

December 2009

## TAX NEWS BULLETIN: Dutch Ministry of Finance gives up its plans for group interest box regime and certain restrictions on interest deduction.

- **Dutch Ministry of Finance gives up its plans for group interest box regime**  
*(Read more....)*
  
- **Introduction of an interest deduction disallowance provision for acquisition holding companies**  
*The State Secretary of Finance announces the introduction of an interest deduction disallowance provision for acquisition holding companies. In the Consultation document, this provision was proposed in combination with a second interest deduction disallowance provision, relating to debts incurred for financing the acquisition of participations. (Read more...)*
  
- **Repeal of the deductibility of foreign permanent establishment losses**  
*Profits of permanent establishments (p.e.'s) are exempt from Dutch corporate income tax. Losses are deductible from the taxable basis of the Dutch head office, subject to a loss recapture (later profits are not exempted from Dutch corporate income tax until previously deducted losses have been recaptured). (Read more...)*

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## *DUTCH MINISTRY OF FINANCE GIVES UP ITS PLANS FOR GROUP INTEREST BOX REGIME AND CERTAIN RESTRICTIONS ON INTEREST DEDUCTION.*

On 15 June, 2009, the Dutch State Secretary of Finance issued the so called Consultation document. The Consultation document contained proposed amendments to the Dutch Corporate Income Tax Act ("DCITA"), most notably the introduction of the group interest box regime and of certain interest deduction disallowance provisions, and the improvement of the participation exemption regime<sup>1</sup> (for details on the Consultation document we refer to our newsletter of June 2009, [www.ohp.nl](http://www.ohp.nl)).

On 5 December 2009, the Dutch State Secretary of Finance sent a letter to Parliament. The letter was announced during the recent Parliamentary proceedings relating to the 2010 Budget Plan and was promised to explain the current status of the possible amendments to the Dutch Corporate Income Tax Act. The "possible amendments to the DCITA" refers to the amendments proposed in the earlier Consultation document. The Consultation document has resulted in many responses from tax practitioners. In his letter, the State Secretary of Finance takes into account these responses. The most remarkable and surprising element of his letter is the abandonment of the long expected group interest box regime.

The State Secretary of Finance renounces the group interest box regime, in spite of having received confirmation from the EC that the group interest box would not be considered state aid. The most important reason given is the negative impact of the regime (which would be mandatory) to foreign investors who have financed their Dutch operations with group loans (the interest on which would effectively be deductible at only 5%). In addition, the State Secretary notes, cash pooling activities would become so unattractive that they would likely be removed from the Netherlands.

The State Secretary of Finance states that the Study Group Fiscal System (which has been formed recently to investigate possibilities for fundamental improvements to the entire Dutch fiscal system) is exploring possibilities for more fundamental amendments to the DCITA. It is possible that the amendments to be proposed by the Study Group will achieve the objectives of the group interest box, while eliminating the objections against the group interest box. The amendments to be proposed by the Study Group, however, are not to be expected in the short term.

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<sup>1</sup> The improvements to the participation exemption regime have been transferred from the Consultation document to the 2010 Budget Plan and are expected to become effective as of 1 January 2010.



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## *INTRODUCTION OF AN INTEREST DEDUCTION DISALLOWANCE PROVISION FOR ACQUISITION HOLDING COMPANIES*

In short, in his letter of 5 December, 2009, the State Secretary of Finance announces the following measures to be included in a legislative proposal to amend the DCITA, which is expected to be published in the spring of 2010:

1. Introduction of an interest deduction disallowance provision for acquisition holding companies
2. Repeal of the deductibility of foreign permanent establishment losses

The State Secretary of Finance announces the introduction of an interest deduction disallowance provision for acquisition holding companies. In the Consultation document, this provision was proposed in combination with a second interest deduction disallowance provision, relating to debts incurred for financing the acquisition of participations. The State Secretary of Finance now indicates that for the time being he will neither propose the introduction of this second provision, nor the introduction of the earnings stripping provision (which was proposed in the Consultation document as an alternative to the first two interest deduction disallowance provisions). Only the interest deduction disallowance provision for acquisition holding companies remains. The reason given for abandoning the other provisions is the uncertainty as to whether they would be compliant with EU law. A negative aspect of the interest deduction disallowance provision for acquisition holding companies is the fact that it will also apply to interest paid by acquisition holding companies to unrelated creditors. Under current law, as well as under the provisions proposed in the Consultation document, interest paid to unrelated creditors is never disallowed.

A positive aspect is the fact that the so called “goodwill gap”<sup>2</sup> will be taken into account. The importance of the goodwill gap becomes apparent in the counter proof provision: the interest paid by acquisition holding companies is deductible if the average amount of debt does not exceed three times the average amount of equity of the acquisition holding company. The acquisition holding company therefore has an interest in showing a high average amount of equity. The 3:1 debt-to-equity ratio was mentioned in the Consultation document. It is not certain whether this same ratio will be followed in the expected legislative proposal. It also remains unclear in which manner the goodwill gap will be “taken into account” for the purposes of the interest deduction disallowance provision.



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<sup>2</sup> When a Dutch target company is acquired by a Dutch acquisition holding company (of a foreign investor) and is included in a fiscal unity with the acquisition holding company, the cost price of the shares of the target company is replaced by the assets and liabilities of the target company in the balance sheet of the acquisition holding company. The difference between the price paid for the shares in the target company and the net asset value of the target company (book value of the assets minus liabilities) is deducted from or added to the equity of the acquisition holding company. When the acquisition holding company has paid more for the shares in the target than the net asset value of the target (“goodwill”, the fair market value of the assets minus liabilities exceeds the book value of the assets minus liabilities), the equity of the acquisition holding company will be reduced correspondingly by the same amount (the “goodwill gap”)

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## *REPEAL OF THE DEDUCTIBILITY OF FOREIGN PERMANENT ESTABLISHMENT LOSSES*

Profits of permanent establishments (p.e.'s) are exempt from Dutch corporate income tax. Losses are deductible from the taxable basis of the Dutch head office, subject to a loss recapture (later profits are not exempted from Dutch corporate income tax until previously deducted losses have been recaptured). The State Secretary of Finance proposes to repeal the deductibility of p.e. losses, based on:

- the principle of territoriality,
- the supposed tax deferral possibilities for tax payers (e.g. the conversion of a p.e. to a participation once the p.e. turns profitable, while deferring dividend distributions after the conversion), and
- the supposed administrative burden related to the deduction of p.e. losses

So called “p.e. structures” or “branch structures”, which are particularly interesting to tax payers expanding their business across the border and expecting losses in the start up phase, would be expected to lose their appeal. Losses incurred upon ceasing the business of the p.e. will remain deductible (as liquidation losses of participations are also in principle deductible).

According to sources which have not yet been confirmed officially, the amendments proposed in the letter from the State Secretary of Finance will not have retroactive effect and will become effective on 1 January 2011.

Should you have any questions or require further information, please do not hesitate to contact one of the Tax Advisers mentioned below.

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