Navigating Changes for Dutch Holding Companies

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Every year on the third Tuesday of September, Budget Day occurs in the Netherlands. This core political and governmental ceremony includes public release of the 2022 budget and fiscal policy statements. A day earlier Swedish 2022 budget plans were announced. For Turkish investors with Dutch or Swedish holding, financing, and operating companies, both budget announcements are relevant. The Dutch are also about to adopt mandatory rules for gender diversity on board of directors and senior management of BV’s and NV’s.

In spring 2020, Swedish regulators issued a plan to adjust the dividend withholding tax rules by January 2023. Last Tuesday, in their budget an announcement was made to delay changes to January 1st, 2024. From a policy point of view, it still seems dividends paid by Swedish companies to recipients outside the European Economic Area would no longer automatically benefit from exemption of dividend withholding tax.

In the Netherlands, a series of changes are also in the air for intermediary holding BV’s. Dividends paid by Dutch BV’s to low taxed entities become taxable by 2024. Furthermore, new rules governing substance and gender diversity for intermediary holding BV’s are expected as early as 2022. Meanwhile a (remote) possibility of a Dutch exit tax by 2024 looms over any entity reorganization plan one may have.

In the Netherlands, the political and regulators agenda is about making its fiscal regime less attractive for “pass-through” BV’s. One might say, Sweden, like so many other nations, may adopt a similar agenda. After all, since the OECD started the BEPS Project in 2008 combatting “substance-less” international tax avoidance became a norm. True and therefore, one must assess with a wide angle the tax value-risk profile Dutch or Swedish holdings bring on.

In case Sweden eliminates its dividend withholding tax exemption, the base rate of 30% would apply to dividends paid to beneficiaries outside the European Economic Area (the EEA). This rate would be limited to the maximum rate allowed under an applicable tax treaty. For Turkish private individual shareholders, it would be 20%, like in the Dutch treaty. For Turkish corporate shareholders, the rate would basically become a steep 15%. As we will see later on, these changes are not as bad as they may seem at first glance.
For Turkish investors, in comparing Dutch and Swedish holding companies it is worth noting the difference in approach by the Dutch and Swedish governments under the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent BEPS (the MLI). The Netherlands has left the method for avoidance of double taxation to its treaty partners. Sweden has taken the stance that its tax treaties insofar as avoidance of double taxation can only be changed by bi-lateral renegotiation. This essential difference is paramount when considering where Turkey seems to be heading.

Under the MLI, Turkey may very well adopt the credit method. If such choice be ratified with the OECD, the Belgian and Dutch tax treaties with Turkey would change. The Swedish one would not. Dividends from Belgian and Dutch companies to Turkish shareholders would no longer be tax exempt. Rather those incomes would be fully taxable with a credit for the foreign taxes paid. For individuals, this change means a 40% taxation on such dividends under credit of the 20% withholding tax. Swedish intermediary holdings would, however, keep the overall tax rate at 20%, making such holdings a clear choice for private investors.

For Turkish parent companies the change means full corporate income taxation on the dividends because current Turkish domestic participation exemption rules do not exempt Dutch or Belgian dividends from corporate income taxation. Why? because such dividends do not carry at least 15% taxation. As far as we know, changes to these rules are not on the agenda of Turkish Government.

Therefore, looking ahead, as near as 2023, it is possible dividends from Dutch or Belgian holdings declared and paid to Turkish Holdings become fully taxed at the main corporate income tax rate. Such change brings tax free dividends to fully taxed dividends and would disrupt cash flows within Turkish Parent – International Subsidiary relations. Restructuring of international holding structures under such taxation regime could of course become prohibitively expensive.

Let us assume Sweden changes its dividend withholding tax regime to effectively charge 15% on dividends to Turkish parent companies. Such dividends would, by Turkish domestic law, be exempt under participation exemption. Based on the Dutch-Turkish tax treaty, dividends will never reach the minimum 15% taxation as required for Turkish participation exemption.

Future taxation for Turkish Parent Companies of Dutch dividends is dependent on i) how and when Turkey implements the MLI and ii) if, and if so when, Turkey changes its domestic participation exemption requirement of at least 15% actual taxation on the dividend. These uncertainties and their timing can be compared with the certainties a Swedish holding would bring.

