NETHERLANDS

LAW & PRACTICE: p.3
Contributed by De Brauw Blackstone Westbroek

The ‘Law & Practice’ sections provide easily accessible information on navigating the legal system when conducting business in the jurisdiction. Leading lawyers explain local law and practice at key transactional stages and for crucial aspects of doing business.
Law & Practice

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De Brauw Blackstone Westbroek tax practice group focuses on both domestic and international corporate transactions, including M&A and intra-group reorganisations, as well as on financial transactions, including capital markets and structured finance transactions. The team provides tax advice on a regular basis to large Dutch and non-Dutch multinational companies and banks, typically assisting these clients in their more complex tax issues and strategies. The tax practice has special expertise in the tax aspects of innovative financial instruments and stock option and shares plans and regularly co-operates with the investment management group of De Brauw in structuring and analysing investment funds for retail and institutional investors, as well as the private equity industry. The practice covers all aspects of Dutch tax law, including detailed advice on corporate income tax and dividend withholding tax as well as on all international tax issues.

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1. Types of Business Entity, Residence and Basic Tax Treatment

1.1 Corporate Structures and Tax Treatment

Typically, large businesses in the Netherlands are structured as a private limited liability company (besloten vennootschap; BV), a public limited liability company (naamloze vennootschap; NV) or, less frequently, a co-operative (coöperatie; Coop). The common feature of these corporate forms is that they have legal personality: the BV, NV and Coop have rights and obligations independent of their participants. Shareholders of a BV or NV are not personally liable for the debts and obligations of the entity. The same applies for members of a Coop with limited liability.

The BV, NV and Coop are subject to Dutch corporate income tax (CIT). Distributions by a BV or an NV are in principle subject to 15% Dutch dividend withholding tax (DWT) unless relief is available based Dutch domestic tax law or one of the many tax treaties entered into by the Netherlands. No DWT is due on distributions by a Coop except in certain abusive structures.

1.2 Transparent Entities

In the Netherlands, limited partnerships (commanditaire vennootschap; CV), general partnerships (vennootschap onder firma; VOF) and funds for joint account (fonds voor gemene rekening; FGR) can be structured as transparent from a CIT and DWT perspective. These are contractual arrangements without legal personality.

A VOF is by default considered transparent from a CIT and DWT perspective. Hence, a VOF is not itself subject to CIT and no DWT is due on its distributions. Instead, the partners of a VOF may be subject to CIT or Dutch individual income tax (IIT) in respect of the part of the VOF’s profits attributed to them. A similar transparent treatment applies to ‘closed’ CV’s and ‘closed’ FGRs. A CV qualifies as ‘closed’ if the admittance, replacement and exit of any limited partner is subject to the prior approval of all other limited partners and the general partner (the “consent requirement”). An FGR qualifies as ‘closed’ if either the consent requirement is satisfied or if participation in the FGR may only be transferred to and (re-) issued by the FGR itself. If this is not the case, the CV or FGR qualifies as ‘open’ and is independently subject to CIT, provided that an open CV is treated as transparent in respect of the part of its profits attributable to its general partner.

CVs and VOFs are used from time to time by corporates, eg for structuring joint ventures. CVs and FGRs are frequently used for tax transparent investment structures, including private equity and real estate investment funds. Typically, the identity of the investors, the investment assets and, on that basis, the availability of favourable Dutch tax regimes for investment funds are decisive for investing through a tax transparent or opaque investment structure.

1.3 Determining Residence

Pursuant to Dutch domestic tax law, a corporate business form, including a BV, NV and Coop, and, arguably, an open CV or FGR are deemed to be resident in the Netherlands for tax purposes if it is incorporated under Dutch law. This deeming provision continues to apply even if the entity has its place of effective management outside of the Netherlands. However, in those cases a corporate tie-breaker rule of double taxation agreements (DTA) entered into by the Netherlands may render the BV, NV or Coop to be resident for DTA purposes in the jurisdiction where its place of effective management is situated. Entities which are not subject to the deeming provision are considered to be resident in the Netherlands for domestic tax purposes only if their place of effective management is situated in the Netherlands. This would be the case if the entity’s key strategic decision-making occurs in the Netherlands.

1.4 Tax Rates

A corporate taxpayer, whether resident in the Netherlands or subject to CIT as a non-resident, is liable to an annual levy of CIT at a rate of 25% of the amount of its profits exceeding EUR 200,000. A reduced rate of 20% applies to the amount of profits up to EUR 200,000.

An individual taxpayer, whether resident in the Netherlands or subject to CIT as a non-resident, is liable to an annual levy of IIT at progressive rates.

<table>
<thead>
<tr>
<th>Taxable income</th>
<th>IIT rate</th>
<th>Social security contribution rate (applicable to resident individuals)</th>
</tr>
</thead>
<tbody>
<tr>
<td>EUR 0 – EUR 19,822</td>
<td>8.35</td>
<td>28.15</td>
</tr>
<tr>
<td>EUR 19,822 – EUR 33,589</td>
<td>13.85</td>
<td>28.15</td>
</tr>
<tr>
<td>EUR 33,589 – EUR 57,585</td>
<td>42</td>
<td>0</td>
</tr>
<tr>
<td>EUR 57,585 and above</td>
<td>52</td>
<td>0</td>
</tr>
</tbody>
</table>

2. Key Features of The Tax Regime

2.1 Calculation of Taxable Profits

Both for CIT and IIT purposes, taxable profits are calculated separately from the calculation of profit for commercial purposes. In the Netherlands, taxable profits are determined on the basis of the principles of sound business practice (goed koopmansgebruik), specific statutory rules which expand on or deviate from the principles of sound business practice and
the arm's length principle. These principles are developed in case law and govern, among others, the recognition of benefits and costs as well as the valuation of assets and liabilities. Generally speaking, the principles of sound business practice require the taxpayer to calculate their taxable profit on an accruals basis.

2.2 Special Incentives for Technology Investments
The Netherlands has a number of special tax-related incentives to stimulate innovative technology investments, including a wage withholding tax reduction for R&D employees and an innovation box for the development of IP:

- wage withholding tax reduction – Netherlands-based employers are eligible for a wage withholding tax reduction equal to a percentage of their wage costs incurred for carrying out R&D activities. This reduction is applied in their wage withholding tax return and lowers the amount of such tax to be remitted to the Dutch Revenue Service by the employer;
- innovation box – Corporate taxpayers may elect to have the income derived from qualifying intangibles taxed at an effective CIT rate of 5% (instead of the regular statutory rate of 25%). Application of the innovation box is not subject to a cap on the profits derived from qualifying intangibles.

2.3 Other Special Incentives
Shipping companies may elect to apply the tonnage regime rules. The tonnage regime rules allow shipping companies to determine the taxable profits derived from the operation of ships and other vessels on the basis of the vessel’s net tonnage (rather than on the basis of the profits actually derived therefrom). The regular CIT and IIT rates apply to the amount of taxable profit calculated on this basis.

Subject to election, the taxable profit from the operation of ships is calculated as follows:

<table>
<thead>
<tr>
<th>Net Tonnage of Ship</th>
<th>Fixed profit per 1,000 net tons per day</th>
</tr>
</thead>
<tbody>
<tr>
<td>0 – 1,000 net tons</td>
<td>EUR 9.08</td>
</tr>
<tr>
<td>For the excess up to 10,000 net tons</td>
<td>EUR 6.81</td>
</tr>
<tr>
<td>For the excess up to 25,000 net tons</td>
<td>EUR 4.54</td>
</tr>
<tr>
<td>For the excess up to 50,000 net tons</td>
<td>EUR 2.27</td>
</tr>
<tr>
<td>50,000 net tons or more</td>
<td>EUR 0.50</td>
</tr>
</tbody>
</table>

Furthermore, tax allowances are available for qualifying investments in the energy sector (58%) and environmental friendly investments (36%, 27% or 13.5% depending on the investment). In addition, certain environmentally friendly investments are eligible for an accelerated depreciation regime.

2.4 Basic Rules on Loss Relief
A corporate taxpayer may carry back tax losses and offset these losses against the taxable profit of the previous year. In addition, a corporate taxpayer may carry forward tax losses for a period of nine years. The carry back and carry forward rules do not distinguish between capital and ordinary losses.

2.5 Limits on Deduction of Interest
While the Netherlands does not currently have a statutory general interest limitation rule, there are several rules which disallow interest deductions under specific circumstances which are considered to give rise to abusive practices. These interest limitation rules include:

- a limitation rule for related party debt – interest charges on related party debt are not deductible if the debt is connected with acquisitions, capital contributions or distributions made by the taxpayer or a related party. A safe harbour rule applies if the taxpayer demonstrates that the debt has been incurred and the acquisition, contribution or distribution has been made predominantly for valid business reasons. Alternatively, the deduction may be allowed if the corresponding interest income is subject to an effective tax of at least 10%, yet the Dutch Revenue Service may still deny the deduction in the absence of valid business reasons.
- a limitation rule for interest-free and low-interest debt – interest charges on related party debt are not deductible if the underlying debt carries no or a low interest rate and does not have a maturity date or a maturity date exceeding ten years.
- a limitation rule for debt-financing of subsidiaries – excessive interest charges on debts which are incurred to finance an equity investment in a subsidiary are not deductible if the benefits derived from the shareholding in the subsidiary are exempt pursuant to the Dutch participation exemption. This limitation applies to related party debts as well as third party debts. A tax escape is available to debt incurred to expand the group’s operational activities. Also, a de minimis applies for interest charges not exceeding EUR 750,000 per annum.
- a limitation rule for leveraged acquisitions – interest charges on debts which are incurred to finance the acquisition of a subsidiary which is included in a Dutch fiscal unity post-acquisition, are not deductible to the extent that these interest charges are considered excessive and exceed EUR1,000,000. Interest is considered excessive to the extent an acquisition debt-to-acquisition price ratio is exceeded. This ratio is 60% in the year of acquisition and is reduced.
in seven years by 5%-point per year to 25%. Please refer to item 2.6 for a discussion of the Dutch fiscal unity rules.

2.6 Basic Rules on Consolidated Tax Grouping
The Dutch fiscal unity allows group companies to be taxed on a consolidated basis for CIT purposes. When group companies are included in a Dutch fiscal unity, the activities, assets and liabilities of each group company are attributed to the parent company of the fiscal unity. As a result, transactions between the group companies included in the fiscal unity are disregarded for CIT purposes and tax losses of one group company are offset against the profits of another group company. The parent company files a single CIT return for the fiscal unity.

A fiscal unity is available, among others, where:

- the parent company holds the legal and economic ownership of shares representing 95% of the aggregate nominal paid-up capital of a subsidiary as well as 95% of its voting rights, profits and assets;
- the parent company and subsidiary apply the same taxable period and standards for determining their taxable profit;
- the parent company and subsidiary are resident in the Netherlands for CIT purposes without being considered a resident outside of the Netherlands for purposes of any DTA concluded by the Netherlands; and
- the parent company and subsidiary are incorporated as a BV, NV or similar corporate form.

Based on European Court of Justice case law, a fiscal unity is also allowed between Dutch group companies if their shares are held by one or more group companies resident in other EU member states. In addition, a fiscal unity may be formed in respect of Dutch permanent establishments of qualifying group companies.

2.7 Capital Gains Taxation
Capital gains and losses realised by a corporate taxpayer are included in its taxable profits and taxed at the same CIT rate as ordinary income. Pursuant to the Dutch participation exemption, benefits (including capital gains and dividends) are exempt from CIT when derived by a corporate taxpayer from a qualifying shareholding in a direct local or foreign subsidiary representing an equity interest of at least 5% in such subsidiary. The participation exemption does not apply to benefits derived from a shareholding in a direct subsidiary which is considered, or deemed to be considered, a low-taxied passive portfolio investment. Following the implementation of the amendments to the Parent-Subsidiary Directive, the participation exemption does not apply to dividends and similar distributions which are deductible at the level of the distributing subsidiary.

2.8 Other Notable Taxes
Whether incorporated or not, businesses may become subject to value added tax in the Netherlands when supplying services or goods in the Netherlands against consideration. The Netherlands does not levy stamp duty. Furthermore, the transfer or Dutch real estate or real estate companies is subject to Dutch real estate transfer tax.

