Executive summary

On 19 September 2017, the Dutch Ministry of Finance published its tax budget proposals (the Proposals) for fiscal year 2018 and future fiscal years. The Proposals are generally in line with the earlier announcements\(^1\) and the consultation document including a first draft of legislative proposals that was opened for public consultation by the Dutch Ministry of Finance earlier this year.\(^2\)

The Proposals contain several anticipated tax law changes to be effective as of 1 January 2018, including anticipated new legislation with respect to the Dutch Dividend Withholding Tax Act. This Tax Alert only addresses the Dutch Dividend Withholding Tax Act.

The Proposals with respect to the Dutch Dividend Withholding Tax Act contain the following two key amendments:

1. Introduction of a broader domestic dividend withholding tax exemption for dividend distributions to recipients resident in the European Union (EU)/European Economic Area (EEA) or a country that has concluded a tax treaty with the Netherlands covering dividends, combined with the introduction of a specific anti-abuse rule.

2. Treat Cooperatives (Coops) that predominantly (for 70% or more) operate as holding/financing companies similar to limited liability companies (BVs and NVs).
Detailed discussion

Expansion of the Dutch dividend withholding tax exemption

The Proposals put forward legislation to expand the existing domestic exemption in the Dutch Dividend Withholding Tax Act to a broader group of recipients. No Dutch dividend withholding tax will be due on distributions if the (non-individual) recipient is the beneficial owner and meets the following cumulative criteria:

- Hold(s) at least 5% in the distributing company (or even lower in certain circumstances if a related company holds such 5% interest)
- Is resident of the EU/EEA or a country that has concluded a tax treaty with the Netherlands covering dividends
- The recipient:
  - Does not hold the interest in the distributing entity with the main purpose or one of the main purposes to avoid the levy of Dutch dividend withholding tax (subjective test); or
  - The arrangement or series of arrangements is not considered wholly artificial; an arrangement or series of arrangements is considered artificial to the extent that it is not put into place for valid commercial reasons which reflect economic reality (objective test).

The subjective test can generally be met if within the chain of ownership the entity that carries out a business enterprise is a resident of a treaty jurisdiction or the EU/EEA.

For purposes of the objective test, valid business reasons are deemed present if the (EU/EEA or tax treaty resident) recipient:

- Carries on an active business enterprise, or
- Is an intermediate holding company performing a linking function between the business operations of the (indirect) parent entity and the operations of the lower-tier subsidiaries and has "relevant substance."

Intermediate holding companies are considered to have relevant substance if they: (i) meet the Dutch minimum substance requirements in their country of residence; (ii) have at least €100,000 of (internally or externally rendered) labor costs relating to the holding activities; and (iii) own/rent an office space that is used to perform their activities for at least 24 months. A grandfathering period for the above-mentioned labor cost and office space requirements exist and should ultimately be met on 1 April 2018.

The Proposals put forward a notification requirement for the distributing entity. Upon a dividend distribution to non-Dutch taxpayer(s) whereby the domestic exemption is applied, the distributing entity should notify the Dutch Tax Authorities within one month after the dividend distribution that the requirements to apply the domestic exemption are met.

It has been explicitly mentioned that the subjective test and the objective test are the Dutch domestic implementation of the Principle Purpose Test of the Organisation for Economic Co-operation and Development's (OECD's) Base Erosion and Profit Shifting (BEPS) Action 6, while adhering the General Anti-Abuse Rule of the EU Parent-Subsidiary Directive and EU law as established in case law by the European Court of Justice.

Hybrid entities

Specific provisions are included with respect to situations in which the recipient is not considered to be the qualifying recipient as a result of its hybrid nature. A qualifying recipient is a non-transparent entity that is treated as a taxpayer in its country of residence. However, if the recipient is considered as a transparent entity in its country of residence, the underlying participants can be considered the recipient if the income is treated as an item of income at the level of all underlying participants.

Amendment of the Dutch dividend withholding tax treatment of Coops

Under the current legislation, dividend distributions by BVs and NVs are in principle subject to 15% dividend withholding tax (although reductions and exemptions might be applicable based on treaties, EU legislation or domestic legislation), while dividend distributions by Coops are in principle not subject to dividend withholding tax, except for certain "abusive" situations.

The Proposals put forward legislation to eliminate the difference between distributions by limited liability companies (BV and NV) and Dutch Coops that predominantly act as holding/financing companies (Holding Coops). Based on the updated Dividend Withholding Tax Act, only Holding Coops will be deemed a company with a capital divided into shares, resulting in the fact that distributions by such Holding Coop will beCOME subject to dividend withholding tax. Distributions by a Dutch Coop that does not qualify as a Holding Coop are still not subject to Dutch dividend withholding tax.
A Holding Coop is defined as a Coop that is part of an international holding structure and predominantly (70% or more) performs holding activities and/or intercompany financing activities. In the Proposals, two illustrative examples are given of situations in which a Coop should not be considered to be a Holding Coop:

- A Coop holding more than a 70% investment in subsidiaries which actively holds these subsidiaries, has employees on the payroll and performs other headquarter activities.
- A Coop holding more than a 70% investment in subsidiaries that based on other facts and circumstances – such as employees, office space and active involvement in the business of the subsidiaries – is actively managing its subsidiaries' businesses, as for example for private equity structures.

As a result, only distributions made by Holding Coops to (affiliated) members that (directly or indirectly) hold a membership interest of at least 5% shall become subject to 15% statutory Dutch dividend withholding tax, unless the member can benefit from the above-mentioned Dutch dividend withholding tax exemption or treaty exemption.

Next steps and timing

The Proposals are currently subject to the review and discussions by the Dutch Parliament and as such may be subject to further possible amendments. Voting is scheduled for 16 November 2017. If adopted, the Proposals are expected to come into effect on 1 January 2018.

Once enacted, distributions after 1 January 2018 may become subject to dividend withholding tax, even if they are derived from profits generated before that date. Similarly, recipients that currently don’t meet the requirements for the domestic exemption, may be able to benefit from the expanded exemption after 1 January 2018 on distributions of profits generated before that date.

Implications

The expansion of the Dutch dividend withholding tax exemption could be seen as an important step in further strengthening the Dutch fiscal investment climate for genuine economic activities. At the same time, the proposed changes address the outcome of the OECD’s BEPS Action 6. Therefore, the requirements to benefit from the proposed domestic dividend withholding tax exemption could be seen as the Dutch implementation of the Principal Purpose Test of BEPS Action 6, as well as the General Anti-Abuse Rule of the EU Parent-Subsidiary Directive.

Also, next to the ability to benefit from the domestic dividend withholding tax exemption certain recipients can benefit from reduced dividend withholding tax rates based on applicable tax treaties.5

Endnotes


3. The 24 month office space requirements may also be met prospectively.


5. As for the possible impact of the MLI on the workings of certain tax treaties, see EY Global Tax Alert, OECD releases multilateral instrument to implement treaty related BEPS measures on hybrid mismatch arrangements, treaty abuse, permanent establishment status and dispute resolution, dated 2 December 2016.
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