of that year. This amendment simplifies the preparation of the notification which has to be submitted by the taxpayer within three months after the calendar year.

iii. An R&D withholding agent will be allowed, for each tax return period to which a R&D declaration relates, to deduct a self-determined amount of the granted R&D-wage tax reduction. The maximum of the deduction is the amount of the owed payroll tax for that tax return period and to the extent that this part has not already been taken into account during an earlier tax return period.

iv. It is clarified that only costs and expenses that have been applied for and for which an R&D-wage tax reduction has been granted can be included in the notification. The reason for this clarification is that it should be avoided that costs and expenses for which an R&D-wage tax reduction has *not* been granted are included in the notification since these costs and expenses have not been assessed against the conditions of the Salaries Tax and National Insurance Contributions Act (*Wet vermindering afdracht loonbelasting en premie voor de volksverzekeringen*).

Practical impact assessment

The simplification and clarification of the R&D-wage tax reduction system is a welcome improvement, also because the R&D-wage tax reduction (and R&D declaration) is a critical entry ticket for applying the Dutch innovation box regime. We assist clients on a daily basis with securing the abovementioned benefits provided for in Dutch tax law with respect to research and/or development activities and we believe the proposed changes to the will make the R&D-wage tax reduction application process even more efficient.

Mandatory method for applying foreign tax credits under CFC regime

Applying foreign tax credits under CFC regime clarified

Since 1 January 2019, the Netherlands apply a limited controlled foreign company (CFC) regime. Under the CFC regime certain categories of undistributed tainted income, such as royalties, realized by a controlled subsidiary in a listed low-tax jurisdiction, are included in the Dutch taxable basis annually. However, foreign taxes payable by such controlled subsidiary are -under certain circumstances- creditable against the Dutch corporate tax due. Such credit is limited to the Dutch corporate tax due. If the foreign tax to be credited exceeds the Dutch corporate tax due, the excess can be carried forward. In case a Dutch taxpayer owns multiple CFCs, the creditable foreign tax is calculated per CFC separately. If there are multiple CFCs, Dutch law currently does not prescribe the order in which foreign taxes are credited in case the aggregate of the foreign tax per CFC exceeds the Dutch corporate tax due.

The Dutch government proposes to apply a mandatory order to credit foreign taxes per 1 January 2022 in case there are multiple CFCs. This order adheres to the amount of the creditable foreign tax and is ascending, so the smallest creditable foreign tax is credited first. Excess creditable foreign taxes after the application of proposed rule, can be carried forward under the regular existing rules.

Practical impact assessment

The mandatory order provides for a pragmatic solution in case a Dutch corporate taxpayer has multiple CFCs subject to the Dutch CFC regime. The practical impact of this clarification is expected to be limited.

Reverse hybrid entities to become subject to Dutch tax

Implementing the last stage of ATAD2

As the last stage of implementing the EU's Second Anti-Tax Avoidance Directive ("ATADII"), as of 1 January 2022 Dutch reverse hybrid entities will become subject to Dutch corporate income tax. This new rule is the latest in a series of measures aimed at reverse hybrid entities. It forms the implementation of the last part of ATADII in the Netherlands.

Dutch reverse hybrid entities become Dutch tax resident

Dutch reverse hybrids are entities that are disregarded for Dutch tax purposes ('fiscally transparent'), but that are regarded as a company in the jurisdiction of their shareholders or members ('fiscally opaque'). Under the new rule, reverse hybrids will become Dutch tax residents if they are currently established in the Netherlands or if they were incorporated under Dutch law. Consequently, these reverse hybrids will be subject to Dutch corporate income tax and effectively no longer 'hybrids'.

