The Dutch policy with regards to attracting and keeping real substantial business activities remains unchanged. In the recently published Note regarding the parliamentary records the State Secretary for finance has indicated he wants to differentiate further between substantial business activities and artificial arrangements. Substantial companies with real business in the Netherlands should not be affected by this further differentiation. In these new documents the State Secretary gives a further commentary regarding the interpretation of the proposed measures. The State Secretary also emphasizes the importance of international collaboration in this respect.

**Background**

The proposals are a direct result of the changes in the EU Parent-Subsidiary Directive. This Directive provides the EU Member States with binding rules on the tax treatment of profit distributions paid within the EU by subsidiary companies to their parent companies. The Directive is aimed at eliminating juridical and economical double taxation. If the conditions are met, such profit distributions must be exempt from withholding tax. And, economic double corporate income taxation must be prevented either by applying the exemption or credit method. The provisions of the Directive are implemented in the Dutch Corporate Income Tax Act and the Dutch Dividend Tax Act.

The former provisions of the EU Parent-Subsidiary Directive gave rise to some undesired outcomes. The existing anti-abuse clause lacked clarity. Double non-taxation could arise because of the obligation for Member States to exempt profit distributions received by parent companies from taxation, even if the profit distribution had been treated as a tax deductible payment with the subsidiary. This effect could arise in case of hybrid financial instruments. To tackle the unintended effects, the Parent-Subsidiary Directive has been amended by the adoption of a GAAR and a specific provision to prevent double non-taxation in case of hybrid mismatches between the different tax systems used in the Member States.

**Participation exemption regime and dividend tax largely unaltered**

The implementation of the GAAR as now included in the Parent-Subsidiary Directive does not affect the participation exemption and dividend tax exemption as such. Further comments by the State Secretary have not changed this fact. The Dutch participation exemption regime aims at eliminating economic double taxation of profit distributions paid by a subsidiary to its parent company. A corporate taxpayer is exempt from Dutch corporate income tax on all benefits connected with a qualifying shareholding, in general a shareholding of at least five per cent. Such benefits are also eligible for an exemption of Dutch dividend withholding tax if distributed by a Dutch resident entity.

**Prevention of double non-taxation**

The participation exemption regime is amended to include a specific clause to prevent double non-taxation as a result of mismatches in tax effects. A clause which must be implemented by all EU Member States. A corporate taxpayer will not be eligible for the participation exemption or participation credit for received distributed profits to the extent that such distributed profits are deductible by the subsidiary. This might be the case for certain hybrid financial instruments. The intention of the taxpayer is irrelevant in this respect. The State Secretary has indicated that this clause affects any remunerations that are deductible. It is however not relevant whether they have actually been deducted. The clause does not deal with mismatches as a result of a different transfer pricing approach. Further the clause does not apply to capital gains with regard to the instrument, but this may be different in the case where particular installment are alienated or where an usufruct is established.

**Influence of foreign legislation**

According to the State Secretary, the Belgian notional interest deduction (NID) does not have any consequences for the application of the specific clause to prevent double non-taxation as a result of mismatches in tax effects. This is because there is no direct link between the NID and the actual payment or remuneration according to the State Secretary. For the application of this clause it is not relevant whether the other state consciously grants benefits or facilities. Of relevance is whether the remuneration or payment is deductible by its nature. The State Secretary indicates that this is for example the case in an Allowance for Corporate Equity (ACE) regime. Further, a system comparable to the fiscal unity regime or a group relief may have as a consequence that the payment is factually deductible for a group company and therefore indirectly by the payer, according to the State Secretary. The applicability of a foreign Controlled Foreign Company (CFC) regime to a Dutch shareholding cannot prevent that received gains are subject to Dutch taxation.

**Substantial holding regime**

The substantial holding regime changes in order to implement the Directive’s new GAAR. An entity resident outside the Netherlands that holds a substantial shareholding, i.e. five per cent or more, in a Dutch resident company will be subject to Dutch corporate income tax if the holding is held with Dutch dividend tax or personal income tax avoidance as one of the main purposes and if it is not put into place with valid commercial reasons which reflect economic reality. Even though the phrasing of the law is slightly changed to align with the GAAR, no substantive changes in the current practice are intended in this respect.
Would you like to receive more information on the requirements and conditions regarding the application of the participation exemption from 1 January 2016 onwards or advice for your specific situation please contact your PwC-adviser who will be pleased to assist you. You may also contact:

Knowledge Centre Tax & HRS
+31 (0)88 792 43 51
knowledge.centre.taxhrs@nl.pwc.com

**Withholding taxation**

The Dutch Dividend Tax Act will also be amended because of the GAAR. A co-op that is resident in the Netherlands will be obliged to withhold dividend tax on dividends distributed to its members if tax avoidance is one of the main purposes of the arrangements and the arrangement is not put into place with valid commercial reasons which reflect economic reality. Even though the phrasing of the law is changed to fit the GAAR, no substantive changes in the current practice are intended in this respect. Valid commercial reasons may for example exist if the co-op has a sound economic relevance. Valid commercial reasons may also exist if the membership in the co-op is attributable to the member’s business. In cases where the member is transparent according to Dutch legislation, the analysis must take place with the underlying parties. For the purpose of this clause it is noted that in cases where an exemption would have applied, for instance through a tax treaty, tax avoidance is never one of the main purposes of holding the shareholding. The State Secretary has said that in this regard no substantive changes have been aimed at.

**Substance**

The State Secretary has confirmed that the substance requirement of the composition of directors may be fulfilled at the level of the general partners in a limited partnership. For intermediary subsidiaries financial structuring and complying with administrative obligations may play a part in assessing the substance.

**Advance Tax Rulings**

In cases where an Advance Tax Ruling (ATR) has been granted regarding the non-application of the substantial holding regime or the withholding obligation for dividend withholding tax it is important to meet the new requirements in time. If the new substance-requirements are not met on 1 January 2016 the ATR will in principle be cancelled. Under very strict conditions taxpayers may be granted the opportunity to meet the substance-requirements by 1 April 2016. In order for this extension to apply taxpayers must notify this with the tax authorities before year-end. This will be further explained in a Decree that will be published shortly. Any gains received in the period between 1 January 2016 and the moment that the taxpayer meets the renewed substance-requirements will be subject to tax.

**Entry into force**

The proposals have been published by the Dutch Ministry of Finance on 15 September 2015, together with the Dutch Tax Package 2016. The proposal will become effective as of 1 January 2016. Any profits received in 2016 will therefore be subject to new legislation. The measures will apply to existing situations as well as the proposal lacks any transition law. Under circumstances a step-up may be granted for taxpayers that don't meet the new requirements. The proposal is subject to the parliamentary process and may therefor still be amended. We will keep you informed of any changes.

**Recommendations**

Depending on your situation the further commentary by the State Secretary may lead to points of attention. It is important to assess which consequences the law proposal has for your situation. PwC will be pleased to assist you.

**EU Member States**

All EU Member States must implement the changes to the Parent-Subsidiary Directive in their respective national legislation before 1 January 2016. If your company is actively involved in business throughout the EU, you may be affected by other legislative changes due to changes in the Directive. We understand that many Member States, including the United Kingdom, Belgium, Germany and France have together with the Netherlands chosen for a worldwide application of the specific clauses of the Parent-Subsidiary Directive.

**Contact**

Would you like to receive more information on the requirements and conditions regarding the application of the participation exemption from 1 January 2016 onwards or advice for your specific situation please contact your PwC-adviser who will be pleased to assist you. You may also contact: