



# Taxation of cross-border mergers and acquisitions

**The Netherlands**

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# The Netherlands

## Introduction

The Dutch tax environment for cross-border mergers and acquisitions (M&A) has undergone some fundamental changes in recent years. Most of these changes have been implemented as of 2013.

These changes affect fundamental decisions that a prospective purchaser will face:

- What should be acquired: the target's shares, or its assets?
- What will be the acquisition vehicle?
- How should the acquisition vehicle be financed?

## Recent developments

The following summary of recent Dutch tax developments is based on current tax legislation up to and including the Tax Plan 2016, which was announced in September 2015 and took effect as of 1 January 2016.

### Implementation amendments to the EU Parent-Subsidiary Directive

On 1 January 2016, the provisions for the implementation of the amendments to the European Union (EU) Parent-Subsidiary Directive entered into force. The amendments include an anti-hybrid provision and a common minimum general anti-avoidance rule (EU GAAR). These amendments were included in three existing Dutch rules: the Dutch participation exemption, the Dutch non-resident taxation rules and the anti-abuse rules for distributions made by cooperatives. The new rules apply not only to EU situations; they are global in scope.

The anti-hybrid provision has been included in the Dutch participation exemption. As of 1 January 2016 the Dutch participation exemption does not apply to payments received from or made by the participation insofar as the participation can deduct these for profit tax purposes (a hybrid mismatch). The participation exemption therefore no longer applies if a shareholder, for example, receives a dividend that is deductible by the participation. Benefits derived from the disposal of the participation and foreign exchange results remain exempt in principle, given that they are non-deductible at the level of the participation.

The EU GAAR has been included in the Dutch non-resident taxation rules and the anti-abuse rules for distributions made by cooperatives. Under the non-resident taxation rules, foreign entities with a substantial interest (broadly, an interest of at least 5 percent) in a Dutch resident company are subject to Dutch corporate income tax on capital gains and dividends in respect of such substantial interest where:

- the primary objective, or one of the primary objectives, for holding the substantial interest is to evade personal income tax or dividend withholding tax (WHT) (at another level), and
- an artificial arrangement is involved.

Similar rules apply to distributions made by a Dutch cooperative. In principle, distributions by a cooperative are not subject to Dutch dividend WHT (the current statutory rate is 15 percent), unless similar tests are met.

Arrangements or series of arrangements are regarded as artificial to the extent they are not put in place for valid commercial reasons that reflect economic reality. Based on the parliamentary history, valid commercial reasons are present where:

- the shareholder/member of the Dutch company has an operational business enterprise to which the interest in the Dutch company can be allocated
- the shareholder/member is a top holding company that provides strategic management to the group, or
- the shareholder/member is an intermediate holding company and has sufficient substance according to Dutch standards.

With respect to the specific anti-abuse rule for cooperatives contained in the Dutch Dividend Withholding Tax Act, the explanatory notes to the proposed rules state that the anti-abuse rule will not apply to Dutch cooperatives that conduct a business enterprise. Typical elements of a business enterprise are that it employs its own staff and has office space, but this depends on the specific facts and circumstances.

### Fiscal unity with EU/EEA parent or intermediate company

Due to the Dutch residence requirement and the fact that, under current law, an indirect shareholding is only sufficient if the intermediate/linking company is also part of the fiscal unity, it is not possible to form a fiscal unity between a Dutch

company and its Dutch sub-subsidiary if the linking company is resident in a foreign country. Under current law, it also is not possible to form a fiscal unity between two Dutch sister companies that are held by a parent company resident in a foreign country since the parent company is not a Dutch resident (and it is not possible to form a fiscal unity between the two sister companies alone). However, in June 2014, the Court of Justice of the European Union (CJEU) ruled that these restrictions are contrary to EU law where the foreign country concerned is an EU member state.

To comply with this judgement, the Minister of Finance issued a policy statement in December 2014, in which he gave approval (subject to certain conditions) for a fiscal unity of Dutch sister companies of a parent company resident in the EU or European Economic Area (EEA) and for a fiscal unity between a Dutch parent company and Dutch sub-subsidiaries held through one or more EU/EEA-resident intermediate holding companies.

In October 2015, a bill was presented to codify this policy statement. The bill provides more details on the amended regime, including several anti-abuse rules. It also facilitates the inclusion of Dutch permanent establishments of EU/EEA-resident companies in a fiscal unity, even where the permanent establishment functions as a parent company and the shares held in its Dutch subsidiary/subsidiaries are not attributable to the permanent establishment.

### **Temporal ring-fencing participation exemption**

On 1 May 2015, the temporal ring-fencing rules entered into force with retroactive effect to 14 June 2013. These rules deal with situations where the participation exemption does not apply to the entire period that the shareholding has been held. In the past, Supreme Court case law on temporal ring-fencing dealt with situations where the participation exemption became applicable or no longer applied to an existing shareholding (exemption transition) as a result of a change in the facts. In short, case law on temporal ring-fencing meant that the tax treatment of capital gains realized after such a change was determined on the basis of the tax regime applicable during the shareholding period to which the benefit could be attributed.

According to the new legislation, temporal ring-fencing must take place either when there is a transition in qualification for the participation exemption as a result of a change in the facts or when legislation is amended, both in relation to dividends and capital gains. The bill has replaced existing Supreme Court case law and applies to all types of exemption transitions in respect of a shareholding. While the legislation has retroactive effect to 14 June 2013, its substantive retroactive effect dates back even further and the benefits of the participation exemption received in the distant past may as yet be reclaimed.

## **Asset purchase or share purchase**

Generally, from a seller's perspective, a sale of assets is likely to generate a taxable gain or loss unless tax relief applies or the gain can be deferred by creating a reinvestment reserve. This reserve operates by way of a rollover, so that the gain on the sale of one business asset can be used to reduce the tax basis of another business asset or assets. The relief is subject to various conditions, including a 3-year reinvestment period and, in some cases, the type of new asset.

Where shares or assets are acquired from an associated party at a price that is not at arm's length, a deemed dividend distribution or capital contribution may result.

Capital gains realized on the sale of shares qualifying for the participation exemption are tax-exempt. For details, see this report's section on purchase of shares.

### **Purchase of assets**

When a Dutch company acquires assets, the assets are reported in the acquiring company's financial statements in accordance with generally accepted accounting principles (GAAP).

Any financing costs relating to the acquisition of assets are generally deductible on an accruals basis for Dutch corporate income tax purposes. See, however, the restrictions discussed in the section on choice of acquisition funding later in this report.

The transfer of Dutch real estate may be subject to transfer tax at a rate of 6 percent.

Generally, any resulting gain (sometimes referred to as tax on hidden, i.e. untaxed, reserves) on the sale or other transfer of assets by a Dutch-resident company (or a non-resident company that holds the assets through a Dutch permanent establishment) is subject to Dutch corporate income tax, unless the transaction qualifies for relief as an asset merger, legal merger or demerger (division). Corporate reorganizations involving simple transfers of assets and liabilities between companies forming a fiscal unity for corporate income tax purposes are generally tax-exempt, as are transfers of any other assets or liabilities within a fiscal unity. See group relief/consolidation.

An asset merger essentially involves the transfer of a business (or independent part thereof) by one company to another company in exchange for the issue of new shares to the transferor. The relief consists of an exemption from tax for the transferor and a rollover of the transferor's existing tax basis in the transferred assets and liabilities to the acquiring company, effectively deferring any gain.

In principle, the relief is not restricted to resident companies or companies incorporated under Dutch law. In practice,

the involvement of non-resident companies does have implications (described later).

The relief applies automatically where certain conditions are met (e.g. ensuring that avoidance opportunities are not present). In other cases, the relief must be specifically requested and may be granted subject to additional conditions. The relief does not apply if the merger is primarily aimed at the avoidance or deferral of taxation. Advance certainty (in the form of an advance tax ruling) can be obtained from the Dutch revenue.

Generally, the transferor's pre-merger losses may not be transferred to the acquiring company, and the acquiring company's post-merger losses may not be carried back to be set off against the transferor's profits. However, an exception to this rule, subject to conditions and a request being filed, is made where a Dutch permanent establishment is converted into a private limited liability company (*Besloten Vennootschap* — BV) or public limited liability company (*Naamloze Vennootschap* — NV) by way of an asset merger.

In a legal merger, the assets and liabilities of one or more companies are transferred to another new or existing company, and the transferor(s) then cease(s) to exist. As a rule, the acquiring company issues new shares to the shareholder(s) in the transferor(s) in exchange for the transfer.

The tax relief available for a legal merger consists of an exemption from tax for the transferor and a rollover of the transferor's existing tax basis in the transferred assets and liabilities, as well as fiscal reserves, to the acquiring company, effectively deferring any gain. A legal merger may involve non-Dutch companies, subject to conditions. Generally, the tax relief is not restricted to resident companies but also applies to companies resident in the EU. A Dutch NV can also merge with similar entities from other EU member states to form a new *societas Europaea* (SE).

A similar procedure to that of asset mergers is available for obtaining the relief and advance certainty. The transferor's pre-merger losses may be transferred to the acquiring company, and the acquiring company's post-merger losses may be carried back to be set off against the transferor's profits, provided a request is filed and applicable conditions are satisfied.

There are two basic forms of demerger (division) under Dutch civil law. The first generally results in the division of a company's business between two or more acquiring companies, with the transferor ceasing to exist (pure demerger). The second involves a transfer of all or part of a company's business to one or more new or existing companies, but the company continues to exist (split-off). In both cases, new shares are issued in exchange for the transfer. Typically, the acquiring company issues the new

shares to the shareholders in the transferor. The tax relief applies in the same way as for legal mergers. A similar procedure to that of asset mergers is available for obtaining the relief and advanced certainty.

For a pure demerger, pre-demerger losses can be carried forward and post-demerger losses carried back, as is the case for legal mergers. However, for a legal merger, a request must be filed with the Dutch tax authorities. For a split-off, losses may only be transferred to the acquiring entity subject to certain conditions, including that the demerging entity ceases to be a taxpayer in the Netherlands. The tax losses available for carry forward and carry back then remain available at the level of the company that continues to exist.

For a legal merger and legal demerger involving an acquisition company that has been debt-funded, the interest deduction limitation rule applies in the same way as for acquisition holding companies that have been included in fiscal unities. See choice of acquisition funding.

### **Purchase price**

Acquisition prices from affiliated parties may be challenged under transfer pricing rules. There are no particular rules for allocating the purchase price between the assets acquired, other than using the fair market value for each of the assets acquired.

### **Goodwill**

Goodwill is reported in the acquiring company's financial statements for financial reporting and tax purposes as the difference between the value of the acquired assets and the price paid. The maximum annual amortization of goodwill for tax purposes is 10 percent of the acquisition or development costs.

### **Depreciation**

Depreciation is available on the acquired assets that are necessary for carrying on the business, provided that their value diminishes over time. Maximum annual amortization and depreciation percentages apply to goodwill (10 percent) and business assets other than goodwill and real estate (20 percent).

Depreciation of real estate is possible until a residual value is reached. For investment properties, the minimum residual value equals the value established by the municipality under the Valuation of Immovable Property Act (WOZ). For properties used as part of one's own business (such as the business premises), the residual value is half the value determined under the WOZ. Under the new depreciation system, it continues to be possible to record impairment to buildings at a lower going-concern value.

Accelerated amortization/depreciation is possible in respect of qualifying environmental assets.

## Tax attributes

Tax losses are not transferred on an asset acquisition. They remain with the company. However, an exception to this rule is made in the case of qualifying mergers or divisions, or when a Dutch permanent establishment is converted into a BV or an NV by way of an asset merger or split-off. In the latter cases, where the transferor is no longer subject to Dutch tax after the transaction, a request may be submitted to allow a carry forward or carry back of losses, subject to the losses being offset against the profits attributable to the assets that generated the losses. The transfer of assets within a fiscal unity does not generally affect tax attributes, so the transfer does not, for example, result in taxable gains. A clawback may apply where the fiscal unity is dissolved within a 6-year period following such a transfer.

## Value added tax

Value added tax (VAT) is the most important indirect tax in the Netherlands.

Dutch VAT is levied on the net invoiced amount charged by businesses for supplies of goods and services taxable within the Netherlands. Businesses are only allowed to reclaim the input VAT on their investments and costs attributable to:

- activities subject to VAT
- VAT-exempt financial services rendered to non-EU persons and to non-EU permanent establishments.

Input VAT can only be recovered where the business is the actual recipient of the services and a correct invoice is issued to this business.

No VAT is due when all or an independent part of a company's business is transferred and the transferred business continues as before (also known as transfer of a business as going concern). These transactions are out of scope for VAT purposes. This relief also applies to legal mergers but not to the sale of single assets or trading stock (e.g. inventory).

Where the acquirer in a merger or share acquisition transaction wishes to reclaim VAT on the transaction costs, the acquirer should always ensure it has activities subject to VAT or provides VAT-exempt financial services to non-EU parties. The post-deal VAT recovery position depends largely on the facts and circumstances of the proposed structure.

## Transfer taxes

A real estate transfer tax at the rate of 6 percent (2 percent on homes) of the real estate value (which must equal at least the purchase price) is due on all transfers of titles to Dutch real estate. This tax also applies to shares in Dutch real estate companies, provided the acquirer holds at least one-third of the economic interest in the real estate company. A company

is considered to be a real estate company if the assets (at fair market value) consist of more than 50 percent real estate. Real estate located outside the Netherlands is included, provided the assets consist of at least 30 percent real estate located in the Netherlands (asset test). If the asset test is met, then the actual activities must be assessed to determine whether at least 70 percent of these activities involve the exploitation of this real estate (e.g. investment).

The transferee is liable for the tax, but the contract may stipulate that the transferor will bear the expense.

## Purchase of shares

Shares in a company generally are acquired through a purchase or exchange of shares. In principle, the acquisition of shares is capitalized in the acquiring company's financial statements.

In practice, shares that are held as a shareholding qualifying for the participation exemption (discussed later) are carried at cost for tax purposes; this is only relevant for specific purposes, given that a disposal of such a shareholding is tax-exempt. Costs directly related to such acquisitions are generally non-deductible. Costs related to obtaining debt-financing may be deducted if and to the extent that interest on acquisition loans is tax-deductible.

Shares held as a portfolio investment are generally carried at cost or market value, whichever is lower. Specific regulations apply to a participation of 25 percent or more in a low-taxed investment company (i.e. generally, 90 percent or more of its assets comprise passive investments and are subject to tax at a rate lower than 10 percent).

Where shares in a Dutch target are acquired in exchange for new shares issued by a Dutch company, as in a share-for-share exchange, the new shares are only treated as paid-up to the same extent that the target's shares were paid-up. In effect, the potential dividend WHT that would have been due on profit distributions by the target is shifted to the acquiring company, as and when it distributes profits. To mitigate the impact of this rule, concessionary treatment applies when a Dutch company acquires a foreign target.

In certain circumstances, a change in ownership of shares in a Dutch company may result in the company losing its right to carry forward losses (discussed later).

Where the price the purchaser pays for the shares is higher than the book value of the underlying assets of the acquired company, the basis of the company's underlying assets may not be stepped up to the price paid for the shares and the excess cannot be treated as payment for amortizable goodwill.

The acquisition or transfer of shares is exempt from VAT. An important issue is often the extent to which a business is entitled to reclaim the Dutch VAT levied on its transaction costs for the sale of shares of a subsidiary (generally not taxed for VAT purposes) to an EU-based purchaser. VAT levied on the costs attributable to an asset transaction and a statutory merger generally can be recovered by the seller on a pro rata basis. Under a special decree for majority shareholdings, the VAT on costs attributable to their sale is fully reclaimable.

The transfer of shares in a company owning real estate may be subject to transfer tax at a rate of 6 percent. A company is considered to be a real estate company where its assets (at fair market value) consist of more than 50 percent real estate. Real estate located outside the Netherlands is included, provided that the assets consist of at least 30 percent real estate located in the Netherlands (asset test). Where the asset test is met, then the actual activities must be assessed to determine whether at least 70 percent of these activities involve the exploitation of this real estate (e.g. investment).

The acquisition of shares is not subject to capital contribution tax, other indirect taxes or local or state taxes.

The sale of a shareholding that qualifies for the participation exemption (as described later) is exempt from tax. A loss is accordingly non-deductible. Costs directly relating to the sale of a qualifying participation are also non-deductible.

In principle, the participation exemption applies to shareholdings in Dutch or non-Dutch companies of at least 5 percent unless the subsidiary can be considered to be held as a passive investment (motive test). A subsidiary is considered to be held as a passive investment if the taxpayer's objective is to generate a return that may be expected from normal active asset management. Where more than 50 percent of the subsidiary's assets comprise shareholdings in companies representing an interest of less than 5 percent or where the subsidiary's main function is to provide group financing, such subsidiary is also considered to be held as a passive investment.

A subsidiary that is considered as a passive investment may still qualify for the participation exemption where one of two conditions are met:

- Less than 50 percent of the fair market value of the assets (on a special consolidated basis) comprise non-business-related, low-taxed investments (asset test).
- The company is taxed at a reasonable tax rate (10 percent or more) based on Dutch tax principles (subject to tax test).

Generally, assets held by subsidiaries are taken into account for the asset test. The relevant entity's activities determine whether an asset qualifies as a non-business-related investment, which is an investment that cannot reasonably be considered necessary for the business operations of the entity holding these investments. The question of whether investments qualify as non-business-related should be answered case-by-case.

Due to the implementation of the EU Parent-Subsidiary Directive, the Dutch participation exemption has been amended. As of 1 January 2016, the Dutch participation exemption does not apply to payments received from or made by the participation insofar as the participation can deduct them for profit tax purposes (a hybrid mismatch). The participation exemption therefore no longer applies if a shareholder, for example, receives a dividend and this dividend is deductible by the participation. Benefits derived from the disposal of the participation and foreign exchange results remain exempt in principle, given that they are non-deductible at the level of the participation.

On 1 May 2015, the temporal ring-fencing rules entered into force with retroactive effect to 14 June 2013. These rules deal with situations where the participation exemption does not apply to the entire period that the shareholding has been held. In the past, Supreme Court case law on temporal ring-fencing dealt with situations where the participation exemption became applicable or no longer applied to an existing shareholding (exemption transition) as a result of a change in the facts. In short, case law on temporal ring-fencing meant that the tax treatment of capital gains realized after such a change was determined on the basis of the tax regime applicable during the shareholding period to which the benefit could be attributed.

According to the legislation, temporal ring-fencing must take place either when there is a transition in qualification for the participation exemption as a result of a change in the facts or when legislation is amended, both in relation to dividends and capital gains. The bill will replace existing Supreme Court case law and applies to all types of exemption transitions in respect of a shareholding. The legislation has retroactive effect to 14 June 2013. Its substantive retroactive effect dates back even further, and the benefits of the participation exemption received in the distant past may as yet be reclaimed.

#### **Tax indemnities and warranties**

In a share acquisition, the purchaser takes over the target company together with all related liabilities, including contingent liabilities. Therefore, the purchaser normally requires more extensive indemnities and warranties than in the case of an asset acquisition.

## Tax losses

Generally, tax losses may be carried forward for 9 years and carried back for 1 year within the same company or fiscal unity. However, the carryover may be restricted or denied in circumstances involving a change of 30 percent or more in the ownership of the company where the company has primarily held passive investments during the years concerned or its business activities have significantly decreased. The carry forward of prior-year losses by a holding and finance company may also be restricted, as may the carry back of losses. According to legislation, a company is a holding and finance company where 90 percent or more of its activities, for 90 percent or more of the financial year, comprise holding participations and/or the financing of affiliated companies. The losses incurred by such companies may only be set off against profits where the company also qualifies as a holding and finance company in the profitable year and where the net amount of affiliated loan receivables is not greater in the profitable year or if the net amount is greater, then this was not primarily done to take advantage of the loss set-off.

The existing rules for setting off losses within a fiscal unity are extensive, but the normal time limits for such set-off still apply. Generally, pre-fiscal unity losses can be set off only where the fiscal unity as a whole has a profit for tax purposes after setting off the results of the various fiscal unity companies. Thereafter, the total result of the fiscal unity is divided into the parts attributable to the participating companies in the fiscal unity. If the individual participating company still shows a profit, only the pre-fiscal unity losses of that company may be set off against that profit. The same procedure is followed for carrying back the loss incurred by a fiscal unity company to be set off against its pre-fiscal unity profits. Other specific rules apply to the treatment of losses and foreign tax credits after a fiscal unity is dissolved or when a company leaves a fiscal unity.

## Crystallization of tax charges

A tax charge does not arise on a share transfer if the transfer qualifies as a share-for-share merger. This essentially involves an exchange of shares in the target company for shares in the acquiring company. The relief consists of an exemption from tax for the transferor and a rollover of the transferor's existing tax basis in the target shares into consideration shares in the acquiring company, effectively deferring any gain.

This relief is available where:

- A company resident in the Netherlands:
  - acquires, in exchange for the issue of shares in its own capital (or profit rights), shares in another company resident in the Netherlands
  - can exercise more than 50 percent of the voting rights in the latter company after the acquisition.
- A company resident in an EU member state:
  - acquires, in exchange for the issue of shares in its own capital (or profit rights), shares in a qualifying company resident in another EU member state
  - can exercise more than 50 percent of the voting rights in the latter company after the acquisition.
- A company resident in the Netherlands:
  - acquires, in exchange for the issue of shares in its own capital (or profit rights), shares in a company resident outside the EU
  - can exercise at least 90 percent of the voting rights in the latter company after the acquisition.

A cash element of up to 10 percent of the nominal value of the shares issued under the share-for-share merger is permitted (but the relief is limited to the share element). Relief is not available where the transaction is primarily aimed at avoiding or deferring taxation. Unless the taxpayer can demonstrate otherwise, this motive is presumed where the transaction does not take place for sound business reasons, such as a restructuring or rationalization of the activities of the companies involved. Before carrying out the transaction, the taxpayer can request confirmation from the Dutch tax authorities that it will not deny relief on these grounds.

For corporate taxpayers, the importance of the share merger facility is limited by the broad scope of the participation exemption. Moreover, although the share-for-share merger facility also applies for personal income tax purposes where Dutch individual shareholders are involved, the importance of the facility generally is limited to those owning at least 5 percent of the target (i.e. holders of substantial interests), as gains on smaller shareholdings are not usually taxable.

The disposal outside a fiscal unity (see group relief/consolidation) of a subsidiary that has been involved in the transfer of assets within the fiscal unity in the preceding 6 years may give rise to a tax liability from the previously transferred assets. The transferred assets are revalued at market value prior to the fiscal unity being terminated. An exception is made where the transfer of the assets is part of the normal businesses of both companies.

Once a company has left a fiscal unity, it remains jointly and severally liable for taxes payable by the parent company of the fiscal unity (both corporate income tax and VAT fiscal unity) and allocable to the tax periods in which the company was included in the fiscal unity. This liability arises pursuant to the Dutch Tax Collection Act and should be addressed in the sale-purchase agreement.

### **Pre-sale dividend**

The participation exemption applies to a pre-sale dividend, provided it meets the applicable conditions and the seller is a Dutch resident. Where the seller is non-resident, the relevant treaty or the applicable domestic type of relief determines whether the Netherlands will withhold tax on the paid dividend.

### **Transfer taxes**

A 6 percent real estate transfer tax is due on all share transfers in Dutch real estate companies. A company is considered to be a real estate company if its assets (at fair market value) consist of more than 50 percent real estate. Real estate located outside the Netherlands is included, provided that the assets consist of at least 30 percent real estate located in the Netherlands (asset test). If the asset test is met, then the actual activities should be assessed to determine whether at least 70 percent of the activities involve the exploitation of this real estate (e.g. investment).

