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Bill against excessive borrowing from own company presented to the Lower House

On June 17, 2020, the Deputy Minister of Finance presented the bill on the Excessive Borrowing from Own Companies Act to the Lower House of Parliament. The measure was already announced in September 2018 on Budget Day, after which a draft of the bill was released for consultation in March 2019. In the case of substantial interest holders who borrow more than EUR 500,000 from their company, it is proposed to tax the excess as income derived from a substantial interest. Home acquisition debt is excluded. The measure will apply for the first time for the calendar year 2023, one year later than originally planned. Each substantial interest holder who borrows more than EUR 500,000 will have to review their position before then.

What does the bill entail?

The government intends to use the measure to combat the deferral of tax for personal income tax purposes in Box 2 and to bring taxation more in line with the time at which the substantial interest holder, or any person related to them, actually has the funds at their disposal. The taxation of the substantial interest will be brought forward. If more than EUR 500,000 is borrowed from the own company, the excess will be taxed as a deemed ordinary benefit at the end of the calendar year ('the excessive part of the debt') in Box 2 in the hands of the substantial interest holder and their partner. Debt is defined as all civil-law indebtedness and commitments at the end of the calendar year on the basis of nominal value. The maximum amount of EUR 500,000 applies in this respect to the substantial interest holder and their partner. Loans from multiple companies in which a substantial interest is directly or indirectly held are added together.

The scope of the measure will be limited to the substantial interest rules. This means that the measure will not affect Box 1 and Box 3 as regards personal income tax, dividend withholding tax and corporate income tax. This is intended to keep enforcement costs as low as possible, but it is doubtful whether the desired effect will also be achieved. The measure has no civil law significance. The loan will generate deemed income in Box 2, but will continue to exist for civil-law purposes, so interest still has to be taken into account and the repayment of the debt is required at some point. For the company (the creditor) this means that the value of the receivable from the shareholder (the debtor) as it appears on the balance sheet for tax purposes will not change as a result of this measure and that the creditor will also regularly take into consideration the interest on the substantial interest holder's excessive part of the loan and must account for this in its income statement. If the debt falls in Box 3, it will reduce the capital yield tax base for income from savings and investment.

The Explanatory Memorandum underlines that current case law on loans and home acquisition debt will continue to apply in full. In short, this means that if it is established that the debt cannot or will not be repaid, a deemed dividend distribution will be assumed and the tax on the substantial interest will have to be paid. This applies to both debt in excess of and below EUR 500,000. It is not the intention for double taxation to arise: if there is a deemed dividend distribution that can also be regarded as excessive debt, tax will only be levied once.

No longer economic double taxation

The economic double taxation that could have arisen under the original proposal (in addition to the deemed dividend distribution as described above) will be avoided as far as possible by means of a change in methodology. The intention is to only bring forward the taxation, not to introduce an additional tax. The maximum amount of debt in principle amounts to EUR 500,000. If this is exceeded at the end of the year, the excess is taxed as a deemed ordinary benefit and the maximum amount is increased by the same amount. Due to a full or partial repayment of the debt in a later year, the total debt at the end of the year will be lower than the increased maximum amount. A negative deemed ordinary benefit in the year of repayment can consequently be taken into account. If, as a result, a loss from the substantial interest arises, this can be set off in accordance with the rules for setting off a loss from a substantial interest. The maximum amount will subsequently be reduced by the same amount. If the entire substantial interest is disposed of, a negative deemed ordinary benefit can also be taken into account. In situations where there is no longer a substantial interest at the end of the year, the debt is deemed to have been repaid in full. However, the total negative deemed ordinary benefit may never exceed the total positive deemed ordinary benefit that was previously taken into account.

In the original proposal, transitional rules only provided for the set-off of a deemed ordinary benefit in the first year (2022 according to the original proposal), in the form of a 'disposal credit' on the subsequent disposal of the entire substantial interest. For deemed ordinary benefits in subsequent years there were no rules for the avoidance of double taxation.

Which loans qualify?

All debt qualifies with the exception of home acquisition debt. Debt does not fall under the proposed measure insofar as a mortgage right is established thereon. The latter mortgage condition does not apply to home acquisition debt existing on December 31, 2022.

It is irrelevant whether the debt was entered into for consumer expenditure (i.e. 'current account overdrafts') or that it was, for example, entered into to finance the acquisition of (property) investments. Receivables and rights to the company will not be set off against the debt to the company to arrive at a net figure. All types of loans count toward determining the total amount of debt. Accrued interest and guarantees given by the company are not excluded, nor is the onlending of funds to the substantial interest holder that were borrowed from the company by other people. When a person related to the substantial interest holder, who does not hold a substantial interest themselves, borrows excessively from the company, the excessive amount is taxed at the substantial interest holder (and their partner) insofar as this excessive amount is not higher than the substantial interest holder's threshold. An example of this is children who borrow from their parent's company.

Transitional rules

Limited transitional rules have been proposed. As stated above, only home acquisition debt in place on December 31, 2022 will also be disregarded if no mortgage right has been established.

Existing agreements

As a rule, existing agreements with the Dutch tax authorities are canceled as a result of legislative amendments. However, settlement agreements covering total debt of less than EUR 500,000 will not be canceled. According to the Explanatory Memorandum, this is not clear in advance with regard to settlement agreements covering total debt in excess of EUR 500,000 and depends on the agreements made.

Immigration, emigration and remigration

Protective assessments for the profit from a substantial interest will be imposed on substantial interest holders who emigrate. A deferral of payment for this will, in principle, be granted in the usual manner. If the emigrated shareholder subsequently receives an ordinary or disposal benefit, the deferral of payment can be withdrawn in this respect. Insofar as debt to the own company increases to more than the maximum amount after the emigration of the substantial interest holder, a deemed ordinary benefit will be presumed. This will result in the tax on the protective assessment being collected in this respect. Whether the deemed ordinary benefit can still be taxed depends on the applicable tax treaties.

A step-up will be granted in the event of immigration resulting in domestic taxpayer status: the maximum amount will be set at the amount of qualifying debt at the time of immigration, but will be at least EUR 500,000. This will avoid debt that arose in the period outside the Netherlands falling under the measure. If a person who was a foreign taxpayer immigrates and thus becomes a domestic taxpayer, no step-up will in principle be granted. Nor will a step-up be granted in the case of remigration. The maximum amount applying to the taxpayer upon emigration will again count as the maximum upon remigration.

Further rules may be drawn up to determine the maximum amount of debt upon immigration and remigration.

Meijburg & Co comments

The proposal is designed to combat excessive borrowing from companies in which a substantial interest is held. Part of the bite has been removed from the proposal in the sense that, in most cases, taxation is merely brought forward rather than economic double taxation being imposed. Nevertheless, it is certain that each substantial interest holder who, alone or together with their partner, has borrowed more than EUR 500,000 from their own company will have to review their position. Substantial interest holders who have emigrated will also have to re-examine whether the proposal will result in tax; this also applies to situations where the children, grandchildren or parents of the substantial interest holder have borrowed from the company. Where appropriate, action will have to be taken by year-end 2023 at the latest. However, it is advisable to take

stock of the consequences of the proposal at an earlier stage. It should also be noted that real estate transfer tax is not going to include any tax relief for property investments financed by the own company. Transferring this property to the company for the repayment of the debt is therefore not possible without real estate transfer tax.

If you would like more information on any of the topics discussed here, your Meijburg advisor will naturally be happy to be of assistance.

Meijburg & Co
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