This summer the Dutch State Secretary of Finance send a letter to the Parliament indicating a cross functional team of government bodies, regulators, tax police had conducted a search for illegal fiduciary activities. This search has identified thousands addresses and people potentially involved with illegal holding company related fiduciary activities. Likely some of those leads point to “substance less” holdings.

Moreover, in the latest Dutch budget it was announced the government is still working on actively reducing the number of substance-less intermediary holding BV’s. It is possible
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substance requirements would be introduced for intermediary holding companies that apply the participation exemption to dividends from foreign subsidiaries. Later this year rules may be introduced allowing a tax inspector who deems a holding BV not to have enough substance to exchange of information with the dividend/interest/royalty paying states. Effectively 2022, this measure could be introduced through amendment of an existing Decree.

Looking at regulatory guidance regarding substance requirements for holding and financing BV’s, we can find minimum standards. These standards are not haven rules. To comply with the essence of Dutch corporate income tax rules and regulations, one must look at who is doing what exactly from the Netherlands. Are most BV board members actually located in the Netherlands? Do they have genuine and sufficient legal authority and group management structure mandate to conduct holding BV’s business? Do the board members in fact take care of executing the board decisions, together with their staff? Does BV have the basics in place; main bank account in the Netherlands, at least 2 years office lease, adequate administrative and bookkeeping functionality?

For financing companies, it is relevant how much equity is deployed and how much actual financial risk is incurred. Looking at the history of Dutch regulators guidance on intermediary holding companies, it can be said such companies need to demonstrate a link function between a foreign parent and BV’s subsidiaries. To demonstrate a relevant link function, one needs to look at the seize of the investments owned, the complexity of the business, the seniority and actual involvement of Dutch based statutory directors, their staff and the financial risks incurred.

Even though Swedish Holdings owned by Turkish Parent Companies may go from 0% to 15% dividend withholding tax, overall Swedish holdings are still an alternative to Dutch Holdings to be considered.

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<th>NL current</th>
<th>NL possible future</th>
<th>SWE current</th>
<th>SWE possible future</th>
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On September 28th, a bill was adopted in Dutch Parliament to enforce gender diversity in management and supervisory boards of Dutch entities. Possibly effective by 2022, with mandated reporting to the Social Economic Council, in scope are entities listed on the Euronext Amsterdam stock exchange. Those entities are legally required to have certain female representation on their boards.

Also, in scope are unlisted larger seize NV’s and BV’s meeting at least two of the following criteria: 1) Value of Assets exceeds Euro 20 million, 2) Turnover exceeds Euro 40 million per annum and 3) Average Headcount exceeds 250 staff members on annual basis. These entities, which may very well include intermediary holding companies, are required to establish ambitious targets for female representation at board and sub-board levels.

What may these rules mean for intermediary holdings? It may mean tax inspectors will have another angle to evaluate the true and genuine economic and business substance of such holdings. Remember, intermediary Dutch holdings are required to perform a link function, bridging the foreign shareholder to the operating subsidiaries, to benefit from participation exemption. To assess if the bridge function is met, one looks at all facts and circumstances, including, we would say, compliance with gender diversity rules.

Currently, Dutch and Swedish Holdings render similar financial outcomes for Turkish investors. However, as time passes and new regulations are introduced, Swedish holdings may become (much) more advantageous than Dutch ones.

The total tax charge on Swedish holdings appears predictable over a five-year horizon. Swedish substance requirements are less prescriptive than Dutch ones and potentially cheaper to adhere to. For Dutch holdings, in the mid-term their total taxation for Turkish investors cannot be predicted due to i) uncertainties in the Turkish legislative agenda, ii) operational risks from a Dutch tax inspector informing dividend, interest and royalty paying nations and iii) introduction of substance and gender diversity requirements by 2022.

From the angle of restructuring, it is worthwhile considering the Netherlands may eventually introduce an exit taxation by 2024. Time has come to assess intermediary holding structures and devise tax strategies.

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To navigate in this landscape of many moving parts we would be happy to assist.