3. Division of Tax Base Between Corporations and Non-Corporate Business

3.1 Closely Held Local Businesses
On the basis of the information from the Dutch Central Bureau of Statistics, 50.48% of the total number of businesses in the Netherlands operate in non-corporate form.

3.2 Corporate Rates and Individual Rates
For purposes of Dutch wage withholding taxes, an individual holding a substantial interest – which typically is a 5% or more equity interest – in a company is considered to earn wages at an amount which the same individual would have earned if this individual had performed his or her activities as employee. The amount of wages which is imputed to this individual on this basis, is subject to Dutch wage withholding taxes (as an advance levy) and to IIT. Please refer to 1.4 for a discussion of the substantial interest rules.

3.3 Accumulating Earnings for Investment Purposes
Individuals holding a substantial interest – typically a 5% or more equity interest – in an investment institution that qualifies for CIT exempt treatment are deemed to receive an annual return from their interest of 4% calculated on the fair market value of their interest as per the beginning of the relevant fiscal year. Furthermore, individuals holding a substantial interest in a company that is entitled to carried interest or similar rights will be taxed on the (undistributed) income from these rights at progressive rates up to 52% unless at least 95% of the income is distributed by the company. The individual is subject to 25% IIT on the income so distributed.

3.4 Sale of Shares in Closely Held Corporations
Individuals who hold, or are considered to hold, shares representing an interest of at least 5% in a company are subject to the substantial interest rules for IIT purposes. Under these rules, benefits (including capital gains and dividends) derived from a substantial interest in a company are subject to IIT at a flat rate of 25%.

3.5 Sale of Shares in Publicly Traded Corporations
Individuals who do not hold, and are not considered to hold, shares representing a substantial interest in a company, are
not subject to the substantial interest for IIT purposes. Rather, these individuals are subject to IIT at a rate of 30% of their income from savings and investments. In this respect, income from savings and investments is calculated as being equal to a fixed yield of 4% over the fair market value of their assets reduced by their liabilities subject to the savings and investment rules and measured, in general, at the beginning of the fiscal year. Legislative changes in respect of the determination of the fixed yield are supposed to come into force as of 1 January 2017. However, we expect that these changes will be subject to further political debate.

4. Key Features of Taxation of Inbound Investments

4.1 Withholding Taxes
The Netherlands does not impose withholding taxes on outbound payments of interest and royalties. The Netherlands does impose dividend withholding tax (DWT) on dividends and other distributions made by a company which is resident in the Netherlands to its shareholders at the rate of 15%. A full exemption, relief or a reduced rate may be available to shareholders either on the basis of Dutch domestic tax law or an applicable DTA. For example, a full exemption from DWT is available to a Dutch or foreign corporate taxpayer having a shareholding in a Netherlands-based company which qualifies for the Dutch participation exemption.

4.2 Primary Tax Treaty Countries
Based on the information from the Dutch Central Bureau of Statistics and the Dutch Central Bank, foreign investments into the Netherlands are predominantly made from Germany, France and the United States. The Netherlands has concluded DTAs with each of these countries.

4.3 Use of Treaty Country Entities by Non-Treaty Country Residents
In our experience, the Dutch Revenue Services does not challenge application of a DTA if there is no legal basis for such challenge in the DTA and more generally seems not to take an aggressive approach in this respect.

4.4 Transfer Pricing Issues
For CIT purposes, the arm’s length principle applies in full to transactions between affiliated entities. A key issue for inbound investors operating through a Netherlands-based company involves the valuation of intangibles, specifically hard-to-value intangibles, as well as the pricing of specific contractual arrangements, such as a cost contribution agreement, and transfer pricing questions regarding intra-group financing arrangements.

4.5 Related Party Limited Risk Distribution Arrangements
The Netherlands generally follows the OECD Transfer Pricing Guidelines. Accordingly, as long as limited risk distribution arrangements between affiliated corporate taxpayers are consistent with the OECD Transfer Pricing Guidelines, these should not be subject to challenge.

