The Netherlands proposes changes to dividend withholding tax

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The Dutch government has released an attractive proposal to fully exempt withholding tax on dividends paid to non-resident shareholders in treaty countries provided certain conditions are met. Many multinational enterprises should be able to benefit from this exemption. In addition, the proposal brings certain Dutch cooperatives into the scope of the Dutch dividend withholding tax rules.

On May 16, 2017, the Dutch government released a public consultation for the previously announced legislative proposals. The Dutch government intends to have the new changes to the Dutch Dividend Withholding Tax Act (DWTA) enter into force on January 1, 2018.

Expansion of full dividend withholding tax exemption

The Dutch government proposes to expand the withholding tax exemption for dividends distributed by Dutch companies where their non-resident shareholder is an entity that:

1. holds an interest of at least 5 percent in the Dutch company and
2. resides (for tax treaty purposes) in a jurisdiction that has concluded a tax treaty including a dividend clause with the Netherlands.
In addition, a new anti-abuse rule will be introduced in the DWTA, according to which the exemption will not apply if:

1. the interest is held with the principal purpose, or one of the principal purposes, of avoiding dividend withholding tax from being levied and
2. the interest is part of an artificial structure or transaction or series of transactions, which will be the case if there is no valid business reasons.

The anti-abuse provision is in line with the general anti-abuse provision in the EU Parent-Subsidiary Directive (EU PSD). The proposed rules further clarify that there are valid business reasons in the situation where the non-resident shareholder carries out a business to which the interest can be attributed. There are also valid business reasons if the non-resident shareholder functions as an intermediate holding company (for an indirect shareholder that carries out a business), that meets the relevant substance requirements set out in the Dutch rules in the country of establishment. The current substance requirements, which have already taken effect from January 1, 2016, will be expanded with two further requirements. Under the amended rules, non-resident shareholders that function as intermediate holding companies must, among other things, have:

1. a payroll expense of at least €100,000 related to the intermediate holding activities and
2. premises at their disposal (for a period of at least 24 months) in the country of establishment from which they actually carry out their intermediate holding activities.

Examples – how will the proposed rules apply?

The next examples illustrate some possibilities for multinational companies to benefit from the proposed expansion of the dividend withholding tax exemption.

**Example 1: Restructuring Canadian investments in Europe**

Under the proposed rules, Canadian investments into Europe could be structured via the Netherlands to allow dividends to be repatriated tax-free to Canadian shareholders.

Under the structure illustrated in Figure 1, dividends distributed by the EU company should be exempt under the EU PSD assuming certain conditions are fulfilled. Dividends received and future capital gains should be fully exempt from Dutch corporate income tax (CIT). Under the new proposal, dividends distributed by the Dutch company to the Canadian company should in principle be exempt of Dutch dividend withholding tax because Canada has a qualifying tax treaty with the Netherlands, which includes a dividend clause, and provided that the Canadian company conducts a material business enterprise or fulfills, as an intermediate holding company (that meets all the relevant substance conditions), a linking function between the indirect shareholder that conducts a material business enterprise and the Dutch company.
Similar benefits are available for shareholders residing in one of the approximately 100 countries with which the Netherlands concluded a tax treaty.

**Example 2: Bypassing the United States – Netherlands tax treaty LOB requirements**

Figure 2 illustrates an example where the proposed exemption from withholding tax is useful for US shareholders. The tax treaty between the Netherlands and the US provides for an exemption from dividend withholding tax in the Netherlands but, assume for purposes of this example, the US company does not qualify for treaty benefits under the LOB provisions.

Figure 2

Dividend distributions from the Mexican company to the Dutch company should under certain conditions be exempt from dividend withholding tax. Dividends received and future capital gains should be fully exempt from Dutch CIT. Dividends distributed by the Dutch company to the US company should, in principle, be exempt under the expanded Dutch withholding tax exemption provided that the conditions for the proposed exemption are met. This should be the case for US tax resident companies conducting a material business because the US has concluded a tax treaty with the Netherlands which includes the requisite dividend clause. The LOB provision and the 12-month holding requirement in the tax treaty between the US and the Netherlands should be no longer relevant, as the dividend withholding tax exemption applies under domestic law.

**New withholding tax obligation for Dutch “holding cooperatives”**

The Dutch government has previously announced that it wants to bring the treatment of Dutch cooperatives more in line with the treatment of Dutch NVs and BVs. In order to achieve this objective the Dutch government has proposed changes to bring certain Dutch cooperatives into the scope of the Dutch dividend withholding tax rules if both of the below conditions are met:

1. the cooperative is a “holding cooperative” – *i.e.*, its actual activities in the year preceding the profit distribution consisted primarily (*i.e.*, for 70 percent or more) of the holding of participations or the direct or indirect financing of related entities or individuals and
2. the members of the cooperative have “qualifying membership rights” – *i.e.*, membership rights that grant an entitlement of at least 5 percent of the annual profits or at least 5 percent of the liquidation profits. In assessing whether there is a qualifying membership right, the membership rights of a member and the entities and individuals related to that member will be taken into account.

Non-holding or “real” cooperatives (cooperatives running a business enterprise and/or with a large group of members) will remain exempt from dividend withholding tax.

Companies that currently operate a Dutch cooperative in the Netherlands should carefully review the potential impact of...
these proposed new rules to their structure. It is expected that private equity and similar structures could be particularly affected by these proposed rules. The draft explanatory notes state that, under some circumstances, it is conceivable that a cooperative used in private equity structures would not qualify as a “holding cooperative.” This could be the case because of factors such as the number of employees, office premises, and the active involvement of employees in the underlying business of the participation held by the cooperative.

Timing

The public consultation is expected to be completed on June 13, 2017 and the final bill will be presented on or around Budget Day (September 19, 2017). The intention of the Dutch government is to have the new changes to the DWTA enter into force on January 1, 2018.

Comments

The proposed rules provide for more flexibility for multinationals doing business in or through the Netherlands to facilitate dividend repatriation free of dividend withholding tax. The Dutch government expects that multinational enterprises will benefit from the expansion of the dividend withholding exemption for a total of €30 million per year.

More importantly, together with the existing withholding tax exemption for interest and royalties, this change is expected to further strengthen the Netherlands as an attractive holding company location offering additional flexibility in terms of repatriating profits in a post-BEPS environment.

The proposed rules are particularly interesting for companies that wish to make foreign investments in or through the Netherlands for example, in the European Union. In the latter, income derived by Dutch companies from other European subsidiaries should benefit from European Directives and dividends received and capital gains should benefit from the participation exemption under Dutch domestic law. Furthermore, the dividend withholding tax exemption applies to many investors into the Netherlands without having to meet some of the stringent conditions under tax treaties, such as the LOB requirements in the treaty between the US and the Netherlands, or remit income to a domestic bank account.

Contact any of the authors to find out more about the implications of this development.

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