As Dutch tax residents, dividend distributions by these reverse hybrids will in principle become subject to Dutch dividend withholding tax, unless an exemption applies. Royalty and interest payments by these entities may be subject to the new 'conditional' withholding tax if such payment flows to a low-taxed or non-cooperative jurisdiction (this fairly recent (limited) withholding tax applies since 1 January 2021). On the other hand, the reverse hybrids, when becoming a Dutch taxpayer, will in principle also be entitled to benefits from tax treaties concluded by the Netherlands.

Practical impact assessment

Structures with reverse hybrid entities have already become less popular as a result of other introduced anti-hybrid measures. However, legacy reverse hybrid entities are still present in some structures and this addresses those entities left in the structure by taking out the hybrid element. Baker McKenzie Amsterdam is experienced in winding down reverse hybrid entities and offers advice and guidance on the best way forward.

Restrictions on arm's length corrections

Downward adjustments of profit may be restricted to prevent mismatches

As of 1 January 2022, downward arm's length adjustments of the profit of Dutch taxpayers in relation to transactions with affiliated parties will be denied if there is no corresponding upward adjustment at the level of the affiliated party. These restrictions were already announced last year on Budget Day 2020, and draft legislation was submitted for consultation in March 2021.

The arm's length principle prescribes that a company involved in intercompany transactions should apply terms and conditions in accordance with the *arm's length* standard appropriate to e.g. its functions, assets and risk profile.

To adhere to the arm's length principle, the Dutch tax system currently provides that income derived by a Dutch entity from intercompany transactions is subject to a downwards adjustment insofar such income exceeds the income as determined based on the arm's length standards. However, if no corresponding upward adjustment is applied at the foreign affiliated company, it may occur that part of the profits are not taxed anywhere. In those cases, the downward adjustment results in a transfer pricing mismatch and the abovementioned rule is targeting such mismatch.

Downward transfer pricing adjustments may be limited

Under the proposed legislation, downward transfer pricing adjustments of a Dutch taxpayer's taxable profit will be limited insofar a corresponding upward transfer pricing correction is not included in the taxable base of the foreign affiliated company. As a result, transfer pricing mismatches resulting from upward arm's length corrections will be eliminated. The burden to proof that an upward adjustment at the level of the foreign affiliated company took place will lie with the Dutch taxpayer that wants to claim a downward adjustment.

Regardless of various concerns voiced and objections filed as part of the consultation process, the proposal intends to limit future amortization deductions after January 2022 insofar the amortization results from a transaction that took place between 1 July 2019 and 1 January 2022 and the transaction would have been considered a transfer pricing mismatch, had these rules been in place at the time of the transaction.

Compared to the draft legislation that was submitted for consultation, the new law contains several additional provisions as clarification but do not materially limit the scope of the proposal.

Practical impact assessment

The new restrictions on downward arm's length adjustments will mean that Dutch taxpayers must take into account the transfer pricing adjustments of the affiliated foreign companies that they deal with. A proper and comprehensive transfer pricing documentation will be key in staying compliant and maintaining efficiency. A review of historic transactions may also be necessary to assess the impact of the proposed rules on determining the Dutch taxable base of entities that may be affected.

VAT OSS and IOSS simplified

Dutch VAT refunds through the OSS and IOSS made easier

As of 1 July 2021, the VAT Mini One Stop Shop (MOSS) has been extended to a variety of B2C supplies, resulting in the One Stop Shop (OSS). The MOSS allowed businesses that make B2C supplies of telecommunications-, broadcasting- and electronically supplied services to register for VAT in one Member State and to report and pay all EU VAT through that single Member State. This facility prevented businesses from the obligation to register for VAT in each Member State in which the VAT is due (i.e. the Member State of their B2C customer).

One Stop Shop

Under the new OSS, businesses are able to also report VAT for other B2C services, intra-Community distance sales of goods as well as certain domestic supplies of goods. This also includes businesses that are deemed to facilitate the supply through their electronic interface / online platform. In practice, this results in lower administrative burdens for business that operate throughout the EU.

