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Introduction of subject

The state has been regulating the transfer of a testator’s property since time immemorial. Unsurprisingly so, as contradictory interests arise when an inheritance devolves. Apart from the testator’s freedom to bequeath by will, in most legal systems inheritance law represents other interests too. Testators may thus be tempted to avoid the binding rules of inheritance law. As such avoidance behaviour needed to be countered, Roman law had already introduced the legal concept of the “gift mortis causa”, under which certain benefits for future heirs were equated with an inheritance.

Regulation of inheritance law has traditionally been linked to taxation at death. In the Netherlands the levy of inheritance tax is included in the Inheritance and Gift Tax Act 1956. Inheritance tax is levied on the value of all that is acquired under inheritance law upon someone’s death. Still, just like the mandatory rules of inheritance law may motivate people to transfer property without interference of inheritance law, the aversion to paying taxes may lead to similar avoidance schemes. Already in the 19th century fictitious acquisitions by way of inheritance have been written into law to counter the avoidance of inheritance tax. This regards situations where acquisitions do not fall under inheritance law but the legislature nevertheless considers taxation to be desirable because of the resemblance with an inheritance. This encompasses certain acquisitions under matrimonial property law, gifts related to death and benefits from a life insurance. This thesis examines the taxable event of the inheritance tax.

Problem formulation

The legislation referred to before has made the taxable event in Dutch inheritance tax an extremely complex issue. No matter how much criticism this complexity draws, it would appear to be difficult to avoid within the existing legal methodology. Criticism on the desirability of certain fictitious acquisitions and the system of fictitious acquisitions in general is expressed in literature, too. The argument made here is that the rationale of some fictitious acquisitions does not, or no longer, suit the current legislation and that the legislative system can be improved.

What’s more, the legislative text and literature show the taxable event to be strongly civil law oriented. Distinctions under civil law are important to taxation. By law, the levy is conditional to there being an acquisition “under inheritance law”, so the civil law qualification of the acquisition is basically decisive for its taxability. This approach (hereafter: ‘juridical approach’) is likewise considered
to be important for the additions to this assumption: the fictitious acquisitions by way of inheritance. As a result, in certain situations unequal treatment occurs in economically identical cases. Given the economic approach of most taxes, the question is whether this matches the intentions of the legislature.

On the back of these points of criticism, the following research question has been formulated:

Considering the intention of the legislature on which positive law is based, should the taxable event for inheritance tax purposes be amended? If so, looking at this intention and the principles of proper legislation, how would such amendment have to be formulated?

As this research focuses on the legislature’s intention on which positive law is based, the justification of inheritance tax itself has not been researched. Similarly, it has not been discussed whether a tax at death should be designed as an inheritance tax or as an estate tax. On the contrary, the starting point has been the principles of the current inheritance tax. The principles of proper legislation as referred to before in the research question are based on the quality requirements imposed by the Dutch legislature.

Part I: towards an economically taxable event

In answering the first part of the research question it should be determined whether the taxable event corresponds to the intention of the legislature that underpins positive law. More specifically, the research focused on whether the strong orientation on civil law and the resulting unequal treatment of economically identical cases corresponds to the intention of the legislature. An analysis of the legal history reveals the following picture:

- As from the end of the 16th century various provinces in the Republic of the Seven United Netherlands levied an inheritance tax. The taxable event of those levies had been wide in scope. Apart from inheritances, acquisitions that were similar in economic terms, such as gifts on account of death, were taxed as well. Several special regulations derogated from the reality under civil law, too, so the economic result could be taxed or the levy could be allocated to the recipient of the benefit.
- In 1805, the economic approach was continued in the Batavian Commonwealth. The legal title was irrelevant for whether inheritance tax should be levied or not. Still, this changed in 1812, when the French empire annexed the Kingdom of Holland and introduced the French registration duty upon death, which follows a juridical approach. Although the Netherlands had already regained its tax autonomy by the end of 1813, the merger with the Southern Netherlands led to the implementation of an inheritance tax in 1817, with a more limited, taxable event based on a juridical approach.
- In 1859, the juridical approach was confirmed by the legislature. The levy of inheritance tax solely applied to acquisitions under inheritance law. Because this offered possibilities to avoid the levy, the first fictitious acquisitions by way of inheritance were written into law in 1869 and 1897. Although this already showed the glimpse of a change, the economic path was ultimately followed with the introduction of the levy on benefits from a life
insurance and the introduction of the gift tax in 1917. The legislature thus clearly showed it wanted to tax the enrichment with the acquiring party.

The support by the legislature for an economic approach can be inferred from this development, with no value being attached to distinctions under civil law. This approach likewise matches the grounds put forward by the legislature to justify the inheritance tax. The current law, at the same time, has been found to make juridical distinctions, revealing a discrepancy between the intention of the legislature and the design of the taxable event. The historical development shows this is caused by the limited juridical starting point of the taxable event introduced in the 19th century. The statutory system has not been fundamentally amended since 1817, so the juridical approach then chosen is still the first cause of the problematic operation of the taxable event. An extension of the juridical starting point may eliminate the conflict between the rationale and the legislative text.

Part II: set-up for a new taxable event
The conclusion about the discrepancy between the taxable event and the intention of the legislature inevitably leads to the second part of the research question. The search is for a new standard, one with the clearest possible description of the conditions for levying inheritance tax deemed relevant by the legislature. While these conditions can be derived from legislative history, to arrive at a new taxable event they cannot be written into law indiscriminately. Apart from the requirement about the identical treatment of economically identical cases, other principles of proper legislation – such as legal certainty, efficiency and simplicity – should likewise be taken into account. Hence, these principles have been used to arrive at a concrete standard. Material derived from other legal systems and legal history has been used as a source of inspiration.

This method has led to a taxable event encompassing the following four conditions.

1. The inheritance tax is a tax on certain acquisitions and spotlights the position of the acquiring party. Instead of imposing a tax on the property bequeathed or its transfer, the acquisition is taxed. In addition, the inheritance tax relates to a specific date. The levy is aimed at what has been acquired on the date of the acquisition.

2. The object of the acquisition comprises the property acquired, within the meaning of article 3:1 Dutch Civil Code. The taxable event is not restricted to a certain property. This wide scope implies that an entitlement to future income is subject to the levy of inheritance tax as well. As long as the acquiring party may apply an acquisition price for the levy of income tax that equals the value over which it has paid inheritance tax, concurrence with income tax will not arise.

3. The acquisition should be the result of the testator’s death. This condition distinguishes the inheritance tax from the gift tax. The gift tax is a separate
levy in the Dutch system, relating to all benefits from generosity that take place during life, also if their motive involves the saving of inheritance tax. Acquisitions based on legal acts during life may nevertheless be subject to the levy of inheritance tax, if the acquisition cannot be valued according to an objective criterion until the death of the testator. Situations where this occurs will be detailed later on.

4. It needs to be possible to allocate the acquisition to the estate of the testator or to a withdrawal from the testator's property during his life. Although the inheritance tax is an acquisition tax, which taxes enrichment on account of death, at the same time it is important to whose property the enrichment may be allocated. Only a benefit provided by the testator can be taxed. The testator cannot grant the acquiring party a greater benefit than the former actually possesses. Generosity from the part of the testator is not required. Still, the acquisition should not involve business motives. As this criterion is rather vague, the law may best list any acquisitions not based on business motives. A catch-all provision based on the rationale of the regulation may be added, to prevent any abuse. Income tax may be levied if it regards benefits from business activities.

Essential to application of these conditions is the realisation that the legislature pursues an economic concept of acquisition, which can be summarized as follows:

• In principle, at the time of the legal acquisition the levy is based on the fair market value.
• As long as it is not possible to determine the value of an acquisition according to an objective criterion, there will not be any levy until such objective assessment of the value is possible.
• Changes in an acquisition occurring subsequent to the testator's death are solely followed if they are the consequence of an optional right being exercised that had already existed on the date of death or resulted from the will of the testator.

These concrete standards have been combined into a proposition to amend the Inheritance and Gift Tax Act 1956. The Legislative Drafting Instructions applicable in the Netherlands when preparing legislation and regulations have been used to formulate the proposition. Article 1 discusses the taxable event for inheritance tax purposes. Article 2 includes the taxable event for gift tax purposes. Article 3 contains common provisions relating to the valuation and the timing of the levy.