### **Tax clearances**

See the discussion of share mergers earlier in this report.

## **Choice of acquisition vehicle**

Several potential acquisition vehicles are available to a foreign purchaser for acquiring the shares or assets of a Dutch target. Tax factors often influence the choice of vehicle.

### **Local holding company**

Dutch tax law and the Dutch Civil Code contain no specific rules on holding companies. In principle, all resident companies can benefit from the participation exemption if they satisfy the relevant conditions (see purchase of shares). Under the participation exemption, capital gains and dividends from qualifying shareholdings are exempt from corporate income tax. However, legislation limits the possibility of setting off losses that are incurred by holding and finance companies against profits (again, see the section purchase of shares).

In principle, therefore, an acquirer already active in the Netherlands through a subsidiary or branch could have that entity make a qualifying share acquisition. In practice, a special-purpose company is often incorporated in the Netherlands for the purposes of such acquisitions. The main types of Dutch corporate entities are the BV, the NV and the Dutch cooperative.

For Dutch tax purposes, there are no material differences between the types of entities, except that Dutch cooperatives generally are not subject to Dutch dividend WHT, which makes them particularly attractive for foreign inbound investments by non-treaty residents and/or private equity-type funds. Dividend distributions made by cooperatives are not subject

to dividend WHT unless it appears that the primary objective or one of the primary objectives for using the cooperative is to evade dividend WHT or foreign tax at a different level, and this involves an artificial arrangement.

Arrangements or series of arrangements are regarded as artificial to the extent they are not put in place for valid commercial reasons that reflect economic reality. Based on parliamentary history, valid commercial reasons are present where:

- the shareholder/member of the Dutch company has an operational business enterprise to which the interest in the Dutch company can be allocated
- the shareholder/member is a top holding company that provides strategic management to the group
- the shareholder/member is an intermediate holding company and has sufficient substance according to Dutch standards, or
- the Dutch cooperative conducts a business enterprise.

Typical elements of a business enterprise are that it employs its own staff and has office space, but this depends on the specific facts and circumstances.

In principle, funding costs, such as interest incurred by a local holding company, can be deducted from the taxable profit of the acquiring company. Restrictions apply for the deduction of interest from the taxable profit of the target if a fiscal unity is formed. See the section on choice of acquisition funding earlier in this report.

### **Foreign parent company**

The foreign purchaser may choose to make the acquisition itself. As a non-resident without a Dutch permanent establishment, the foreign purchaser is not normally exposed to Dutch taxation in respect of the shareholding, except for possible WHT on dividends, or if the non-resident taxation rules (as further described under recent developments) would apply. Dutch WHT on dividends is 15 percent unless reduced by a treaty or a domestic exemption applies. Dividends to foreign EU-based corporate shareholders holding at least 5 percent of the shares normally qualify for an exemption from WHT.

### **Non-resident intermediate holding company**

Due to the Netherlands' extensive network of tax treaties, there is often no benefit to interposing a treaty country intermediary. However, where the acquirer is resident in a non-treaty country, the dividend WHT may be reduced by interposing a Dutch cooperative (in principle, not subject to dividend WHT; see this report's section on local holding company) or a foreign holding company resident in a treaty country between the acquirer and the target company.

## Local branch

A branch of a foreign company is subject to Dutch corporate income tax in the same way as a domestic company. In principle, non-resident entities that have Dutch permanent establishments to which qualifying shareholdings can be attributed can benefit from the participation exemption. In principle, funding costs, such as interest incurred by a local branch, can be deducted in computing the taxable profits of the target if a fiscal unity can be formed after the acquisition (see group relief/consolidation later in this report). No WHT is levied on distributions to the foreign head office, which can be an advantage when acquiring a Dutch target's assets. If the deal is properly structured, using a branch to acquire shares in a Dutch target also offers the possibility of distributing profits free from WHT. A negative commercial aspect of using a branch is that the branch may not be considered a separate legal entity, fully exposing the head office to the branch's liabilities. Additionally, the Dutch tax authorities generally deny a deduction for interest charged by the head office unless the deduction relates to external loans.

## Joint venture

Joint ventures can be either incorporated (with the joint venture partners holding shares in a Dutch company) or unincorporated (usually a limited partnership). A partnership may be considered transparent for Dutch tax purposes, if certain conditions are met. In this case, the partnership's losses can be offset against the partners' profits. However, selling the business may lead to taxable profit at the level of the partners. Due to the participation exemption, where the conditions are met, the profit or loss on the sale of the shares of a tax-transparent partnership do not lead to taxable profit.

## Choice of acquisition funding

### Debt

Interest expenses are generally deductible on an accruals basis for Dutch corporate income tax purposes. This also applies to interest relating to a participation to which the participation exemption applies, irrespective of whether the shareholding is in a resident or non-resident company, unless a specific restriction on the deductibility of interest applies.

### Deductibility of interest

Specific restrictions on deducting interest expenses (including costs and foreign exchange results) apply for interest paid to affiliated companies and individuals where the loan is used for the acquisition of shares in companies that, after the acquisition, become affiliated with the acquirer as a consequence of such acquisition. Certain guarantees by affiliated companies and individuals may qualify a third-party loan as a loan by these affiliated companies or individuals.

These restrictions do not apply where the taxpayer shows that both the transaction and the related debt were predominately motivated by sound business reasons (double business motivation test) or where the recipient of the interest (or, for a conduit company, the ultimate recipient) is subject to effective taxation at a rate that is considered reasonable according to Dutch standards (generally, 10 percent or more, computed under Dutch corporate income tax principles). In the latter case, the restrictions still apply where the Dutch tax authorities can show that the transaction and the related debt were not both predominately motivated by sound business reasons.

