KPMG Meijburg & Co Tax & Legal

Year end 2021 tax accounting considerations

Dutch tax measures for 2022

November 2021

Introduction

On November 11, 2021, the Lower House of Parliament adopted the 2022 Tax Plan that was presented on September 21, 2021. It now needs to be adopted by the Upper House of Parliament to be considered substantively enacted.

Many of the proposed measures will take effect on January 1, 2022 or as from the financial year that starts on or after January 1, 2022. However, this could still impact the tax position of your 2021 financial statements when the proposed measures are (substantively) enacted before December 31, 2021.

This memorandum outlines the main tax accounting consequences of the 2022 Tax Plan under IFRS and the impact it may have on the tax position of your financials. Reference is also made to our [memorandum] released on September 21, 2021 for a complete overview and description of the tax measures of the 2022 Tax Plan.

Content

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1. Corporate income tax

1.1 Increase of corporate income tax rate

It is proposed to increase the headline corporate income tax rate to 25.8% (was: 25.0%) with effect from January 1, 2022. The 15% corporate income tax rate for the first bracket remains unchanged, however the brackets itself increases from EUR 245,000 towards EUR 395,000 as of January 1, 2022. For 2022, this results in the following:

Enacted 2020	2021	2022	Bill 2021	2021	2022
≤ € 245,000	15%		≤ € 245,000	15%	
≤ € 395,000		15%	≤ € 395,000		15%
> € 245,000	25%		> € 245,000	25%	
> € 395,000		25%	≤ € 395,000		25,8%

If the fiscal year differs from the calendar year, then the CIT rate will be a mixed percentage, depending on the days of the fiscal year in 2021 and the days of the fiscal year in 2022.

This will have an impact on the reported deferred taxes, as these will have to be remeasured once the tax rate changes have been (substantively) enacted.

The effect of the rate changes should generally be recorded in the profit and loss account. The effect of the rate change is recorded through OCI or directly in equity if the underlying item (or transaction) to which the temporary difference relates is previously recognized outside the profit and loss account.

Whether the increase of the CIT rates results in an increase or decrease of the Effective Tax Rate ("ETR") in 2021 depends on whether the company has recognized deferred taxes for deductible temporary differences and or tax losses (decrease ETR) or for taxable temporary differences (increase ETR).

Expected ETR impact =

Actions needed

Assessment of deferred tax assets and liabilities including if the resulting deferred tax adjustment relates to items previously recognized in the profit and loss account or outside the profit and loss account.

1.2 Tightening of earnings stripping measure

It is proposed to tighten the generic interest deduction limitation rules ("earnings stripping measure") for corporate income tax. This interest deduction limitation currently has the effect that the interest, on balance, payable by a taxpayer can only be deducted up to 30% of the EBITDA for tax purposes, or up to EUR 1 million if that is higher. It is proposed that the interest payable on balance will only be deductible up to 20% of the EBITDA for tax purposes. The threshold of EUR 1 million remains unchanged. The tightening will apply for the first time to financial years commencing on or after January 1, 2022.

The tightening of the earnings stripping measure might result in a change of the deferred tax asset ("DTA") to be recognized for interest available for carry-forward. This depends on the availability of sufficient (future) EBITDA and/or net interest income against which the carry-forward interest can be utilized.

Expected ETR impact =

Actions needed

Update reversal schedule for recognition DTA

1. Corporate income tax

1.3 Adjustment of pre-fiscal unity loss set-off against the profit of subsidiary included upon incorporation in the fiscal unity

Until January 1, 2019, specific provisions were in place limiting the utilization of holding and financing losses. Although these rules were canceled as of January 1, 2019, they still apply, pursuant to transitional rules, to losses available for set off on January 1, 2019. As a result of a judgement by the Supreme Court from June 11, 2021, a parent company may set off any pre-fiscal unity holding company losses it incurred against other types of profit realized by a newly incorporated and direct subsidiary included in the fiscal unity. According to the Deputy Minister of Finance, the consequences of this judgment are contrary to the spirit and intent of the holding company loss scheme and result in a significant loss of tax revenue. The proposed repair measures will have the effect that these pre-fiscal unity holding and financing losses cannot be offset against profits realized by a newly incorporated and direct subsidiary that is included in the fiscal unity.

In the event the company has recognized a DTA for pre-fiscal unity losses and the repair measures will limit the loss utilization, this may result in a decrease of the deferred tax asset.

