

Amendments to dividend withholding tax

The Netherlands: September 2017

In Brief

A formal legislative proposal with respect to amendments to the Dutch Dividend Withholding Tax Act has been published on Dutch Budget Day (19 September 2017). These rules are expected to be effective as from 1 January 2018.

The legislative proposal introduces a broadened unilateral dividend withholding tax exemption in conjunction with anti-abuse rules along the lines of Action 6 of the OECD Base Erosion and Profit Shifting (“BEPS”) Project and seeks to align the dividend withholding tax treatment of holding cooperatives and Dutch entities with a capital divided into shares (e.g. BV/NV). With the broadened exemption the Netherlands aims to uphold the attractive fiscal climate of the Netherlands. At the same time this legislative proposal is an example of legislation that aims to tackle tax avoidance. A draft version of this legislation was opened for consultation in May 2017. We appreciate that reactions to this consultation have been taken into account to some extent when drafting this formal legislative proposal.

Broadened dividend withholding tax exemption

The legislative proposal broadens the current dividend withholding tax exemption for all Dutch resident entities subject to Dutch dividend withholding tax, including BVs/NVs and cooperatives with qualifying membership rights. The dividend withholding tax exemption applies if:

- the recipient of the dividends distributed by the Dutch entity is a resident of the EU, EEA or another state with which the Netherlands has concluded a tax treaty that includes a dividend article (including tax treaties with other countries within the kingdom of the Netherlands); and
- the recipient of the dividends would have been able to apply the Dutch participation exemption or participation credit to the dividends if it would have been a resident of the Netherlands.

Currently this exemption is only available to corporate shareholders with a qualifying interest in a Dutch entity that are established within the EU or EEA. The legislative proposal therefore substantially

broadens the scope of the exemption.

In cases where a Dutch entity distributes a dividend under the exemption, a notification of this should be made to the Dutch Tax Authorities within a month of the distribution.

Treatment of holding cooperatives

In order to align the dividend withholding tax treatment of cooperatives and entities with a capital divided into shares (e.g. BVs/NVs), so called ‘holding’ cooperatives (“Holding Coop”) will be treated similar to entities with a capital divided into shares, whereby dividend distributions by such Holding Coops will (as a starting point) be subject to dividend withholding tax (similar to e.g. BVs/NVs). However, a main precondition to the legislative proposal is that dividend distributions by ‘regular’ cooperative enterprises should continue to be exempt from dividend withholding tax in any event. Therefore, only these specific Holding Coops need to withhold dividend withholding tax if and to the extent that (i) the above-mentioned exemption does not apply, and (ii) distributions are made on qualifying membership rights (i.e. membership rights that entitles the holder thereof to at least 5% of the annual profits and/or the liquidation proceeds of the Holding Coop).

Holding Coops

A Holding Coop is defined as a cooperative of which the factual activities predominantly (at least 70%) consist of holding participations or intra-group financing activities. For the purpose of this test the activities of the cooperative during the year preceding to the dividend distribution are taken into account. The factual activities are primarily assessed on the basis of the total assets held by the cooperative.

However, other factors, such as revenue, activities that generated the profits, time spent by employees, total of assets and liabilities etc. may also be taken into account. In this regard two specific examples have been given.

Active top holding companies

The legislative proposal provides an example of a cooperative functioning as the top holding company of a group. Although the top holding cooperative's assets according to its balance sheet may consist for at least 70% of participations, the active management of its participations, employees and conducting other headquarter activities would result in this top holding cooperative to not being regarded as a Holding Coop.

Cooperatives in private equity structures

The legislative proposal also makes explicit reference to the use of cooperatives in private equity structures. In respect of these cooperatives it is noted that even if the assets of such a cooperative predominantly consist of interests in participations (at least 70%) it may nevertheless be considered a 'regular' cooperative and thus remain out of scope of dividend withholding tax. Relevant factors mentioned are employees, office space and the active involvement in the business activities of its participations.