In a decree issued in March 2013, the Deputy Minister of Finance presented his views on, for example, financing structures that he considers are not business-motivated. Loans used to finance an acquisition that are funded by the issuance of a hybrid financing instrument are potentially not business-motivated. Other mismatches resulting from the use of hybrid entities are also mentioned. The facts and circumstances at hand could still provide a good basis for arguing that the interest on such loans should be tax-deductible.

Interest on a loan between affiliated entities that has no defined term or a term exceeding 10 years and carries a return of less than 70 percent of an arm's length return is not deductible.

As of 1 January 2013, an interest deduction limitation rule applies to excessive deduction of interest related to the financing of participations (participation debt). The non-deductible amount of interest is calculated by dividing the excessive amount of participation debt by the total amount of debt and multiplying this by the total amount of interest paid. The excessive participation debt is calculated as the value of the participations for tax purposes (historic cost price and capital contributions) less the total amount of equity for tax purposes. An exemption is provided for expansion investments, that is, investments in participations that expand a group's operating activities. The acquisition price of these participations does not have to be taken into account in calculating disallowed interest. The exemption does not apply where, for example, a double dip structure or a hybrid entity/instrument was used to finance these participations.

Generally, no disallowed interest should arise on the basis of the excessive participation debt rules where:

- The amount of equity for tax purposes exceeds the acquisition price of the participations.
- The Dutch taxpayer has included all its participations in the fiscal unity for corporate income tax purposes (not possible for foreign participations).

- The participations of the taxpayer were all historically incorporated or acquired as an expansion of a group's operating activities, no double dip structures or hybrid entity/financing structures were implemented, and the acquisition, expansion and financing were not entered into because of the interest deduction.
- The excessive amount of 'participation debt' is less than 15 million euros (EUR) (assuming an interest rate of 5 percent), due to a safe harbor amount of EUR750,000. This amount of interest is always deductible under these rules.

The deduction limitation applies to financial years starting on or after 1 January 2013. Transitional rules allow for an optional fixed amount: the taxpayer may disregard 90 percent of the acquisition price (i.e. to the extent considered as an expansion investment), without further proof, where the participation was acquired or expanded or equity was contributed to the participation during a financial year starting on or before 1 January 2006. The taxpayer must prove that, in relation to the old participations to which the 90 percent rule has been applied, no double dip structures or hybrid entity/financing structures were implemented.

The participation interest measure includes a concession for active group financing activities. Under this concession, the test for determining whether there is a participation debt and non-deductible participation interest does not take into account loans and their accompanying interest and costs to the extent that these loans relate to receivables held by the taxpayer in respect of the active group financing activities.

There is an implementation decree for internal reorganizations that is intended to avoid overkill as a result of other statutory restrictions of interest deduction.

Further, an interest deduction limitation rule applies to acquisition holding companies that are debt financed where the acquirer and the target enter into a fiscal unity for corporate income tax purposes. This restriction only applies for fiscal unities formed after 15 November 2011. Under this restriction, acquisition debts exist where the debt is related directly or indirectly, by law or by fact, to the acquisition or expansion of a participation in one or more companies.

Interest expenses on the acquisition debt are deductible up to the amount of the acquirer's own profit before deducting the acquisition interest expenses (own profit). Where the acquisition interest exceeds the own profit and the excess amount is less than EUR1 million (franchise), then the new rule does not limit the interest deduction. Where there is no excess acquisition interest (financing escape), the interest also remains fully deductible (subject to other possible limitations).

The excess acquisition interest equals the interest on the acquisition debt that exceeds a specific part of the acquisition price: 60 percent in the year in which the acquisition was included in the fiscal unity, 55 percent in the following year and so on, until a percentage of 25 percent is reached. In the case of multiple acquisition debts, particularly where they relate to companies included in the fiscal unity in different years, the excess acquisition interest must be determined for each of those years separately. Acquisition debts and acquisition prices regarding acquisitions that are included in a fiscal unity in the same year are combined.

If there is excess acquisition interest as described earlier, the non-deductible interest is limited to the lower of the following two amounts:

- acquisition interest less positive own profit minus EUR1 million
- the amount of the excess acquisition interest.

Acquisition interest that is non-deductible in any year is carried over to the following year, where it will again be assessed to see if it falls under the interest deduction limitation. In respect of the interest carried forward, the EUR1 million franchise and the financing escape are not taken into account again.

Corresponding measures apply where the target does not join the fiscal unity but a legal merger or a legal division takes place on or after 15 November 2011. Mergers and divisions that took place before 15 November 2011 are also subject to the transitional rules.

#### **Withholding tax on debt and methods to reduce or eliminate it**

WHT of 15 percent is levied on dividend distributions. No WHT is levied on interest (except for interest paid on hybrid loans, as described later), royalty payments or transfers of branch profits to a foreign head office. In the absence of WHT on interest, it is often advantageous to fund a Dutch company with debt rather than equity. See, however, the restrictions on interest deduction for profit tax purposes discussed in this report's section on choice of acquisition funding.

(For the dividend WHT implications of share-for-share acquisitions, see the section on purchase of shares.)

#### **Checklist for debt funding**

- The deduction of interest may be restricted, especially where the acquisition of shares is financed with an intercompany loan.
- If the target owns subsidiaries (which are not part of the same fiscal unity), the deduction of interest may be restricted in case of excessive deduction of interest related to the financing of participations.

- If the level of the purchaser's profits is not sufficient, an effective deductibility of the interest could be achieved by forming a fiscal unity within the limitations provided by the rules on acquisition holding companies described earlier.

## Equity

A purchaser may use equity to fund its acquisition, possibly by issuing shares to the seller in satisfaction of the consideration (share merger). Contributions to the capital of a Dutch company are not subject to capital contribution tax.

## Hybrids

According to Dutch case law, a loan may be re-qualified as equity for corporate income tax purposes in the following situations:

- The parties actually intended equity to be provided (rather than a loan).
- The conditions of the loan are such that the lender effectively participates in the business of the borrowing company.
- The loan was granted under such circumstances (e.g. relating to the debtor's financial position) that, at the time the loan was granted, neither full nor partial repayment of the loan could be expected.