4.6 Variation from OECD Standards
The Netherlands generally follows the OECD Transfer Pricing Guidelines.

5. Key Features of Taxation of Non-Local Corporations

5.1 Taxation of Non-Local Corporations Versus Local Subsidiaries
Generally speaking, a corporate taxpayer which is not resident in the Netherlands for CIT purposes but has a permanent establishment in the Netherlands is subject to CIT for the profits attributable to this permanent establishment in principle in the same manner and at the same rates as a corporate taxpayer which is resident in the Netherlands and has a foreign company as its sole shareholder. In the case of a permanent establishment, however, the profits of a non-resident corporate taxpayer have to be attributed to the permanent establishment on the basis of a functional analysis. Furthermore, the treatment of internal financing and licensing arrangements between the foreign company and its Dutch permanent establishment is different from financing and licenses provided to a Dutch subsidiary.

5.2 Capital Gains of Non-Residents
The Netherlands renders a corporate taxpayer which is not resident in the Netherlands subject to CIT in respect of the benefits derived from a substantial interest in a Netherlands-based company if:

• the substantial interest – typically a 5% or more equity interest – is held with the main purpose, or one of the main purposes, to avoid the levy of IIT or DWT on a person other than the foreign corporate taxpayer; and
• there is an artificial arrangement or series of arrangements, which shall not be considered absent if there is sufficient substance.

Relief from CIT may be available on the basis of DTAs concluded by the Netherlands to the extent these allocate the taxation rights on capital gains on the disposal of or dividends on shares in a Netherlands-based company to the state where the shareholder is resident.
5.3 Change of Control Provisions
The Netherlands does not levy CIT solely by reason of the disposal of an indirect holding in a resident corporate taxpayer. However, the Netherlands has anti-loss trafficking rules that may result in a forfeiture of tax loss carry forwards in case of a direct or indirect change of control preceded or followed by a significant reduction of the business activities.

5.4 Determining the Income of Foreign-owned Local Affiliates
The Netherlands does not apply formulary apportionment to determine the pricing of transactions between affiliated corporate taxpayers which are resident in the Netherlands and foreign-owned. The Netherlands applies the at arm's length principle to determine the pricing of such transactions, including those involving the sale of goods and rendering of services.

5.5 Deductions for Payments by Local Affiliates
The Netherlands also follows the OECD Transfer Pricing Guidelines in this respect. On this basis, the Dutch State Secretary of Finance makes a distinction between intra-group services and shareholder activities. No fees may be charged for shareholder activities while an arm's length fee, including a profit mark-up, should be charged for intra-group services. However, certain head-office costs – administration, legal, HR – and, subject to approval by the Dutch Revenue Service, costs for certain other non-core activities may be on-charged without a mark-up.

5.6 Constraints on Related Party Borrowing
For CIT purposes, related party borrowing and lending between foreign-owned local affiliates and non-local affiliates may be subject to specific interest limitation rules, such as the anti-base erosion and acquisition debt rules described in 2.5 above.

6. Key Features of Taxation of Foreign Income of Local Corporations

6.1 Foreign Income of Local Corporations
A resident corporate taxpayer is subject to CIT on its worldwide profits, including the profits derived from foreign sources. However, two significant exceptions apply to the system of worldwide corporate taxation. Firstly, if a resident corporate taxpayer derives benefits (including capital gains and dividends) from a shareholding which qualifies for the Dutch participation exemption, these benefits are exempt from CIT. Secondly, if a resident corporate taxpayer derives profits from a foreign permanent establishment or foreign real estate, these profits are also exempt from CIT pursuant to the Dutch permanent establishment exemption. Exceptions apply to low-taxed passive investment subsidiaries and permanent establishments.

6.2 Non-Deductible Local Expenses
Costs attributed to a foreign permanent establishment of a Dutch corporate taxpayer are in principle not deductible in the Netherlands.

Transaction expenses relating to the acquisition or disposal of shares in a subsidiary that qualifies for the participation exemption are not deductible. Furthermore, limitations on the deductibility of interest on loans (deemed) attributable to certain qualifying subsidiaries could apply as well based on the statutory anti-base erosion or acquisition debt rules.

6.3 Taxation of Dividends from Foreign Subsidiaries
Please refer to item 6.1.

6.4 Use of Intangibles
In cases where a resident corporate taxpayer transfers intangibles to a foreign affiliated company, the resident corporate taxpayer is deemed to have sold the intangibles to this company at their fair market value. As a result, the resident corporate taxpayer has to recognise a capital gain or loss on the transfer. If, instead, a resident corporate taxpayer licenses intangibles to a foreign affiliated company, an arm's length royalty is imputed to the resident corporate taxpayer.