Article 1.
1. Inheritance tax is levied upon an acquisition of property as a result of or after the death of a person who lived in the Netherlands at the time of death, insofar as the acquisition can be attributed to the estate of the testator or to a withdrawal from the property of the testator, and if the acquisition takes place: a. under inheritance law; b. under matrimonial property law;
c. under a gift within the meaning of article 186(2) Book 7 of the Dutch Civil Code;
d. under the payment to a natural obligation within the meaning of article 3 of Book 6 of the Dutch Civil Code, including the conversion of such obligation into a legally enforceable obligation;
e. from separated private property within the meaning of article 2.14a(2) of the Income Tax Act 2001; or
f. in other cases than those referred to above, if the acquisition is not set off by an arm’s length payment.

2. In the event of an acquisition within the meaning of the first paragraph, section e, the property acquired is deemed to be attributable to a withdrawal from the property of the testator, insofar as the property and debts from the separated private property have been allocated to the testator until his death, under article 2.14a(2) of the Income Tax Act 2001. The first sentence applies mutatis mutandis regarding property and debts within the meaning of article 2.14a(7) of the Income Tax Act 2001 that would have been allocated to the testator up to the moment when the latter died if the latter article had not been applied.

3. Upon an acquisition after the death of the testator, inheritance tax will solely be levied insofar as the acquisition results from the exercise of an optional right that had already existed on the date of death or arose on the back of a last will of the testator. Insofar as the exercise of the optional right changes an earlier acquisition, the levy relating to that acquisition will be revised in this respect.

4. The inheritance tax is levied with the acquiring party for the part the latter acquires net of the debts and expenses it has assumed for the acquisition of the property.

Article 2.
1. Gift tax is levied upon the acquisition of property under a donation by someone who resided in the Netherlands at the time of the donation.
2. For the application of this Act, donation is considered to be the gift within the meaning of article 186(2) Book 7 of the Dutch Civil Code and furthermore the payment to a natural obligation within the meaning of article 3 Book 6 of the Dutch Civil Code.
3. The term gift neither includes the benefit as a result of renunciation by an heir or legatee, nor the benefit as a result of the spouse renouncing a statutory distribution of the inheritance under article 18 Book 4 Dutch Civil Code.
4. The gift tax is levied over what the donee acquires, possibly net of expenses and obligations related to the gift, as a result of which either the donor or a third party is benefited.
5. Insofar as inheritance tax is due on an acquisition, gift tax will not be levied.

Article 3.
1. At the time of the acquisition the acquisition is taken into account for the fair market value.
2. For the application of this Act the following acquisitions will not be taken into account:
   a. the acquisition of a property that is subject to a usufruct, insofar as this usufruct entitles to disposing of and consuming the property;
   b. the acquisition of a receivable, insofar as the receivable can only be claimed upon or after the death of the debtor, or earlier upon the commencement of a future uncertain event;
   c. the acquisition that depends on a future uncertain event, insofar as the use has not yet started for the acquiring party;
   d. the acquisition in other cases than referred to before, insofar as valuation of the acquisition according to an objective criterion is not possible.
3. When an exception as referred to in the second paragraph no longer applies in full or in part to the acquisition or its benefits, an acquisition will be taken into account for that part. For the application of article 1(1) and article 3(1) of
this Act the date of the acquisition is put on a par with the date on which the acquisition has been taken into account.

4. The acquisition of usufruct within the meaning of the second paragraph, section a, is taken into account for the fair market value of the property to which the usufruct relates.

5. The debt corresponding with the receivable as referred to in the second paragraph, section b, is taken into account for a value of nil.

6. Upon an acquisition of a property under the resolutive condition of death, with which the acquiring party is entitled to dispose of and consume the property, the property is taken into account at the value applicable as if the property had been acquired unconditionally.

Adopting this legislative text would lead to a considerable simplification. Twelve full articles are deleted, whereas a mere three articles are implemented. They include a sound description of the taxable event. An additional advantage of a single general standard is that it avoids complicated concurrence between the various fictitious acquisitions. Most points of criticism discussed in literature are remedied, too. Above all the proposition leads to the introduction of an economically taxable event, thus observing the intention of the legislature to treat economically identical cases in the same manner.

