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## Substance requirements for Dutch companies



### Background

The Netherlands offers a solid combination of a stable economy, a reliable tax regime and a sophisticated, internationally oriented infrastructure. In addition, the Dutch economy is noted for its stable industrial relations and plays an important role as a European logistic hub. The Government strongly supports that the legal and economic environment remains attractive for multinational companies. The Netherlands' strategic location is ideal for locating (regional) headquarters, warehouse facilities, R&D centres and other group services functions.

In order to strengthen its position in the international tax context the Government has taken some proactive measures vis à vis the abuse of Dutch financial services companies (FSCs). Existing substance rules have been codified as of 1 January 2014. In addition to this on 4 November 2016, the State Secretary of Finance has sent a letter to Parliament discussing the possibilities for the future treatment of FSCs in light of the OECD Base Erosion and Profit Shifting (BEPS) action plans. In essence the Government is of the opinion that the current substance rules are up to standard and that the international focus should be directed on enhancing source countries to effectively combat treaty abuse.

### The position of the Dutch Government and existing substance rules for FSCs

The Government keeps emphasizing the importance of maintaining an attractive tax climate to guarantee its key position for international investments. It will not alter the most important elements of the Dutch tax regime, such as the tax treaty network, the possibility to obtain advance tax rulings and the participation exemption. In addition the Government favours a coordinated and international approach for addressing the issues of international tax planning and to combat tax avoidance and is

therefore actively supporting the above-mentioned BEPS action plans. The Government believes that solutions should be binding for all states, safeguarding a level playing field between states and companies. Decisions in this respect should be taken at a supranational e.g. OECD and/or EU level.

In order to avoid the improper use of Dutch companies, a set of rules has been developed which contains certain minimum substance requirements. These rules have been in place now for more than 10 years for FSCs that apply for a ruling. If FSCs do not meet one or more of the minimum substance requirements (non-compliant FSC), no ruling can be obtained. Please note that the Dutch authorities can in that event also spontaneously exchange information to the authorities of the other country on the activities of an FSC. Depending on the response of the tax authorities of the other country, treaty benefits claimed in the past may be reversed, possibly leading to an additional tax liability.

## ○ Substance requirements

The substance rules apply to all FSCs whether applying for a ruling or not. The FSC is obliged to report whether it meets the substance requirements on an annual basis in the corporate income tax return. If an FSC does not meet the substance requirements, the FSC must on its own initiative inform the Dutch tax authorities which specific requirements it does not meet and provide them with all substance related information as well as an overview of all interest, royalty and similar payments for which a reduction of (withholding) tax has been or could have been claimed under any tax treaty or the rules of the European Interest & Royalty Directive as implemented in Dutch tax law. This information will be exchanged spontaneously to the source country by the Dutch tax authorities.

The substance requirements are met when a company established in the Netherlands meets all of the following conditions mentioned below:

- At least half of the directors of the company should be resident of the Netherlands.
- The Dutch resident directors should have the professional knowledge and skills to properly perform their duties. These duties at least include the decision making process regarding the company's transactions and follow-up.
- The company will have adequate support to run its business.
- The (most important) board decisions of the company are made in the Netherlands.
- The principal bank account of the company is maintained from the Netherlands.
- The bookkeeping of the company must take place in the Netherlands.
- The business address of the company is in the Netherlands.
- The company must comply with all its tax obligations in the Netherlands and is not treated as a tax resident of another country.
- The company runs a real risk with respect to its financing, licensing or leasing activities. The company has an equity at risk that corresponds to the functions performed.

## Holding companies

The Dutch tax authorities will only consider ruling requests of holding companies (ATR and/or APA) to the extent such a company has sufficient nexus with the Netherlands. The nexus requirements will be fulfilled if the aforementioned substance requirements are met. In addition holding companies should finance the acquisition of their participations with at least 15% equity. Under circumstances the same may be required from a foreign intermediate company investing in a Dutch holding.

## Conclusion

The Dutch substance requirements are up to standard and the Dutch tax authorities are actively checking whether FSCs meet these requirements. Non-compliant FSCs run the risk that the Dutch tax authorities will spontaneously exchange information to the source country. In view of the international developments like the BEPS project, we recommend Dutch FSCs to make sure that the substance requirements are met and to regularly check whether the company is still compliant in this respect.

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