Import One Stop Shop

In addition, as of 1 July 2021 businesses that sell goods to EU-based B2C customers (including businesses that are deemed to facilitate the supply through their electronic interface / online platform), and these goods are imported into the EU, such businesses can register for the Import One Stop Shop (IOSS). In cases where the intrinsic value of the consignment does not exceed EUR 150, the seller charges local EU VAT to his customer at the moment of checkout. As a consequence, the customer does not need to pay import VAT at the moment of delivery (often increased with handling costs by the carrier).

To make use of the OSS and IOSS facility, the business is required to obtain a registration in its Member State of identification, through which it declares the VAT. The Member State of identification then distributes the VAT to the right Member States. It can be the case that this results in a negative VAT amount for a business in a certain Member State, i.e. a receivable position. For example in case reported VAT needs to be corrected as a result of returns of goods. That would in principle require the business to lodge a VAT refund request in that particular Member State.

Under the legislative proposal that has been presented today, if such a situation were to occur in the Netherlands in respect of Dutch VAT, a correction that results in a negative Dutch VAT amount will automatically qualify as a request for a refund of Dutch VAT. This measure prevents the business to be required to file a formal VAT refund request in the Netherlands.

Practical impact assessment

Under today's proposal, refunds of VAT through the One Stop Shop and the Import One Stop Shop have been simplified. As such a VAT refund request still have certain formal and practical angles that should be considered, we're happy to discuss this with you in case this applies to your business.

Share option plans

Shifting the taxable moment from exercise to tradability

Taxation of employee stock options

Under current Dutch wage tax law, employee stock options are normally taxed at the moment when these option rights are exercised (or alienated). However, at exercise of a stock option, the employee does not always have (sufficient) liquid assets available to pay the wage tax due. This is especially true for the start-up and scale-up sector, where stock option rights are a common means to attract and retain staff.

The Tax Plan therefore contains a measure proposing a shift of the taxable moment of employee stock options to the moment when the shares acquired through the exercise of the option can be traded. After all, at that moment, part of the shares can be sold if necessary, providing the employee with the liquid assets needed to pay the wage tax due.

Since there is not a lack of liquid assets in all cases, the proposal also provides the employee with a choice to have the taxable moment remain at exercise (as it is now), provided additional conditions are met.

Practical impact assessment

This measure intends to make it more attractive for companies to use stock option rights as a compensation item. While the measure's primary focus is on start-ups and scale-ups, its application is much broader as it can in principle be applied in all situations where the shares are not tradable upon exercise of the option.

Other Income and Wage Tax

Key income and wage tax measures

Working from home cost reimbursement

During the COVID-19 pandemic, the Dutch government has urged employees who can work from home to do so as much as possible. Although a large proportion of these employees will likely start working (in whole or in part) in their offices again once this measure has been relaxed, it is expected that a substantial part of the workforce will still work from home for part of the week. Many employers have indicated that they wish to reimburse their employees for the extra costs associated with working from home. The Tax Plan therefore introduces a possibility for employers to grant such an allowance free of Dutch wage tax, by introducing a so-called "targeted exemption" under the Dutch work-related costs scheme (WKR). The cabinet considers an average of € 2 per day worked from home to be a realistic amount as compensation for the extra costs an employee incurs due to working from home. It therefore proposes to exempt from tax a fixed amount of maximally € 2 per day worked from home, or part thereof.

Temporary increase of the 'free space' under the work-related costs scheme

In accordance with the already published Decree on emergency measures for the COVID crisis, the cabinet intends to increase the so-called 'free space' under the Dutch work-related costs scheme (WKR) for the 2021 calendar year. The 'free space' is 3% of the total wages up to and including € 400,000, plus 1.18% of the total wages over this amount.

Reduced customary wages of director-major shareholders of innovative start-ups

As of 2017, the taxable wages of director-major shareholders of innovative start-ups may be set at the statutory minimum wages for the application of the Dutch customary wages scheme. This measure will be continued to January 1, 2023 and will then expire, unless the scheme is evaluated positively by the Ministry of Economic Affairs and Climate.