Pursuant to Dutch case law, loans referred to under the second bullet point above may be re-characterized as equity where:

- The term of the loan is at least 50 years.
- The debt is subordinated to all ordinary creditors.
- The remuneration is almost fully dependent on the profit.

Where a loan is re-characterized as equity under the above conditions, interest payments are non-deductible and may be deemed to be a dividend distribution, triggering 15 percent WHT (unless reduced by treaty or domestic relief).

## Discounted securities

Where securities are issued at a discount, because the interest rate is below the market rate of interest, in principle, the issuer may be able to obtain a tax deduction for the discount accruing over the life of the security.

## Deferred settlement

Payments pursuant to earn-out clauses that result in additional payments or refunds of the purchase price are covered by the participation exemption applicable to the relevant participations.

Similarly, the participation exemption covers payments related to indemnities or warranties to the extent that they are to be qualified as an adjustment of the purchase price.

Where settlement of a purchase price is deferred, part of the purchase price may be re-characterized as interest for tax purposes, depending on the agreed terms and the parties' intent.

## Other considerations

### The seller's concerns

No corporate income tax is due on share transfers, provided the conditions of the participation exemption are met. Relief from corporate income tax may be granted on a share-for-share merger, asset merger, legal merger and demerger. Where available, relief generally takes the form of an exemption for the transferor and a rollover, such that the acquired assets and liabilities retain the same tax basis they had when owned by the transferor. Certain conditions for this rollover must be met. For example, where the shares are sold within a certain period after an asset merger, the granted exemption can be revoked.

The disposal outside a fiscal unity of a subsidiary that has been involved in the transfer of assets within the fiscal unity in the preceding 6 years may give rise to a tax liability with respect to the previously transferred assets. The transferred assets are revalued at market value prior to the fiscal unity being terminated. An exception is made where the transfer of the assets is part of the normal businesses of both companies.

### Company law and accounting

Under Dutch law, a company may operate in the Netherlands through an incorporated or unincorporated entity or a branch. All legal entities have to register their business with the trade registry (*Handelsregister*) at the local Chamber of Commerce (*Kamer van Koophandel*).

The most common forms of incorporated companies under Dutch commercial law are the BV and the NV. Both are legal entities and have capital stock divided into shares. As of October 2012, it is possible to issue shares without voting rights or profit entitlement. Shares of a BV are not freely transferable, which makes this type of company generally preferred as the vehicle for privately held companies. Generally, shares in an NV are freely transferable.

Foreign investment in a Dutch company does not normally require government consent. However, certain laws and regulatory rules may apply to mergers or acquisitions. In a stock merger, the shareholders of the target company either exchange their shares for those of the acquiring company or sell them to the acquiring company. The transfer of title to registered shares is made by a deed of transfer executed before a Dutch civil-law notary.

In a business merger, an enterprise is transferred to the acquiring company for cash and/or shares in the company. Such a transfer requires that all assets and liabilities be transferred separately.

In a statutory/legal merger, shareholders generally exchange their shares in the target company for those of the other (acquiring) company (or a new company); the target company is then dissolved. In addition to this basic form of statutory/legal merger, a number of variations exist, such as a merger between a parent and a subsidiary and a triangular merger under which a member of the acquiring company's group may issue the consideration shares.

Legislation on divisions and demergers/split-offs has been in force since 1998. Participants in mergers must adhere to the requirements of the Dutch takeover and merger code (*SER Fusiegedragsregels*), which protects the interests of shareholders and employees, and the Works Councils Act (*Wet op de Ondernemingsraden*), which protects the interests of employees and requires notification of mergers. Mergers of large companies that qualify as concentrations within the meaning of the Dutch Competition act must be notified to the Dutch authority for Consumers & Markets in advance.

Legislation for financial reporting is laid down in Part 9 of Book 2 of the Dutch Civil Code. Further, the Council of Annual Reporting (CAR — *Raad voor de Jaarverslaggeving*) publishes Guidelines for Annual Reporting (GAR), which is largely based on International Financial Reporting Standards (IFRS).

The financial reporting rules contain requirements about the content, analysis, classification, recognition and valuation of items in the financial statements. The statutory management of a NV or BV must prepare the financial statements within a period of 5 months. This period can be extended for up to 5 more months, with approval from the shareholders and when special circumstances apply.

### **Group relief/consolidation**

A fiscal unity can be formed between a parent company and any companies in which it owns 95 percent of the legal and economic ownership of the nominal share capital. This 95 percent interest should represent at least 95 percent of the voting rights and should be entitled to at least 95 percent of the profits.

The parent and subsidiaries must be formed under Dutch law (usually as BVs, NVs or cooperatives); if they are formed under foreign law, their legal form must be comparable to a BV, NV or a cooperative. A company does not actually have to be resident in the Netherlands. Where the company is not a Dutch resident, it should have a permanent establishment in the Netherlands and be resident in either an EU member

state or a country with a tax treaty with the Netherlands that prohibits discrimination against such a company. If the Dutch permanent establishment is the parent company of a fiscal unity, the shares in the respective subsidiaries should be attributable to the permanent establishment. A number of conditions need to be fulfilled, including identical financial years for both parent and subsidiaries. For newly incorporated companies, the commencement of the first financial year may deviate. A fiscal unity may be deemed to have been formed on the date requested, but the formation date cannot be more than 3 months before the date of the request.

Inclusion in a fiscal unity means that, for tax purposes, the assets and activities of the subsidiaries are attributed to the parent company, in effect producing a kind of tax consolidation. The main advantage of a fiscal unity is that the losses of one company can be set off against the profits of another in the year they arise. However, interest expense incurred in relation to the acquired company is only deductible from the profit of the parent company where the rules on acquisition holding companies described earlier permit (see also choice of acquisition funding).

In addition, assets and liabilities generally can be transferred from one company to another without giving rise to tax consequences. Specific rules apply to combat the abuse of fiscal unities. In particular, the disposal outside a fiscal unity of a subsidiary that has been engaged in the transfer of assets within the fiscal unity in the preceding 6 years may give rise to a tax liability with respect to the previously transferred assets.