Expected ETR impact

Actions needed

Reassess reversal schedule for DTA recognition if holding company losses are available for carry-forward

1.4 Maximum annual loss set-off, however unlimited carry-forward

As part of the 2021 Tax Plan, an indefinite carry-forward loss set-off will apply as of January 1, 2022 (currently, six years carry forward). The carry-back period is and will remain one year. Although an indefinite carry-forward period will apply, losses will only be fully available for carry-forward and carry-back set-off up to an amount of EUR 1 million of taxable profit. In the case of a higher profit, the losses will be able to be offset up to EUR 1 million + 50% of the taxable profit that exceeds EUR 1 million. The proposed changes will apply to all off settable losses incurred as of January 1, 2022 and to losses that are still available for carry forward loss set-off at year end 2021.

Although changes in the loss set-off were part of the 2021 Tax Plan released in 2020, the rules were enacted as of 4 June 2021 therefore impacting the financial statements as of 2021.

Whether the unlimited carry-forward will result in a change of the deferred tax asset recognized depends amongst others on the availability of future taxable profits against which the unused tax losses can be utilized. As such, the limitation to utilize losses up to a maximum of 50% of the excess of EUR 1 million although unlimited in time might impact the recognition of the deferred tax asset.

Expected ETR impact

Actions needed

If tax losses are available for carry-forward, consider the impact on DTA measurement and cash tax payable (for cash flow forecast)

1. Corporate income tax

1.5 Taxpayer status measure for reverse hybrid entities

As of January 1, 2020, several measures took effect, which serve to combat tax avoidance by using so called 'reverse hybrids'. A reverse hybrid entity is an entity that is tax transparent in its jurisdiction of incorporation/resident, while regarded as not transparent from the perspective of the participant in that entity. A typical example is the CV in a BV/CV structure where deductible payments are made by a Dutch BV to a Dutch CV. This CV is transparent for Dutch tax purposes, but not transparent seen from the perspective of the tax legislation of the foreign investors. This generally results in a mismatch due to a deduction of expenses without taxing the corresponding income at the level of the CV.

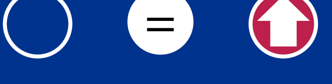
In implementing these measures, the Netherlands made use of the option to have the tax status measure for reverse hybrid entities only take effect as of January 1, 2022. The government has now followed up on this by means of a separate bill, under which a reverse hybrid entity will become fully liable to corporate income tax as a Dutch resident taxpayer. It is possible that (part of) the profits of the reverse hybrid accrue directly at the level of the participants in a state that regards that body as transparent. Under certain conditions, those profits will not be taxed at the level of the reverse hybrid in the Netherlands and creating a deduction for that amount.

The measures may have an increasing impact on the ETR compared to the situation before as now profits of the reverse hybrid entity will become subject to taxation in the Netherlands. At the same time, the impact of any deferred taxes should be considered as the company will become a Dutch tax resident resulting in an opening balance for tax purposes potentially leading to temporary differences.

In addition, the reverse hybrid entity may also result in a withholding tax obligation on dividend distributions made to and by a reverse hybrid entity. Under IFRS, this may require the recognition and measurement of a DTL on so called outside basis differences having an increasing impact on the ETR.

Finally, the reverse hybrid entity may also have a withholding tax obligation on interest and royalties provided that the interest and royalties are paid to an entity in a so called low-tax jurisdiction. If the company classifies the withholding tax as an income tax, the ETR is negatively impacted if withholding tax is due (upon payment or accrual by year end), whereas no full credit is obtained elsewhere. Withholding taxes generally have to be recognized at the level of the entity receiving the interest or royalty.

Expected ETR impact



Actions needed

Check structure for hybrid entities and assess potential impact in 2021 and 2022

1.6 Combating mismatches in non-arm's length transfer pricing *(not part of the 2022 Tax Plan)*

In the current situation, when a Dutch entity pays too little or nothing to an affiliate for goods or services procured from a foreign related party, then the Dutch entity may adjust the agreed remuneration for Dutch tax purposes to an arm's length basis. Under Dutch tax law a distinguish is made between adjusting the agreed remuneration as profit (loss) or step up in value together with a deemed dividend or an informal capital.

1. Corporate income tax

Deemed dividend

The Dutch entity can deduct additional expenses for the difference between the agreed remuneration and the arm's length price. These so-called downward adjustments recognized in the Netherlands could create a mismatch especially when there is no upward adjustment at the level of the foreign related party.

