KPMG Meijburg & Co Tax & Legal

Changes to proposal for a new Box 3 regime as of 2027

The caretaker government has made changes to five aspects of the draft bill relating to the taxing of the actual return on investment in Box 3. The changes were introduced in response to last year's internet consultation (see our memorandum of September 11, 2023). According to the caretaker government, the draft bill should be seen as a building block and tool for a new government. It is up to a new government to take a final decision on this. In this memorandum we first address the changes to the draft bill. This is followed by an overview of the main features of the proposed new Box 3 regime, including the changes.

Main features of the changes

In response to an internet consultation held last year, technical improvements have been made to the proposal for the new Box 3 regime. The changes mean that:

- the flat rate for the first home in Box 3 will be canceled. All homes falling in Box 3 will thus be taxed in accordance with capital gains tax.
- The option to set off a Box 3 loss against Box 3 profits from older years will end (no carried-back loss set off).
- When the new Box 3 regime comes into effect, any property and shares in a family business or an innovative start-up or scale-up already owned by a taxpayer will be valued at the WOZ value or the fair market value respectively.
- The price paid for a right of enjoyment will be deducted in installments (rather than in one go) in the years in which there is a right of enjoyment.
- The foreign exchange gains or losses on bank balances in foreign currencies will be taken into account when determining the return on investment.

In the following sections, we address the main features of the new, revised Box 3 regime as proposed by the caretaker government (thus including the above changes). In order to keep to the effective date of January 1, 2027, the bill must be presented to the Lower House of Parliament in the summer of 2024 and the Lower House must adopt it before March 15, 2025.

Main features of the new Box 3 regime

The general rule of the new regime is that assets falling in Box 3 will be taxed on the basis of the actual return realized by the taxpayer. This actual return consists of the direct and indirect return on investment less any related costs.

Direct and indirect return on investment

The direct return can include the rent, interest and dividends received in a year, less the related costs, such as the interest paid on a loan falling in Box 3. For tenanted property financed with a loan, the direct return consists, for example, of the rent less the interest paid. In line with the rules in Box 1, certain types of costs will be excluded from deduction in Box 3.

When renting out property or lending money in affiliated relationships – transactions between parents and children, for example – a non-business motivated price can be adjusted to the fair market value. However, no adjustment will be made if the deviation remains within a range still to be determined (the 'efficiency margin').

The indirect return concerns the movement in value of the Box 3 assets. As general rule, this concerns both realized movements in value (sales proceeds, for example) and the *unrealized* movements in value in a year (including foreign exchange results on bank balances in foreign currencies). The *unrealized* movements in value in a year corresponds to the fair market value of the Box 3 assets at the end of the calendar year less the value of the assets at the beginning of the calendar year. The outcome of this equity reconciliation will be adjusted by the value of the Box 3 additions and withdrawals. This valuation methodology is derived from the profit regime of Box 1, more specifically from the principle of sound business practice to which the draft bill explicitly refers.

The new Box 3 regime will include an exemption for taxpayer debts that are waived, similar to the exemption for debt relief income tax included in Box 1. For the provider of a loan that falls in Box 3, a business-motivated write-down loss will be deductible.

Loss set-off
The actual return on investment may be negative. Therefore, an option to set off a Box 3 loss against positive Box 3 returns in future years (carried-forward loss set-off) has been provided for. There is no time limit on the carried-forward loss set-off. Carried-back loss set-off, i.e. setting off a loss against profit from an older year, is not possible. A Box 3 loss cannot affect (old, current or future) Box 1 or Box 2 income. The caretaker government also notes that for reasons of efficiency it would be desirable to introduce a loss set-off threshold.

Death and emigration of the taxpayer
Upon the death of the taxpayer, they will be deemed to have disposed of their Box 3 assets at fair market value on the date on death. The total benefit thus determined will then be attributed to the relevant calendar year.

If the taxpayer emigrates, they will be deemed to have disposed of their Box 3 assets at fair market value on the date of emigration. With regard to the taxation of property and shares in family businesses and unlisted innovative start-ups and scale-ups (see also below under ‘Settling the tax bill upon emigration/protective assessment), a protective assessment will be imposed for the tax payable (a protective assessment means that the tax does not have to be paid straightaway). The conditions under which deferral of payment for the protective assessment is granted have yet to be worked out.

Changes as a result of the new regime
The current tax-free amount will be replaced by tax-free income, the amount of which still has to be determined. The green investment scheme will be transformed into a tax credit for green investments. The rules for non-resident taxpayers and double tax relief will also be changed.

What essentially remains the same?
Current exemptions for assets in own use (for example, cars) and for art and antiques will remain in place, provided they are not held for investment. Forests, nature reserves and country estates referred to in the Nature Conservation Act 1928 *(Natuurschoonwet 1928)* (with the exception of built properties) will also remain exempt.

Retirement provisions/term life insurance policies
Under the new regime, net pensions and net annuities will remain exempt under certain conditions. With regard to term life insurance policies, a full exemption has been provided for.

Exceptions and nuances to the general rules
There are several exceptions and nuances to the aforementioned general rules for the new Box 3 regime. These exceptions relate in particular to the obligation to make an annual revaluation to fair market value of those assets.