Lower addition to income for zero-emission cars

The cabinet continues to encourage the sale of emission-free passenger cars in 2022. This implies that the reduction of the addition to income for zero-emission cars will be maintained up to and including 2025. However, the maximum value of the car for which the additional tax credit applies is reduced. This means that the 6% reduction of the addition to income will be applied to a maximum value of €35,000 as from 2022, and to a maximum value of €30,000 as from 2023. For the amount above the maximum value, the normal addition rate of 22% applies. This measure i.a. intends to make cheaper emission-free cars attractive for the business market.

Levy rebates

The cabinet intends to phase out the employed person's tax credit more slowly than originally planned. This measure is expected to have a positive effect on workers, and to reduce the difference in purchasing power development between single and dual earners.

In addition, the maximum amount of the income-related combination tax credit (ICTC) will be reduced by € 395 as of 2022. Because this maximum amount had been increased by € 77 through a prior cabinet decision, an effective reduction by €318 of the maximum amount remains for 2022. Furthermore, it is proposed to equate the treatment under the ICTC of taxpayers with a partner living abroad who is not a qualifying non-resident taxpayer, with the treatment of taxpayers with a partner who is a resident taxpayer, or a qualifying non-resident taxpayer.

Other measures

Finally, the Tax Plan includes a number of technical measures, such as amendments to, and a clarification of the calculation method for the so-called 'deemed capital yield tax' (box 3), adjustments to the Dutch owner-occupied home scheme in partnership situations and in the event of death, a simplification of the system of the R&D contribution reduction under the Research and Development Work Promotion Act (WBSO), et cetera.

What is still to be expected?

Further legislative changes that are pushed to a later date or the next government

The Tax Plan 2022 includes some announcements on further legislative proposals that will be published in the coming months or that are being deferred to the next government.

Holding losses and the fiscal unity regime

In a 11 June 2019 judgment, the Dutch Supreme Court ruled that a grammatical interpretation of the current loss compensation rules, read in conjunction with the rules concerning the fiscal unity regime, permits the offsetting of operating profit with (prior) holding losses of the fiscal unity. The Tax Plan 2022 mentions that such outcome is not only contrary to the purpose and scope of the loss compensation rules (which generally do not permit the offsetting of operating profit with holding losses), the consequence of the judgment will also have a material budgettary impact if not adequately addressed. The government has announced that it will repair the current legislation when the government submits its Memorandum of Amendment to the "Other tax measures 2022"-bill in the next few weeks.

Technical changes to the Withholding Tax Act 2021

Aforementioned Memorandum of Amendment will also contain two technical changes to the Withholding Tax Act 2021. The first change will extend the definition of "permanent establishment" in the Netherlands for the purposes of the Withholding Tax Act 2021. As a result, withholding tax will also be levied on interest and royalty payments, insofar as the income is attributable to specific Dutch sources, such as real estate located in the Netherlands. The second change clarifies the role of "hybrid entities" as mentioned in the Withholding Tax Act 2021. Hybrid entities will no longer be liable for the applicable withholding tax if none of its ultimate beneficiaries (whether or not through a cooperating group) holds a qualifying interest. It is intended that this change will have retroactive effect to 1 January 2021.

What is not included?

In last year's Tax Plan it was announced that there would an investigation of a budget-neutral introduction of a capital allowance in combination with a further limitation of the earnings-stripping rule. The results of this investigation were published on 13 September 2021 and basically it was advised to refrain from implementing unilateral measures in this respect pending the EU DEBRA initiative. A decision following this study is also deferred to a next government.

The legislative proposal introducing a potential dividend withholding tax on exit has received significant press this past parliamentary session, but so far the proposal seems to be exactly where it was a year ago: "under construction”. While the proposal is currently tabled for discussion in the Dutch parliament, no date for the parliamentary debate has been set yet.

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