Anti-abuse rules

The exemption for the withholding of Dutch dividend withholding tax will be subject to targeted anti-abuse rules, which are to be interpreted in accordance with Action 6 of the OECD BEPS Project. These anti-abuse rules do not apply however to cooperatives that do not qualify as a Holding Coop due to the fact that the dividend distributions by these cooperatives will not be subject to Dutch dividend withholding tax to start with.

Under the anti-abuse rules it should be assessed if the interest in the Dutch entity (e.g. Holding Coop,

BV or NV) is held with the main purpose, or one of the main purposes, to avoid the levy of dividend withholding tax (subjective test) and if the structure should be considered part of an artificial arrangement (objective test). A business structure is considered artificial if it is not put in place with business reasons that reflect economic reality. The above is a cumulative test, which in simplified terms, can be summarized as follows:

To determine whether the non-resident entity holds the interest in the Dutch entity with the main purpose or one of the main purposes to avoid Dutch dividend withholding tax (subjective test), it should be assessed whether the direct shareholder/member of the Dutch entity has been interposed to obtain a more favourable Dutch dividend withholding tax position. If so, it should still be determined whether the structure should be considered an artificial arrangement (objective test).

A structure should not be considered an artificial arrangement if it concerns a multinational enterprise/active investment structure. This should be the case if the immediate shareholder/member of the Dutch entity carries on an active business itself. Furthermore, if the immediate shareholder/member of the Dutch entity is an intermediate holding company and is considered to generate a more favourable Dutch dividend withholding tax position compared to the indirect shareholder that carries on an active business, the anti-abuse rules should nonetheless not be applicable if the immediate shareholder/member avails of sufficient relevant substance.

Sufficient relevant substance

Under the legislative proposal, the immediate shareholder/member is considered to have sufficient relevant substance if, in addition to the existing substance requirements, the shareholder/member meets two additional substance requirements. The company is required to have at least 100,000 EUR in employee costs. Furthermore, the company needs to have its own office space available from where it carries out its activities. If all substance requirements are met, the interest in the Dutch entity is deemed to be held for business reasons that reflect economic reality, in which case the anti-abuse rules are non-applicable.

Hybrid entities

Based on the legislative proposal, the withholding tax exemption may also be applicable to a dividend distribution where the relevant recipient is a hybrid entity which is considered an opaque entity based

for Dutch tax purposes but a transparent according to the laws of its State of incorporation. In such case, the treaty eligibility may be assessed at the level of the ultimate shareholders / partners in the hybrid entity, provided that the State of Residence of the relevant shareholders / partners considers the hybrid entity transparent.

In the reverse scenario (where a hybrid entity would be considered transparent for Dutch tax purposes but opaque from the perspective of the State of Residence of the ultimate shareholders / partners) the dividend withholding tax exemption could be applicable if the State of Residence of the hybrid entity would itself be a treaty jurisdiction and tax the dividend income accordingly (as an opaque entity).

Our view

Impact on business

We anticipate the legislative proposal to have a positive impact in most corporate/ multinational structures due to the broadened unilateral exemption. Active investment structures involving Dutch cooperatives which have sufficient people functions, substance and active involvement in the underlying business activities should (continue to) be able to be exempted from dividend withholding tax.

With the new rules being applicable as of 1 January 2018 (with some leeway for Holding Coops to 1 April 2018), existing cooperative structures – both in and outside private equity structures – should be carefully reviewed to confirm their tax efficiency going forward. This especially applies to cooperative structures without value-add functions in the Netherlands, which otherwise will fail to have ‘realistic’ substance.

In case you have a Dutch holding company, you should carefully consider your current structure and assess whether your existing reserves and future profits will remain exempt from dividend withholding tax or become subject to dividend withholding tax, going forward.

Timing

The legislative proposal should take effect as from **1 January 2018** and does not propose transitional provisions or grandfathering rules, except the two additional substance requirements that should enter into force as per 1 April 2018. We currently do not expect that the legislative proposal will be subject to significant amendments during the parliamentary proceedings and we expect that these rules will be timely adopted.

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