To ensure proper assessment and collection of tax, the Ministry of Finance has laid down a number of special conditions, in particular, extensive rules restricting a taxpayer's ability to carry forward pre-fiscal unity losses to be set off against post-fiscal unity profits and to carry back post-fiscal unity losses to be set off against pre-fiscal unity profits.

Due to the Dutch residence requirement and the fact that, under current law, an indirect shareholding is only sufficient if the intermediate/linking company is also part of the fiscal unity, it is not possible to form a fiscal unity between a Dutch company and its Dutch sub-subsidiary if the linking company is resident in a foreign country. Furthermore, under current law, it is not possible to form a fiscal unity between two Dutch sister companies that are held by a parent company resident in a foreign country since the parent company is not a Dutch resident (and it is not possible to form a fiscal unity between the two sister companies alone). However, in June 2014, the CJEU ruled that these restrictions are contrary to EU law where the foreign country concerned is an EU member state.

To comply with this judgment, the Minister of Finance issued a policy statement in December 2014, in which he

gave approval (subject to certain conditions) for a fiscal unity of Dutch sister companies of an EU/EEA-resident parent company and for a fiscal unity between a Dutch parent company and Dutch sub-subsidiaries held through one or more EU/EEA-resident intermediate holding companies.

In October 2015, a bill was presented to codify this policy statement. The bill provides more details on the amended regime, including several anti-abuse rules. It also facilitates the inclusion of Dutch permanent establishments of EU/EEA-resident companies in a fiscal unity, even where the permanent establishment functions as a parent company and the shares held in its Dutch subsidiary/subsidiaries are not attributable to the permanent establishment. At the date of preparing this report, the draft bill had not yet been enacted into law.

### **Transfer pricing**

In principle, intercompany transactions should be at arm's length for tax purposes. To provide evidence that transfer prices are at arm's length, a taxpayer must submit proper transfer pricing documentation to the Dutch tax authorities. If the Dutch tax authorities impose revised assessments, absence of such evidence may shift the burden of proof to the taxpayer (i.e. should the taxpayer wish to argue that a reasonable estimation made by the Dutch tax authorities is wrong). Penalties may also be imposed. Transfer pricing adjustments may entail secondary adjustments, such as hidden dividend distributions or capital contributions.

New transfer pricing documentation rules entered into force as of 1 January 2016. Companies that are part of a group with a minimum consolidated turnover of EUR750 million must notify the Dutch tax authorities by 31 December 2016 as to which group company will file a country-by-country (CbyC) report. If the fiscal year of the group starts on 1 January 2016, the group companies will need to have filed their CbyC report by 31 December 2017. Penalties will be imposed in instances of intentional non-compliance or 'serious misconduct' of the reporting entity regarding its obligation to file the CbyC report. The penalty amounts to a maximum of EUR20,250, and criminal prosecution is possible.

Furthermore, all group entities that are tax-resident in the Netherlands and that are part of a group with a minimum consolidated turnover of EUR50 million need to maintain a master file and local file in their administration at the

time of filing their tax return. Non-compliance with these documentation requirements would result in a reversal of the burden of proof.

### **Information obligation for service entities**

In light of the national and international debate on the taxation of multinationals and developments regarding base erosion and profit shifting (BEPS), the Cabinet introduced a measure that concerns the information obligation for service entities.

In short, 'service entities' are Dutch resident companies whose main activities involve the intragroup receipt and payment of foreign interest, royalties and rental or lease payments. A service entity can request the Dutch tax authorities to provide advance certainty on the tax consequences of proposed related-party transactions. The conditions for obtaining advance certainty are laid down in a 2004 decree. In short, these conditions provide for an actual presence in the Netherlands (i.e. substance requirements) and the real risks that must be borne as a result of the functions performed. The substance rules require, for example, that the management and administration be carried out in the Netherlands and that the amount of equity held is appropriate to the company's functions and risks.

As of 1 January 2014, these substance requirements apply to service entities, regardless of whether advance certainty was requested. They therefore apply to all service entities, which must also confirm, at the latest in their annual corporate income tax return, whether they meet these requirements.

### **Dual residency**

In principle, a company that has been incorporated under Dutch civil law is subject to Dutch tax, regardless of whether it is also resident in another country. In certain circumstances, a Dutch company that is resident under a tax treaty in another country may be deemed non-resident for Dutch tax purposes or it may be denied certain types of relief (such as being able to join a fiscal unity).

### **Foreign investments of a local target company**

In principle, similar rules regarding the availability of the participation exemption apply to both Dutch and non-Dutch subsidiaries. However, special rules apply to low-taxed, passive investment companies. See this report's section on purchase of shares.

## Comparison of asset and share purchases

### Advantages of asset purchases

- All or part of the purchase price can be depreciated or amortized for tax purposes.
- A step-up in the cost basis for taxing subsequent gains is obtained.
- Generally, no previous liabilities of the company are inherited.
- No acquisition of a tax liability on retained earnings.
- Permits flexibility to acquire only part of a business.
- Greater flexibility in funding options.
- Profitable operations can be absorbed by loss-making companies in the acquirer's group, thereby effectively increasing the ability to use the losses.

### Disadvantages of asset purchases

- Possible need to renegotiate supply, employment and technology agreements.
- A higher capital outlay is usually involved (unless a business' debts are also assumed).
- May be unattractive to the seller, thereby increasing the price.
- Higher real estate transfer tax.
- Seller retains the benefit of any losses incurred by the target company.

### Advantages of share purchases

- Lower capital outlay (purchase of net assets only).
- Likely more attractive to the seller, so the price is likely lower.
- May benefit from tax losses of target company.
- Lower real estate transfer tax.
- May benefit from the seller's ability to apply the participation exemption.

### Disadvantages of share purchases

- No depreciation of purchase price.
- No step-up for taxing subsequent capital gains.
- Liable for any claims against or previous liabilities of the entity.
- No deduction for purchase price.
- Purchaser inherits a potential dividend WHT liability on retained earnings that are ultimately distributed to shareholders.
- Less flexibility in funding options.

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