Part III: application

The justice of a statutory standard is directly proportional to its application. The standard set on the basis of the theoretical approach should lead to a practical result that corresponds with the research assumptions. This being a new standard, it is obviously not possible to prove its merits based on everyday practice. What can be examined, though, is how application of the standard would work out in concrete cases. Applied to a number of major practical cases, the following changes can be recognized compared with the current Act.

**Statutory distribution**

Under the existing Act, the receivable that a child acquires as part of the statutory distribution is directly taxed at a lump-sum value. Under the proposition the non-claimable receivable of a child on account of a statutory distribution is not yet taken into account because this solely regards a bare expectation for which there is no identifiable fair market value. As a result, the surviving spouse is taxed for all property. The child is as yet involved in the levy, insofar as repayments are made on the receivable or the receivable becomes due and payable. If so, the receivable is taxed at the fair market value. Hence, this includes added interest.

**Usufruct**

The acquisition of usufruct is currently based on lump-sum valuation rules and may involve complex anti-abuse legislation. This existing methodology does little justice to economic reality. As an alternative, it is proposed to make a

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579. Dutch intestate succession contains the so-called "statutory distribution", meaning that all property and debts are allocated to the surviving spouse by operation of law, while the children acquire a receivable from the surviving spouse amounting to their share in the inheritance. Both the principal sum of the receivable and any interest can basically only be claimed upon the death of the surviving spouse.
distinction according to the rights attached to usufruct. If the right of usufruct entitles to powers to dispose of and consume the encumbered property, the usufructuary is taxed on the value of the unencumbered property. Just like with a statutory distribution, in such a case the bare owner solely has a bare expectation - only at the end of the usufruct can his acquisition be included in the levy. Other acquisitions of usufruct are subject to the main rule of valuation at the fair market value.

The treatment of a fideicommissum follows the same methodology. A fideicommissum de residuo (the fideicommissary heir has the power to dispose of and consume) is subject to the same rules as a usufruct to which the rights of disposal and consumption are attached. As the tax on a “classic” fideicommissum (only the income from the property accrue to the fideicommissary heir) is the same as on another usufruct, it is levied at the fair market value.

Set-off clause in marriage contract

If a final set-off clause applies that is solely effective upon death, under current case law the receivable resulting from the set-off acquired by the surviving spouse is not taxed with inheritance tax. Under the proposal, however, levy does take place in such a situation. The reason to do so is that in the event of a limited effect of the set-off clause (unilaterally, optional, not applicable in the event of a divorce, and so on), the acquisition of the surviving spouse can be traced to a decrease in wealth of the testator. Hence, this is taxable.

Revocable gift

Under the current legal methodology a revocable gift immediately leads to taxation. The gift tax levied is refunded upon a revocation. Under the proposal, a revocable gift is not yet considered to be an acquisition, as the acquisition cannot yet be valued according to an objective criterion. This is because due to the revocation the donor can once again dispose of that which has been gifted. Taxation can solely take place if the acquisition becomes irrevocable. In this respect, only acquisitions resulting from death fall within the scope of the inheritance tax. Other than under the current law, gifts in the event of an approaching death may solely be taxed with gift tax, provided they are unconditional and irrevocable.

Separated private property

The current Act includes a fiction as a consequence of which heirs are taxed on their separated private property (“Afgezonderd Particulier Vermogen” - APV), irrespective if or and to what extent they have actually benefited (or will benefit) from that property. Still, the bare expectation of a future benefit from the APV

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580. A set-off clause in a marriage contract can arrange that certain types of income or the property of the spouses are shared. A distinction can be made between a final set-off clause, effective when a marriage is dissolved, and a periodic set-off clause, effective during a marriage. The set-off clause will grant one spouse a claim on the other spouse under the law of obligations.

581. Dutch tax legislation has a specific regime for property separated in a trust, foundation or a comparable legal form for private purposes. The separated property is fully allocated to the grantor for income tax purposes. Upon the death of the grantor allocation takes place to his heirs.
is insufficient as a basis for taxation. Hence, it is proposed to solely levy inheritance tax upon an acquisition from the APV.