Dutch Legislation Targets Deferral of Exit Taxes

by Paulus Merks and Gabriël van Gelder

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Dutch State Secretary for Finance Frans Weekers on May 15 submitted a bill on deferral of exit taxes that brings Dutch legislation in line with EU law and that, unlike a previous decree, addresses cross-border mergers and de-mergers. The bill is intended to take effect on January 1, 2013, with retroactive effect to November 29, 2011.

The bill is a result of the European Court of Justice decision in National Grid Indus (C-371/10, Nov. 29, 2011), which concerned the application of a final settlement, or exit, tax when the registered office (normally the place where the effective management is conducted) of a Dutch private limited liability company relocates to another EU jurisdiction. Before National Grid Indus, the European Commission had already started an infraction proceeding stating that the provisions regarding exit taxes in the Dutch Income Tax Act and the Dutch Corporate Income Tax act (CITA) were not EU proof (European Commission v. Netherlands, IP/10/299, IP/10/1565, and C-301/11). (For a related ECJ release, see Doc 2011-17374 or 2011 WTD 156-15.)

Exit Taxes

Exit taxes are levied when an enterprise is relocated to another jurisdiction. The ITA and CITA have provisions that provide for an immediate levy of exit tax upon the emigration of an enterprise or an individual holding shares in a Dutch LLC. In that event, tax is levied on the hidden reserves, tax reserves, and goodwill present at the time of emigration. These exit taxes could restrain businesses from exercising their right of freedom of establishment within the EU and may therefore conflict with EU law.

National Grid Indus

In National Grid Indus, the ECJ held that a member state (in this case, the Netherlands) does not have to abandon its right to tax hidden reserves (surplus value). The ECJ did say, however, that denying the option to defer payment results in disproportionality because businesses often lack sufficient cash to immediately pay the tax assessment. The ECJ said that an arrangement offering a taxpayer the choice between paying the tax immediately and deferring payment would be suitable. (For the ECJ decision in National Grid Indus, see Doc 2011-24891 or 2011 WTD 230-22; for related analysis, see Tax Notes Int’l, Jan. 2, 2012, p. 7, Doc 2011-26317, or 2011 WTD 244-2; see also Tax Notes Int’l, Jan. 30, 2012, p. 371, Doc 2012-1269, or 2012 WTD 19-18; and Tax Notes Int’l, Jan. 16, 2012, p. 201, Doc 2012-28, or 2012 WTD 10-17.)

The ECJ’s decision in this case differs somewhat from its judgments in de Lasteyrie (C-9/02) and N (C-470/04). In de Lasteyrie, an individual held a substantial interest in a French limited company and upon migration of the individual to another jurisdiction, the French tax authorities issued an exit tax on the surplus value. It was possible to defer the tax payment, but only if de Lasteyrie could provide the French tax authorities with a guarantee. According to the ECJ, such a guarantee requirement was not reasonable and hence in contradiction with the right of freedom of establishment. In a comparable Dutch case, N, the question was whether the state that had imposed an exit tax (in this case, the Netherlands) needed to lower the amount of the exit tax in the event that the value of the shareholding decreased after the relocation to another jurisdiction (a step down). (For the ECJ judgment in de Lasteyrie, see Doc 2004-21394 or 2004 WTD 215-11; for the ECJ judgment in N, see Doc 2006-18757 or 2006 WTD 174-9.)

De Lasteyrie and N were both cases in which a private individual held shares in an LLC and was migrating to another jurisdiction. National Grid Indus concerned an LLC migrating to another jurisdiction within the EU. As such, one might expect the ECJ to judge the exit tax assessment in a similar fashion; however, this was not entirely the case. The ECJ pointed out that the cases were different, as de Lasteyrie and N related to the shares in a company, while National Grid Indus involved the company’s asset. In National Grid Indus, the ECJ held that a decrease of the value of the asset should not be taken into account and that a (bank) guarantee is allowed in order to mitigate the risk of noncollection of the tax due. The ECJ disregarded the mutual assistance directive (2008/55/EC Directive of May 26, 2008, on mutual assistance for the recovery of claims relating to some levies, duties, taxes, and other measures) in its judgment in National Grid Indus.
Finance Minister Decree

On December 14, 2011, shortly after the ECJ’s judgment was rendered, the finance minister issued a decree that, in anticipation of legislation, brought the practical implementation of the exit tax in line with the ECJ’s decision. The decree states that a taxpayer can pay the tax assessment within the payment term stated on the tax assessment notice or can opt to defer payment. Security (for example, a bank guarantee) will, however, be required if the taxpayer opts to defer the tax payment. This decree was highly criticized because it addressed only the migration of a taxpayer to another EU/European Economic Area jurisdiction and not with a cross-border merger or cross-border spinoff.

Legislative Proposal

On May 15 the finance minister submitted a legislative proposal to amend the Tax Collection Act. Once this legislative proposal is enacted it will replace the decree of December 14, 2011. This bill exceeds the scope of the decree because it contains provisions regarding (cross-border) mergers and de-mergers. In the case of a legal merger, company merger, or a de-merger, a situation may arise in which an asset is transferred abroad in connection with that merger, company merger, de-merger, or division. The finance minister has confirmed that a form of exit tax may also apply in that situation. The aim of the proposal is to provide taxpayers with the opportunity to defer a tax payment until the asset (or shareholding) has been sold.

Furthermore, the proposal, as well as the December 14 decree, gives taxpayers the option to pay the tax due in 10 equal annual installments. Taxpayers that opt to pay in 10 equal annual installments (without deferral) will have to satisfy less burdensome administrative obligations. Taxpayers that opt to postpone payment and make payments in 10 equal annual installments must provide security — such as a bank guarantee or the creation of a mortgage on property in favor of the Dutch tax authorities. Also, interest will be charged on the overdue tax.

Once the bill is enacted a taxpayer will have three options:

- pay the tax due the moment it migrates to another EU/EEA jurisdiction;
- pay the tax due the moment the asset is no longer in the possession of the taxpayer; or
- pay the tax due in 10 equal installments.

Restructuring Within the EU or EEA

Under the ECJ National Grid Industries decision, the legislative proposal provides a taxpayer with the possibility of deferring an exit tax on a cross-border merger, spinoff, or migration for an indefinite period. Once enacted, the bill may provide additional opportunities for taxpayers to restructure potentially high-worth assets (for example, intellectual property rights) in a tax-efficient manner within the EU and the EEA.

Paulus Merkus and Gabriël van Gelder are with DLA Piper in Amsterdam.