Budget day 2018: The most important changes for the Real Estate (RE) sector

The Netherlands: September 2018

In Brief

On 18 September 2018, the Dutch Ministry of Finance announced a number of important changes and amendments to the Dutch tax legislation for 2019 and onwards. In addition, the Dutch government introduced draft legislation to implement the EU Anti-Tax Avoidance Directive (ATAD) in the Netherlands. Furthermore, draft legislation was introduced which will abolish the current Dutch Dividend Withholding Tax Act and introduce a new conditional withholding tax on dividends payable to related parties that are established in low-tax jurisdictions or in specific cases of abuse.

The most important proposed changes

- starting in 2019, the corporate income tax (CIT) rate will be incrementally reduced to 22.25%;
- the loss carry-forward period will be reduced from nine to six years, the loss carry-back period of one year remains unchanged;
- the tax depreciation on buildings used within a business will be limited to 100% of the actual value as determined by the competent municipality (the so-called 'WOZ-value');
- article 13l regarding the interest deduction limitation for excess participation debt will be abolished;
- article 15ad regarding the interest deduction limitation for acquisition holdings will be abolished;
- article 20, paragraph 4 with respect to holding and financing losses will be abolished;
- the Fiscal Investment Institution (*fiscale beleggingsinstelling*) will no longer be allowed to invest directly in Dutch real estate as from 2020;
- implementation of the Anti-Tax Avoidance Directive (ATAD) in Dutch tax law;
- the Dutch Dividend Withholding Tax Act will be abolished from 2020;
- introduction of a conditional withholding tax on dividends paid to related parties established in low-tax jurisdictions, coming into effect from 2020;

Our observations relevant to the RE market

Decrease in corporate income tax rate and amendment of rules related to loss carry forward

The corporate income tax rate will be reduced to 22.25% (2019: 24.3%, 2020: 23.9% and 2021: 22.25%). The step up rate applicable to taxable profits up to €200,000 will be reduced to 16% (2019: 19%, 2020: 17.5% and 2021: 16%).

The loss carry-forward period will be reduced from nine to six years for losses incurred in book years commencing on or after 1 January 2019, the loss carry-back period of one year remains unchanged.

PwC observation: The change in the statutory corporate income tax rates also has an impact on the valuation of deferred tax assets and liabilities in the financial statements (as of the date the tax rate reduction has been 'substantively enacted', ie, the tax rate change has been approved by the Dutch Senate/"Eerste Kamer"). The deferred positions need to be analysed and revalued against the applicable rate (ie, against the tax rate in the year in which the respective part materialises). The change in value of the deferred tax position could have an impact on regulatory capital. For example for insurers, the maximum loss absorbing capacity of deferred taxes under Solvency II (LACDT) will decrease, which may impact the Solvency II ratio.

Tax depreciation on buildings

The depreciation for tax purposes of buildings used within a business will be limited to the actual (ie, 100 per cent) value as determined by the competent municipality (the so-called 'WOZ-value'). This restriction already applied to buildings kept as investments, but will now be extended to buildings used within a business. The consequence of this change is that companies will, in many cases, no longer be able to depreciate their buildings because depreciation will no longer be possible on buildings of which the tax book value is lower than the WOZ-value. If the book value of the building is lower than the WOZ value due to depreciation prior to 2019, there is no need to revalue.

For business taxed at the level of individuals, it will remain possible to depreciate up to 50 per cent of the WOZ-value.

PwC observation: The result of the restriction on tax depreciation on buildings used within the own business can be significant. An example can be the depreciation on a building used as a hotel by the owner/occupier. For tax payers, it may become more important to distinguish expenses as tax deductible maintenance costs rather than as capitalised investment.

Fiscal Investment Institutions (fiscale beleggingsinstelling) will no longer be allowed to invest directly in Dutch real estate

In order to protect the Dutch tax base on income and gains from Dutch real estate Fiscal Investment Institutions (FII) will no longer be allowed to invest in Dutch real estate directly as from 2020. As a result income from Dutch real estate investments held by listed and non-listed real estate funds (such as Real Estate Investment Trusts - REITS) will become subject to Dutch CIT at the ordinary rates.

PwC observation: This has a significant impact on the Dutch listed and non-listed RE fund industry. The FII regime is currently used by listed and non-listed real estate funds (such as REITs, and AIFs) as well as investment pooling vehicles held by institutional investors. FII's will have to reconsider their tax structure. Non-listed FII's with Dutch real estate are expected to be converted into tax transparent vehicles.

Abolition of Dutch dividend withholding tax and introduction of a conditional withholding tax

The current 15% dividend withholding tax is proposed to be abolished from 1 January 2020.

PwC observation: The main impact of the abolishment of the Dutch dividend withholding tax is that:

- *As from 2020, Dutch based companies will not have to withhold 15% withholding tax on dividends to shareholders. This mainly affects portfolio shareholders as dividends paid to non-portfolio shareholders in most cases already attract a dividend withholding tax exemption.*
- *The Dutch tax regime for Fiscal Investment Institutions (FII) is impacted by the abolition of the Dutch dividend withholding tax as (i) an FII is no longer allowed to invest in Dutch real estate and (ii) foreign withholding taxes can no longer be credited by an FII under the so-called 'afdrachtvermindering' rules.*

The introduction of a new withholding tax for dividend payments to low-tax or non-cooperative jurisdictions where the recipient holds a qualifying interest in the distributing entity, or where there is abuse, is proposed as from 1 January 2020.

