

GMS Flash Alert

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Netherlands - Change in Policy on Taxation of Directors Paid by Foreign Companies

The Dutch Ministry of Finance recently published a Memorandum¹ regarding the policy on tax treaties and announced a revocation of a previously-issued decree that had provided for the application of the exemption with progression method to the taxation of director's fees from a foreign company. That decree has had the effect of exempting such director's fees from Dutch taxation.

WHY THIS MATTERS

This change in policy may result in an increase to a director's overall income tax liability.

The difference in tax liability between directors of Netherlands-based companies and foreign companies will be eliminated.

This could have an impact on the assignment costs of globally-mobile directors, and on assignment policies in respect of this area of taxation, not to mention the tax compliance obligations related to such directors.

Background

A Dutch resident taxpayer who is receiving director's fees from a foreign company is eligible for treaty relief. The right to tax director's fees is, under the tax treaties concluded by the Netherlands, allocated to the state where the company is a resident (note that exceptions may apply, and the specific tax treaty should be considered in each individual case).

In most tax treaties concluded by the Netherlands, treaty relief is granted by way of the foreign tax credit method. This means that the income tax liability in respect of the director's fees in the state where the company is located, may be offset against the Dutch income tax liability (this foreign tax credit is limited to the amount of Dutch tax due on the

director's fees). This will result in an adverse effect if the foreign tax liability is lower than the associated Dutch income tax liability, as the Netherlands will levy an additional amount of tax for the difference.

Policy with Decree in Place – Applying Progression Method

In order to avoid this adverse effect, the Dutch Ministry of Finance had published a decree stating that, subject to conditions, the exemption with progression method could be applied.² The director's fees are then exempt from Dutch taxation (and only has an effect on the graduated rates). The conditions are that the director's fees have been subject to income tax in the foreign state in the same manner as ordinary employment income. No beneficial rate may be applicable and the entire director's fee must be subject to tax in the other country.

MEIJBURG & CO. NOTE

This decree is often invoked as the application of the exemption with progression method is usually more advantageous than the foreign tax credit method.

Change in Policy

Recently, the Ministry of Finance published a Memorandum regarding the policy on tax treaties. In this Memorandum, it is announced that the aforementioned decree will be withdrawn. No date is stated, but it is expected that this will come into effect on 1 January 2021.

MEIJBURG & CO. NOTE

Consequently, if the tax treaty concluded with the country of the company that pays the director's fees provides relief by way of the foreign tax credit method, the director's overall income tax liability may increase.

The difference in the tax burden between directors of Dutch-based and foreign companies will be eliminated.

If the foreign income tax liability is lower, an additional amount of income tax will be due on the Dutch income tax return.

FOOTNOTES:

1 *Notitie Fiscaal Verdragsbeleid* Communicated in a Letter from the *Ministerie van Financiën* to *Tweede Kamer der Staten-Generaal* (reference number: 2020-0000091889).

2 *Besluit Ministerie van Financiën de dato 18 juli 2008 nr. CPP2007/664M.*

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