Measures are proposed combatting these mismatches and will apply for the first time to financial years commencing on or after January 1, 2022. The bill means that for deemed dividend situations downward adjustments of the Dutch taxable profit on the basis of the arm's length principle in transactions between associated entities will, in principle, no longer be taken into account. However, the downward adjustment may be taken into account insofar as the taxpayer can convincingly demonstrate that a corresponding upward adjustment is subject to profit tax at the other related entity.

Informal capital

The Dutch entity can adjust the tax base of the procured assets to an arm's length basis when the purchase price was not considered arm's length. These so called step up adjustments of the assets procured or obtained via contribution could create a mismatch especially when the assets can be depreciated/amortized considering the higher step up value (tax base), while this did not result in a corresponding taxation of the capital gain at the level of the foreign affiliate.

To tackle this, a measure is introduced for these informal capital structures as of January 1, 2022. In short, the measure will have the effect that the Netherlands will not grant a step-up to the higher transfer price if the taxpayer (in this case the buyer) cannot demonstrate that the corresponding capital gain was not subject to income tax at the level of the transferor.

For assets acquired from an associated entity in the fiscal years beginning on or after July 1, 2019, any future depreciation/amortization may be limited (as of financial years commencing on or after January 1, 2022).Not falling under the proposal is the situation that an asset is purchased for the correct arm's length price, but is not taxed at the vendor.

The denial of downward adjustments from 2022 onwards will have an increasing impact on the ETR compared to existing situations. Restrictions to informal capital structures may affect the deferred taxes as from 2022 temporary differences may arise. Also the limitation of depreciation/amortization of assets may result in increased taxable profit levels in 2022 and onwards, thereby potentially impacting DTA's.

Please note that for assets that have been procured or obtained via contribution in the period on or after July 1, 2019, there is no impact on the DTA for temporary differences, even though depreciation/amortization is no longer possible as from January 1, 2022. The reason is that the tax base of these assets is not impacted by this rule. This will be different for assets that will be procured or obtained via contribution as from January 1, 2022.

Expected ETR impact

Actions needed

Assess whether any adjustments to the Dutch tax base are made based on the at arm's length principle for which no corresponding adjustment is taken into account

1.7 Exemptions normal TVL and TVL for SME startups (2021)

It has been proposed to exempt the Overhead Compensation SMEs (Tegemoetkoming Vaste Lasten mkb; TVL SME), the Overhead Compensation (Tegemoetkoming Vaste Lasten; TVL) and the Overhead Compensation start-up SMEs (Tegemoetkoming Vaste Lasten voor startende mkb-bedrijven; TVL start-up SMEs) from tax. This is an extension of the exemption already included in the 2021 Tax Plan for the Compensation for Entrepreneurs in Affected Sectors COVID-19 (Tegemoetkoming Ondernemers Getroffen Sectoren COVID-19; TOGS) and the TVL SME for the period through to September 2020. The downside to this exemption is that any repayments of the above compensation are not deductible.

The exemption of income lowers the ETR, while any repayment of compensations has an increasing impact on the ETR due to its non-deductibility.

Expected ETR impact

Actions needed

Assess whether exempt compensations were applied for

2. Withholding taxes

2.1 Limiting the crediting of dividend tax and tax on games of chance (Sofina judgment)

Dutch corporate tax residents can fully offset Dutch withholding taxes with their corporate tax liability. This is also possible in a year that no corporate tax is due effectively resulting in an immediate refund of Dutch withholding taxes. A company established abroad does not have this option. That seems to be contrary to EU law.

In order to remove any potential conflict with EU law, the government will limit the crediting of dividend withholding tax (incl. tax on games of chance) against corporate income tax as of January 1, 2022. The crediting of these advance taxes will be limited to the corporate income tax payable in one year. The uncredited advance taxes will be carried forward to a later year by means of a decision open to objection.

The uncredited advance taxes can be carried forward indefinitely to future years. For such 'tax credits', in principle a DTA can be recognized to the extent that it is 'probable' that sufficient taxable profits and current tax liability will be available against which the tax credits can be offset.

Whether this measure will affect the ETR depends on whether sufficient future taxable profits with a corresponding current tax liability will be available against which the credits can be offset.