It has been announced that the conditional withholding tax will be extended to interest and royalty payments to low-tax or non-cooperative jurisdictions where the recipient holds a qualifying interest in the payer, and in specific cases of abuse. This is not part of the current withholding tax proposal, but will be included in a separate legislative proposal in 2019.

Main characteristics of the conditional withholding tax on dividend payments

The new Dutch withholding tax will apply to dividend payments to recipients resident in

(1) low-tax, or

(2) non-cooperative jurisdictions which are included on the EU blacklist.

A low-taxed jurisdiction is defined as

(1) a jurisdiction that does not levy corporate income tax,

(2) a jurisdiction with a statutory corporate income tax rate of less than 7%, or

(3) a jurisdiction that is included on the EU list of non-cooperative jurisdictions in the field of taxation.

Anti-abuse measures with respect to intermediary companies which are interposed between the Netherlands and a low-tax jurisdiction are included. Dividend payments to intermediary companies which are set-up on the basis of genuine business reasons which reflect economic reality should not be subject to the conditional withholding tax, similar to the current anti-abuse rules included in the Dividend Withholding Tax Act.

Specific rules are introduced to cover dividend payments to (reversed) hybrid entities.

The conditional withholding tax rate will be tied to the corporate income tax rate, which, for the year 2020, will be 23.9%.

PwC observation: The introduction of the conditional withholding tax may need to be considered by investment funds and private equity funds, which own qualifying interests in Dutch companies, where the fund is based in a low-tax jurisdiction. Based on the proposal it seems that residency is broadly defined and it should therefore be assessed on a case-by-case basis whether or not a structure will be impacted by the proposed measures. In our view, the application of the conditional withholding tax rules to certain investment fund structures should be raised and addressed as part of the parliamentary hearings of the legislative proposal, particularly where it involves tax transparent fund structures.

Implementation of ATAD measures

In addition to the regular Budget Day proposals, the Dutch government issued a legislative proposal regarding the Dutch implementation of the ATAD. Below we have included an overview of the most important measures included in the proposal.

EBITDA –rules

As of 2019, net-interest expenses in excess of 30% of taxpayers EBITDA will generally be non-deductible for Dutch corporate income tax purposes. A threshold of €1m of net-interest expenses will be deductible regardless of the taxpayers EBITDA. Any non-deductible interest will be available for carry forward indefinitely.

The definitions of interest income and interest expenses are broad and, inter alia, include currency exchange results and costs relating to the issuance of the instrument.

The level of EBITDA and net-interest expenses is determined at fiscal unity level.

The ATAD provides EU Member States with the option to implement several exceptions to the EBITDA-rule. These options include:

(i) grandfathering for interest expenses on existing loans,

(ii) a group escape mechanism whereby interest is still deductible if certain group ratios are met,

(iii) an exemption for interest paid in relation to long-term infrastructure projects,

(iv) an exemption for financial institutions. The Dutch government has opted to provide for a grandfathering rule for existing Public Private Partnership projects but has decided not to include any of these other possible exceptions in the Dutch implementation of the EBITDA-rule.

A specific rule has been proposed to include capitalised interest in the scope of the EBITDA-rule.

Concurrent with the implementation of the generic EBITDA interest deduction limitation, several of the specific interest deduction limitation rules included in the Dutch Corporate Income Tax Act will be abolished. These will be the interest deduction limitation for acquisition vehicles (art. 15ad CITA) and the interest deduction limitation for excessive participation debt (art. 13l CITA). Notably the interest deduction limitation with respect to base erosion (art. 10a CITA) will not be abolished.

PwC observation: For real estate companies, the EBITDA-rule may have a significant impact, as contrary to current rules, the deduction of interest on third party (bank) loans may be restricted. Furthermore, it is key that the EBITDA-rule is applied at fiscal unity level as a result of which interest expense of holding companies in the fiscal unity can be netted with the interest income of operational companies. Finally, it may be relevant to assess whether any counterparties (such as borrowers from the bank) could be adversely impacted by these new rules on a net-cash basis (eg, in terms of their covenants, etc).

CFC rules

The ATAD provides two models through which so-called Controlled Foreign Company (CFC) rules could be implemented. Model A, whereby undistributed passive income of low-taxed subsidiaries of the taxpayer is included in the taxable base of that taxpayer and Model B, whereby undistributed income from low-taxed subsidiaries of the taxpayer arising from non-genuine transactions is included in the taxable base of that taxpayer.

The Dutch government announced that it will implement Model A with respect to CFCs established in low-taxed jurisdictions. A low-taxed jurisdiction is defined as a jurisdiction which does not levy corporate income tax, a jurisdiction with a statutory corporate income tax rate of less than 7%, or a jurisdiction included on the EU list of non-cooperative jurisdictions in the field of taxation.

Also, if the CFC is set-up on the basis of genuine business reasons which reflect economic reality, the CFC should not be impacted by this rule.

In other situations than those mentioned above, Model B will apply. The Dutch government have indicated that no changes to the legislation are required to implement Model B, given that art. 8b CITA already covers this.

PwC observation: The impact of CFC-rule for the RE-sector is likely to be limited given the definition of a low-taxed jurisdiction. Nevertheless, where Dutch based companies have subsidiaries in low-tax jurisdictions it should be carefully analysed whether the CFC-rules apply.

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