6.5 Taxation of Income of Non-Local Subsidiaries Under CFC-Type Rules
The Netherlands currently has limited controlled foreign company (CFC) rules. Please note that the proposal for an EU Directive on anti-tax avoidance includes extensive CFC rules which, if adopted, the Netherlands would be required to implement.

Under the existing CFC rules, a resident corporate taxpayer is required to mark to market its shareholding in a direct foreign subsidiary if:

- the resident corporate taxpayer holds a direct interest of at least 25% in the foreign subsidiary;
- the foreign subsidiary's assets consist for 90% or more of portfolio investments; and
- the foreign subsidiary is not subject to a tax on its profits, as determined in accordance with the applicable standards for CIT purposes, of at least 10%.

6.6 Rules Related to the Substance of Non-Local Affiliates
Under specific circumstances, substance requirements apply to non-resident companies holding a substantial interest in a Dutch resident company (see also item 5.2). In those cases, a non-resident company would not become subject to CIT by reason of their substantial interest if it is an intermediate holding company within the group and satisfies the substance requirements for Dutch holding companies. These
substance requirements compel such a holding company, among others, to have at least half of its board members be Dutch residents and to maintain a minimum level of equity appropriate with its risk exposure on transactions with affiliates.

7. Anti-Avoidance
Dutch tax law allows the Dutch Revenue Service to challenge tax avoidance schemes on the basis of abuse of law (fraus legis). Abuse of law may apply if the transaction pursued by a taxpayer results in tax consequences which are contrary to the object and purpose of the relevant statutory provisions and if the taxpayer has pursued that transaction with the aim to avoid Dutch taxes.

8. Audit Cycle
There is no regular routine audit. In fact, audits are rather rare in the Netherlands. In principle, the Dutch tax authorities check a tax return retrospectively. If the tax return requires further investigation, the authorities can ask for further information to verify whether the tax return is correct. In addition to this traditional method, the Netherlands also applies ‘horizontal monitoring’. Horizontal monitoring is a form of working in the present based on mutual trust and transparency between the taxpayer and the tax authorities. If tax risks occur, the taxpayer needs to inform the tax inspector at an early stage about these risks.

9. BEPS
9.1 Government Attitude
The Dutch government has taken due account of the significance of multinational enterprises for its open, services-oriented and knowledge-based economy as well as the importance of preserving a level playing field for multinational and domestic enterprises. Accordingly, it seeks to balance the need to counter abusive practices, whether employed by multinational or domestic enterprises, with the risk that overly broad or insufficiently tailored measures may interfere unreasonably with genuine business activities.

9.2 Profile of International Tax
On 5 October 2015, the Dutch government published a letter describing its official view on the BEPS project. According to the letter, the Dutch government fully supports the outcome of the BEPS projects and it commits itself to take all necessary steps to implement the measures mentioned in the BEPS action plans. The Dutch government stresses the need to stop international tax avoidance and the improper use of domestic and international tax law, which it believes can be achieved only if all OECD member states, or at least all EU member states, act together on these topics. It is not yet clear to what extent the Dutch government’s position will have an impact on the BEPS project.

9.3 Competitive Tax Policy Objective
The Dutch government seeks to balance the need to counter abusive practices with the need to avoid overly broad or insufficiently tailored measures. The Dutch government has taken the position that this balancing act is carried out most effectively in a two-pronged approach. It aims to align, on a pro-active basis, both its domestic legislation and its negotiation position for double taxation agreements with the BEPS actions when it comes to exchange of information, country-by-country reporting and profit attribution based the arm’s length standard. Its reasoning seems that these measures do not affect the attractiveness of the Dutch tax system to sound business operations. In respect of other measures that have been proposed, such as hybrid mismatches, controlled foreign company and interest limitation, the Dutch government seeks to co-ordinate efforts to ensure binding rules are developed with due regard for a level playing field and the fundamental drivers of the competitiveness of the Dutch tax system.