Capital gains tax on immovable property and certain shares
The indirect return on investment on immovable property and shares in family businesses or unlisted innovative start-ups and scale-ups will only be taxed when they are sold or upon the death or emigration of the taxpayer, i.e. a capital gains tax. In practice, this means that these assets do not have to be revalued annually. On the other hand, direct returns on investment (rent and dividends for example) will be taxed each year.

Immovable property
Immovable property that is not already taxed in Box 1 will be taxed in Box 3. As stated above, the indirect return on this immovable property will be taxed in accordance with capital gains tax. This means that tax will only be levied when the immovable property is sold or upon the death or emigration of the taxpayer. In short, capital gains tax will be determined by reducing the selling price by the acquisition price. To ensure the capital gain arising under the new Box 3 regime is properly determined, the acquisition price of immovable property owned by the taxpayer at the time the new Box 3 regime takes effect will be set at the WOZ value.

Shares in family businesses and unlisted innovative start-ups and scale-ups
Shares in family businesses and unlisted innovative start-ups and scale-ups belonging in Box 3 will also be taxed in accordance with the methodology of a capital gains tax (which means that there is no annual revaluation and tax is only levied when the shares are sold, or upon the emigration or death of the taxpayer). The term ‘family business’ still has to be further defined. However, it has been indicated that a family business is considered to exist if one family holds majority control and/or is formally involved in both the management of the company and the company itself. Furthermore, it is proposed to define family in this respect as the taxpayer, their partner, and blood relatives or relatives by marriage in the direct line or through to the fourth degree of kinship (this goes all the way back to second cousins, great aunts, etc.). Based on the wording of the bill and the explanatory notes, it appears that this exception only applies

to persons who also belong to the family and not to shareholders from outside the family (for example, the management).

With regard to shares in unlisted innovative start-ups and scale-ups, it is unclear what the defining criterion will be. The specific structure of the scheme for the envisioned target group is still being looked into.

The capital gain realized on shares in family businesses and unlisted innovative start-ups and scale-ups will, in short, be determined by reducing the selling price by the acquisition price. To ensure the gain arising under the new Box 3 regime is properly determined, the acquisition price of shares in these companies that are owned by the taxpayer at the date on which the new Box 3 regime takes effect, will be set at the fair market value. On the other hand, direct returns on shares – dividends for example – will be taxed in the year they are received.

Exemption transition (taxation)
If shares lose their qualification as family business or innovative start-up, then the difference between the fair market value and the acquisition price must be taken into account at the moment that qualification is lost.

Settling the tax bill in the case of emigration/protective assessment
With regard to immovable property located outside the Netherlands as well as shares in family businesses and innovative start-ups, tax will be paid on the fair market value less the acquisition price if the owner or the shareholder emigrates abroad. A protective assessment will be imposed with regard to this tax. The documents are not entirely clear about how emigration with affect immovable property located in the Netherlands. In principle, the Netherlands retains the right to tax in this regard, which would support delaying the settlement of the tax bill until the year the immovable property is actually sold.

Loans between natural persons
The fair market value of receivables and payables under a loan agreement between natural persons may be set at the nominal value.

Rights of enjoyment
The taxable return also includes what is received as a consideration for the establishment of a right of enjoyment (for example, a right of usufruct) on an asset belonging in Box 3. The price for purchasing a right of enjoyment is not deductible as a lump sum, but is deducted in installments in the years in which there is a right of enjoyment. Assets on which the right of enjoyment is established must be valued without taking the value of the right of enjoyment into account. A right of enjoyment is defined as any entitlement to benefits from goods.

Main features of the most common assets

The following table is derived from the letter on the draft bill that was sent to the Lower House of Parliament:

Category	Taxed direct return	Taxed indirect return
Bank and savings balances	Actual income (interest less costs)	Foreign exchange results on bank balances in foreign currencies
Shares, bonds, profit-sharing certificates, options	Actual income (dividend/interest less costs)	Movement in value in the form of foreign exchange gains or losses less costs (capital growth)
Shares (start-ups, family businesses)	Actual income (dividend/interest less costs)	Movement in value upon realization (capital gain)
Immovable property (general rule)	Actual income (rent/lease less costs)	Movement in value upon realization (capital gain)
Receivables and payables	Actual income (interest less costs). Interest paid on loans is negative income.	Write-down (at the creditor) or released profit (at the debtor) upon remission of the receivable (capital growth)

KPMG Meijburg & Co comments

The further refined draft bill is an attempt by the caretaker government to introduce a tax on the actual return in Box 3 as quickly as current circumstances allow. However, it is, in principle, up to a new government/new coalition to make use of this initiative. It cannot be ruled out that, if it takes a long time to form a new government/coalition or as a result of Supreme Court case law, the caretaker government may have to elaborate on the current draft and present the bill to the Lower House of Parliament, either because it has been asked by the Lower House to do so or because the caretaker government itself feels forced to do so. This is because it is only possible to have the new Box 3 regime take effect as of January 1, 2027 if the bill is presented to the Lower House of Parliament in the summer of 2024.

We will of course keep you informed about the progress of this bill and developments around Box 3. For an analysis of how the draft bill will affect your current situation, please contact your advisor at KPMG Meijburg & Co.

KPMG Meijburg & Co
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