Expected ETR impact =

Actions needed

Assess if a credit is applied for dividend tax or tax on games of chance

2.2 Withholding tax on interest and royalties – expansion PE concept

As of 1 January 2021, a withholding tax on interest and/or royalties can be levied if a Dutch entity pays royalty and/or interest to a related party that is established in a 'low tax' jurisdiction or in tax abusive situations. For the purpose of the conditional withholding tax on interest and royalties, it has been proposed to expand the 'permanent establishment' concept as of 2022. As a result of that, interest and royalties payable by entities not established in the Netherlands will be subject to the conditional withholding tax if these are attributable to a permanent establishment located in the Netherlands. For the meaning of the permanent establishment concept, reference is now made to Section 3 CITA 1969. It has been proposed that a permanent establishment should also include the sources referred to in Section 17a CITA 1969. Consequently, withholding tax will also be imposed on interest and royalties attributable to, among other things, immovable property located in the Netherlands.

If the company classifies the withholding tax as an income tax, the ETR is negatively impacted if withholding tax is due (upon payment or accrual by year end), whereas no full credit is obtained elsewhere. Withholding taxes generally have to be recognized at the level of the entity receiving the interest or royalty.

Expected ETR impact

Actions needed

Perform WHT risk assessment + assess whether withholding taxes are considered income taxes (IAS 12)

2. Withholding taxes

2.3 Expansion of withholding tax on dividends to low tax countries *(2024, enacted during 2021)*

Since the government wants to put an end to the Netherlands being used as a gateway to low-tax jurisdictions, a withholding tax on interest and royalties was introduced as of January 1, 2021. As of 2024, this tax will be supplemented with a conditional withholding tax on dividends. The measure will apply to cash flows from countries with a profit tax rate of less than 9% and to countries appearing on the EU blacklist, even if the Netherlands has a tax treaty with these countries. The withholding tax on dividends will be levied in addition to the existing dividend tax. If the conditional withholding tax on dividends cumulates with the dividend tax, the conditional withholding tax will be reduced by the imposed dividend tax.

The ETR is negatively impacted by the withholding tax if no full credit is obtained elsewhere. Withholding taxes generally have to be recognized at the level of the entity receiving the dividend. The rules were enacted as of 2 November 2021 therefore impacting the financial statements as of 2021.

Expected ETR impact

Actions needed

Perform WHT risk assessment

2.4 Private Member's bill on conditional final settlement of dividend withholding tax

On July 10, 2020 Lower House MP Bart Snels (Greens parliamentary party) presented a private member's bill to the Lower House of Parliament in which he proposes introducing a final settlement obligation for dividend withholding tax purposes. This withholding tax obligation applies to certain types of cross-border relocations of registered office, cross-border mergers, cross-border divisions, and cross-border share mergers. In short, it proposes a dividend withholding tax on retained earnings of a Dutch company in case this company is moving towards another jurisdiction that can be considered a 'qualifying state'. These are states that do not have a withholding tax on dividends comparable to the Netherlands. In these situations, the Dutch company is considered to have paid a dividend to its shareholders. In the event the shareholder is an entity that is part of the group (i.e. consolidated financials), this may have an impact on the withholding tax consequences to be recognized for the taxable reserves.

By amendment of September 18, 2020 the private member's bill is no longer limited to groups with a consolidated group revenue of at least EUR 750 million and the retroactive effect has been changed into September 18, 2020 12:00 CET. By second amendment on October 9, 2020 a completely new text and Explanatory Memorandum were submitted to the Lower House of Parliament. Based on this amendment, the dividend withholding tax will only be payable insofar as the withholding agent's distributable profit is more than EUR 50 million at the time the taxable event occurs. By a third amendment on October 26, 2021 the retroactive affect was removed from the bill. We refer to our memorandum for a more detailed explanation.

The bill is not part of the parliamentary process regarding the 2022 Tax Plan and hence not expected to be enacted prior to year end 2021.

3. Other tax developments

3.1 Denunciation of the Russia-Netherlands Double Tax Treaty

On June 7, 2021, the Russian government officially gave notice of the termination of the double tax treaty to the Dutch government. The notice of termination was the final step in the legislative process to denounce the double tax treaty, meaning that as of January 1, 2022 there will no longer be a double tax treaty between the Netherlands and Russia.

One of the adverse consequences of the denunciation of the double tax treaty is the fact that the full exemption from dividend withholding tax provided under Dutch national law will cease to apply, resulting in a 15% levy on dividend payments made by Dutch taxpayers to Russian shareholders. At the same time, any dividends paid by Russian taxpayers to Dutch shareholders may result in an increased dividend withholding tax. These changes could impact the recognition of deferred tax liabilities on outside basis differences.

Withholding taxes generally have to be recognized at the level of the entity receiving the dividend impacting their ETR.

Expected ETR impact

Actions needed

Perform WHT risk assessment

3.2 MLI and dispute resolution

The Multilateral Instrument (MLI) makes it possible for countries to adjust their tax treaties quickly and efficiently. The MLI entered into force for the Netherlands on July 1, 2019 and provides measures to counter treaty abuse and to improve dispute resolution mechanisms. For which tax treaties and from which moment the MLI can be applied by the Netherlands varies per jurisdiction. Although many MLI's already entered into force before 2021, also in 2021 and 2022 new MLI's between the Netherlands and foreign tax jurisdictions enter into force.

The MLI provides for a mutual agreement procedure which is intended to ensure an effective and timely resolution of treaty-related disputes via a corresponding adjustment. The corresponding adjustment requires jurisdictions to make an adjustment to the profits of a taxpayer in its jurisdiction if the other contracting jurisdiction makes an at arm's length pricing adjustment to the profits of a taxpayer in that other contracting jurisdiction. Any increase or decrease in that other jurisdiction would be mirrored by a corresponding adjustment to the profits of the taxpayer in the first jurisdiction.

As an option, the MLI provides for a mandatory binding arbitration in their tax treaties. This mechanism would solve situations where no mutual agreement can be reached between tax jurisdictions.

In the area of transfer pricing these developments have a positive impact. When both treaty countries signed the MLI and selected the mandatory binding arbitration provision it reduces the risk of double taxation, and therefore may impact the recognition and measurement of uncertain income tax positions (IFRIC 23)

Note that within the European Union the Directive 2017/1852 applies (Dispute Resolution mechanism) providing for similar measure to solve tax disputes. Next to this Directive, other initiatives reduces the risk of double taxation (e.g. ICAP and the EU Cooperative compliance program).

3. Other tax developments

3.3 Progress of new group corporate income tax scheme

As the current fiscal unity regime is vulnerable under EU law, work is in progress on a new group corporate income tax scheme. As part of the Fiscal Unity Emergency Repair Act, some elements have already been amended as of January 1, 2018. However, with regard to other elements, the risks under European law have not (or may not have) entirely disappeared. On Budget Day in 2020, the Deputy Minister of Finance, Mr. Vijlbrief, sent a letter to the Lower House of Parliament in which he had outlined, among other things, the main features of a potential new group scheme and the follow-up process. The decision to present a bill to the Lower House of Parliament has been left to a following government.

The impact of the new group corporate income tax scheme on the ETR will depend on the features of the new scheme and hence cannot be predicted yet.

3.4 OECD Pillar 1 and Pillar 2: taxation of the digital economy

On October 8, 2021, the OECD announced that 136 countries and jurisdictions – of the 140 members of the OECD/G20 Inclusive Framework on base erosion and profit shifting – have agreed that certain multinational enterprises will be subject to a minimum 15% tax rate, effective from 2023. The two-pillar solution means that taxing rights are expected to be reallocated to market jurisdictions with respect to multinationals with global sales above EUR 20 billion and a profitability above 10% (Pillar One) and a global minimum tax rate will be determined at 15% which will apply to companies with revenue above EUR 750 million (Pillar Two). The OECD reported that countries are aiming at signing a multilateral convention in 2022, with effective implementation in 2023.

The impact of the Pillar One and Pillar Two will depend on the exact features of the multilateral convention and hence cannot be predicted yet.

3.5 IAS 12 – IRE/IFRS 16

In May 2021, the International Accounting Standards Board (IASB) published ‘Deferred Tax related to Assets and Liabilities arising from a Single transaction (Amendments to IAS 12)’ that clarify how companies are required to account for deferred tax on transactions such as leases and decommissioning obligations.

The main change is that the initial recognition exemption does not apply to transactions in which equal amounts of deductible and taxable temporary differences arise on initial recognition. Since the Dutch Secretary of State announced in a letter to the parliament (April 4, 2019) that in the Netherlands IFRS 16 will not be followed for corporate tax purposes (i.e. IFRS 16 is not in line with ‘sound business practice’), temporary differences will arise. With the clarification from the IASB, companies are required to recognize deferred taxes on those temporary differences that originate from operating leases. The amendments are effective for annual reporting periods beginning on or after January 1, 2023 but early adoption is permitted.

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