9.4 Key Features of Competitive Tax Policy
The Dutch government has long considered that the features of its business climate which render the Netherlands an attractive jurisdiction for multinational enterprises, are:

- the availability of a full participation exemption for benefits which a Dutch resident corporate taxpayer derives from a qualifying shareholding in a direct foreign or local subsidiary;
- the absence of withholding taxes on outbound interest and royalty payments;
- the extensive network of double taxation agreements which the Netherlands has concluded with other jurisdictions; and
- the possibility to obtain certainty in advance from the Dutch Revenue Service on the Dutch tax consequences of contemplated transactions, by means of an APA or ATR.

In their final form, the BEPS actions do not yield specific vulnerabilities for these key features of the Dutch corporate taxation system. Inevitably, the implementation of some BEPS actions will require certain amendments to, for example, the rules governing the participation exemption. However, these amendments are expected to result in a more robust corporate taxation system for the Netherlands which is also better aligned with the domestic systems of other European member states, notably the United Kingdom, Ireland and Luxembourg. Moreover, the Dutch government intends to appropriate budgetary proceeds arising from implementation of the BEPS actions to offset, where necessary, a reduction in the competitive nature of its corporate taxation system.
9.5 Proposals for Dealing with Hybrid Instruments

The proposal for an EU Directive published on 28 January 2016 lays down rules against tax avoidance practices that directly affect the functioning of the internal market. Article 10 of the proposal sets out rules tackling hybrid mismatches within the EU. No rules have been proposed by the EU yet in relation to hybrids involving non-EU jurisdictions. The proposed rules address structures resulting in multiple deductions or deductions without inclusion created through:

- hybrid entities, meaning entities treated as opaque by one EU Member State while another EU Member State treats the entity as tax transparent; and
- hybrid instruments, meaning instruments that give rise to non-taxed income in one EU Member State while the instrument gives rise to a tax deduction in another EU Member State.

These new rules will apply in addition to the existing hybrid mismatch rule in the Parent-Subsidiary Directive, which the Netherlands has implemented. As of 1 January 2016, the Netherlands applies the hybrid mismatch rule of the Parent-Subsidiary Directive on a worldwide basis, ie to hybrid mismatches between a Dutch resident company and a subsidiary resident elsewhere in the EU as well as those between a Dutch resident company and a subsidiary resident outside the EU.

9.6 Territorial Tax Regime

The Netherlands indeed has a corporate taxation system largely based on the territoriality principle. In practice, the Netherlands only levies tax from Dutch resident corporate taxpayers on profits originating from the Netherlands.

The interest limitation rules currently in force in the Netherlands do not include a general limitation or disallowance of interest deductions. Rather, these rules are tailored to deny interest deduction in specific circumstances which are considered to give rise to abusive practices. As a result, in many structures Dutch corporate taxpayers can deduct interest expenses attributable to exempt foreign investments.

Accordingly, the interest limitation proposals in the BEPS actions and in the proposed EU Directive will have an impact on the current Dutch interest limitation rules. Article 4 of the EU Directive proposal provides for a limitation on interest deduction rule that limits the deductibility of exceeding borrowing costs. This earnings-stripping rule seeks to limit the deduction of net interest expenses to 30% of the taxpayer's earnings before interest, taxes, depreciation and amortisation (EBITDA). EBITDA must be calculated based on the taxable profits of the taxpayer rather than on its commercial accounting profits. Profits from qualifying domestic or foreign subsidiaries which are exempt under participation exemption regimes will therefore not increase the capacity to deduct interest. The proposal includes a group ratio escape. This escape allows taxpayers to fully deduct interest if the taxpayer can demonstrate that its stand-alone debt-equity ratio is lower than the equivalent consolidated ratio of its group. A taxpayer may carry forward EBITDA to the extent EBITDA does not fully absorb its interest expenses for a fiscal year. Similarly, a taxpayer may carry forward interest expenses to the extent a deduction for these expenses is disallowed in a fiscal year. The limitation on interest deduction will not apply to a wide range of financial undertakings. However, the EU has expressed its intention to introduce a rule at a later stage that also applies to financial undertakings.

