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# Dutch Citizen May Deduct Loss on Belgian Property, AG Says

by Eric van der Stoel

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# COUNTRY DIGEST



## Dutch Citizen May Deduct Loss on Belgian Property, AG Says

Advocate General Paolo Mengozzi of the European Court of Justice issued an opinion recently in *R.H.H. Renneberg v. Staatssecretaris van Financiën* (C-527/06) holding that a Dutch citizen who owned and lived in a house in Belgium but worked in his home country was entitled to a tax deduction in the Netherlands for negative income derived from his home in Belgium.

The case is currently pending before the ECJ based on a request by the Netherlands Supreme Court for a preliminary ruling. Under Dutch domestic law, such a deduction can be claimed only by resident taxpayers.

### Facts of the Case

A Dutch citizen (Renneberg) in 1993 bought a house in Belgium and moved his place of residence there. The acquisition of the house in Belgium was financed through a mortgage loan on which Renneberg had to pay interest.

In 1996 and 1997 — the years at issue in the case — Renneberg was employed as a public servant by a municipality in the Netherlands. During those years, his entire employment income was derived from his employment in the Netherlands.

In his 1996 and 1997 income tax returns filed in the Netherlands, Renneberg deducted from his taxable employment income the negative income derived from the house in Belgium (that is, the difference between the house's rental value and the interest paid on the loan).

The Dutch tax inspector denied Renneberg's deduction of the negative income, arguing that such a deduction is available only to Netherlands resident taxpayers. Renneberg claimed that the denial of the tax deduction violated EU law, specifically the guarantee of free movement of workers in article 39 of the EC Treaty.

### Applicable Rules

#### Dutch Domestic Law

In the Netherlands, a resident taxpayer is taxed on his worldwide income, including income from an owner-occupied dwelling, which generally consists of a deemed rental value that can be reduced by interest paid on a loan that was obtained to finance the purchase of the dwelling. If the interest paid exceeds the deemed rental value, the negative amount can be used to offset other types of taxable income.

A nonresident taxpayer[1] is subject to Dutch income tax only on some (Dutch) sources of income. Those sources include income earned through employment in the Netherlands but do not include income derived from a dwelling located outside the Netherlands. Accordingly, any negative income from such a dwelling cannot be used by a nonresident taxpayer to offset other taxable Dutch sources of income.

#### Belgium-Netherlands Tax Treaty

Under the Belgium-Netherlands tax treaty of 1970,[2] the Netherlands has the right to tax Renneberg's employment income. Income from immovable property, however, is taxable in the treaty country where the property is situated.

Another treaty provision states that the Netherlands, when imposing tax on its residents, may include in those residents' tax basis items of income or capital that may also be taxed in Belgium under the provisions of the treaty. In those cases, the Netherlands must grant double tax relief for those items of income.

Based on the treaty provisions and the Dutch unilateral rules for double tax relief,[3] a Netherlands resident can deduct negative income derived from real property

[1]It should be noted that under Dutch domestic law, Renneberg — as a Netherlands citizen and civil servant — was deemed a resident for Dutch income tax purposes. The Supreme Court decided that this fiction of deemed residency is overruled by the Belgium-Netherlands tax treaty and that Renneberg therefore should be treated as a nonresident taxpayer. That ruling appears to deviate from a 1980 Supreme Court decision under which Renneberg would be treated as a ''limited resident taxpayer.''

[2]The 1970 treaty has been terminated and replaced with a new treaty that entered into force on December 31, 2002.

[3]Article 3, paragraph 4 of the Unilateral Decree for the Avoidance of Double Taxation, 1989.

located in Belgium from other, positive income. A recapture rule applies if positive income is derived from that property in later years.

## Discussion

Citing two earlier ECJ judgments,[4] Mengozzi concluded that the Dutch rule that prevented Renneberg from deducting the negative income derived from his dwelling in Belgium is in violation of article 39 of the EC Treaty, which guarantees the free movement of workers.

Mengozzi also addressed the more specific question of whether the Dutch rule leads to indirect discrimination as prohibited by article 39 EC. For discrimination to exist, he said, residents and nonresidents in comparable situations must be treated differently. As a general rule, the situations of residents and nonresidents are not comparable, so no discrimination exists, Mengozzi said. However, he added, based on case law — specifically, *Schumacker* (C-279/93) of February 14, 1995 — discrimination can still arise if the personal and family circumstances of a taxpayer who receives most of his income and almost all of his family income in an EU member state other than his state of residence are taken into account neither in the state of residence nor in the state of employment.

Citing the ECJ's judgments in *Ritter-Coulais* (C-152/03) and *Lakebrink* (C-182/06), Mengozzi concluded that Renneberg's personal and family circumstances were not being taken into account. (For the ECJ judgments in *Ritter-Coulais* and *Lakebrink* (C-182/06), see *Doc 2006-3481* or *2006 WTD 36-6* and *Doc 2007-16769* or *2007 WTD 139-16*, respectively.)

*Ritter-Coulais* and *Lakebrink* have substantial similarities to *Renneberg*. However, as Mengozzi pointed out, there are also some differences. One difference is that *Ritter-Coulais* and *Lakebrink* deal with the determination of the applicable tax rate, while in *Renneberg*, the determination of the tax base is at stake.

Another difference is that the Dutch rule denying Renneberg a deduction for the negative income derived from his dwelling in Belgium appears to result not only from Dutch domestic law, but also from the way the Netherlands and Belgium have allocated their rights to tax in the Belgium-Netherlands income tax treaty.

Although the treaty allocates the right to tax the real estate income to Belgium (the state where the property is located), for Dutch resident taxpayers the Netherlands still includes the Belgian real estate income in the resident's tax base (before applying double tax relief, whereby negative foreign income could lead to a deduction, as explained previously). Therefore, the treaty is not the reason for denying the deduction to Renneberg. Rather, it is that he is not a resident of the Netherlands. Moreover, if the Netherlands would apply the same treatment to a resident of Belgium, it would not harm Belgium's tax position. It is this aspect of the Dutch rule that is discriminatory, Mengozzi said.

The ECJ now will take the case into consideration, and the Netherlands Supreme Court will render its final decision based on the ECJ's position. ◆

♦ *Eric van der Stoel, Otterspeer, Haasnoot & Partners, Rotterdam*

[4] *Hartmann* (C-212/05) of July 17, 2007, and *Hendrix* (C-287/05) of Sept. 11, 2007.