The proposed earnings-stripping rule is likely to have a certain impact on Dutch companies that are on top of or part of cross-border structures that use (low-taxed) intra-group financing companies or hybrid financing arrangements which structures could include private equity funds as well as corporate structure with headquarters or regional headquarters in the Netherlands.

9.7 CFC Proposals

As mentioned, the Netherlands has based its corporate taxation system on the territoriality principle, including a full participation exemption for benefits derived by a Dutch resident corporate taxpayer from a qualifying shareholding in a direct foreign subsidiary. This is based on the principle of capital import neutrality, ie a Dutch group operating in a foreign jurisdiction should be subject to the same level of taxes on its operational profits as a local player in that jurisdiction would be and should not be confronted with an additional tax in the Netherlands. CFC legislation such as a sweeper CFC rule that also covers operational profits of a CFC – including the CFC rule recently proposed by the EU – is not in line with the aforementioned principle. However, one could debate the practical relevance of this argument with reference to the limited number of low-taxed jurisdictions where sizeable operational profits are created by a qualifying CFC.

Turning to CFC proposals, articles 8 and 9 of the EU Directive proposal provide for CFC rules which seek to include CFC income where a CFC is subject to an effective tax rate lower than 40% of the effective tax rate applicable to its parent company and its income consists for at least 50% of tainted profits. These rules will put pressure on offshore intra-group financing, licensing or leasing structures. We do not expect these rules to have a wide effect on EU CFCs held by Dutch corporate taxpayers with reference to the corporate income tax rates applicable within the EU relative to the Dutch rate and the specific regime that applies to EU CFCs. Pursuant to this regime, EU CFCs are only captured in case of wholly artificial arrangements which do not reflect
9.8 Anti-Avoidance Rules

BEPS Action 6 describes a minimum level of protection against treaty shopping, including, among other things, a limitation-on-benefits (LOB) rule, a principal purpose test (PPT rule) and a mechanism that would deal with conduit financing arrangements. The Netherlands announced that they aim to meet this minimum level in new double taxation agreements. As part of the current practice, the Netherlands is already willing to include a PPT or LOB rule to avoid treaty abuse upon request by the other country.

The impact of the rules very much depend on the form of rules that will ultimately be adopted and implemented in DTCs. We expect the impact to be limited in respect of active operating group companies of multinational groups. The new rules are likely to impact (passive) intra-group financing, leasing and licensing structures and, in particular if an LOB rule will be introduced without a specific provision on funds, private equity fund and other fund structures.

9.9 Transfer Pricing Changes

Currently, the Netherlands applies the OECD Transfer Pricing Guidelines also to transactions involving intangibles, including hard-to-value intangibles and special contractual relationships such as a cost contribution agreement. The Netherlands endorses the amendments to the guidelines as set out in BEPS Action 8. These amendments put more emphasis on the characterisation of transactions and the allocation of profits from intangibles based on a functional analysis and are in line with the already existing views of the Dutch State Secretary of Finance.

9.10 Transparency and Country by Country Reporting

Further to BEPS Action 13, OECD members are recommended to extend their transfer pricing documentation requirements and implement country-by-country reporting rules. As part of its 2016 tax bill, the Netherlands proposed to implement country-by-country reporting (CbCr) requirements in accordance with BEPS Action 13. These CbCr requirements apply as of 1 January 2016 and are aimed at companies which are resident in the Netherlands for Dutch corporate income tax purposes and are part of a multinational enterprise which has a consolidated turnover exceeding certain thresholds. In addition, the Dutch government has requested the European Commission to further investigate the possibility of implementing public CbCr requirements for all multinational enterprises.

The Dutch government attaches similar importance to transparency and the spontaneous exchange of information regarding ATRs, including those on preferential tax regimes, permanent establishments and holding company regimes. At the level of both the OECD and the European Union, the Netherlands supports the development of standards and adoption of measures to increase transparency and to better enable other jurisdictions in applying their domestic tax rules.

9.11 BEPS Process

Although the exact form and timing of quite some BEPS measures are still uncertain, it is clear that BEPS already has its impact on corporate tax planning. On the short term, in particular, the efforts of the EU to accelerate parts of the BEPS projects in an EU context and unilaterally and potentially uncoordinated BEPS inspired actions by countries around the world should be closely monitored.