

## TAX NEWS BULLETIN: 2010 BUDGET PLAN

Recently, the Dutch Ministry of Finance presented the 2010 Budget to Parliament. On the same day, the Ministry of Finance presented a number of legislative proposals to Parliament.

This bulletin summarizes the following proposed measures which are most important from an international tax perspective:

### ➤ Improvement of the participation exemption regime

*Under the current participation exemption regime dividends derived from - and capital gains on the sale of - qualifying participations in Dutch or foreign companies are exempt, unless that company is a so called "low taxed passive investment company" ("LTPIC"). The concept of an "LTPIC" has proven to raise difficulties for taxpayers trying to support their position that the participation exemption applies. In addition, the volatility of both the value and composition of assets of a participation can lead to inconsistent conclusions being drawn from the asset test from year to year, resulting in uncertainty for the taxpayer. The aim of the proposed amendment is to eliminate the difficulties and uncertainty. (Read more.....)*

### ➤ Evolution of the "patent box" to a more generous "innovation box"

*Following the current legislative proposals, from 2010 the patent box will be renamed into "innovation box", the effective tax rate of the innovation box will be reduced to 5% and, very importantly, the maximum on the amount of income to be earned under the 5% rate will be abolished. (Read more.....)*

### ➤ Accelerated loss compensation for losses incurred in 2009 and 2010

*As a one-off tax benefit to alleviate the impact of the financial crisis, losses incurred in 2009 and 2010 may (at the request of the tax payer) be carried back to the three preceding years, in stead of the current one preceding year. (Read more.....)*

### ➤ Dividend withholding tax exemption to qualifying EEA (Norway, Iceland) shareholders

*Following two recent ECJ decisions, the exemption from Dutch dividend withholding tax act is extended to qualifying corporate shareholders in the EEA. (Read more.....)*

### ➤ Improvement of the tonnage tax regime

*Following an approval from the EC, the basis for determining the profit of large vessels (tonnage per day exceeding 50,000) is substantially reduced. Furthermore, the 2010 Budget Plan proposes to extend the tonnage tax regime to income from shipping services performed by cable and pipe laying vessels, research vessels and crane vessels. (Read more.....)*

## *IMPROVEMENT OF THE PARTICIPATION EXEMPTION REGIME*

Under the current participation exemption regime, the participation exemption applies to dividends derived from - and capital gains on the sale of - all qualifying participations in Dutch or foreign companies, unless that company is a so called “low taxed passive investment company” (“LTPIC”). A qualifying participation is a participation of at least 5% in the nominal issued and paid-up capital of a Dutch or foreign company with a capital divided into shares. A company is an LTPIC only if:

1. It's aggregated assets consist, for more than 50%, of “free passive investments”, measured by fair market value (“the asset test”),

and

2. It is not subject to a profits tax resulting in the levy at a rate of at least 10% over a taxable profit determined by Dutch standards (“the subject to tax test”),

and

3. It is not a real estate company (i.e. not a company the assets of which consist of real estate for 90% or more, measured by fair market value).

Dutch tax payers are entitled to an ordinary foreign tax credit in relation to LTPICs (in case of dividends from EU resident LTPICs the actual rate of tax to which the LTPIC is subject can be credited, in all other cases a deemed 5% credit applies).

The concept of an “LTPIC” has proven to raise difficulties for taxpayers trying to support their position that the participation exemption applies. In addition, the volatility of both the value and composition of assets can lead to inconsistent conclusions being drawn from the asset test from year to year, resulting in uncertainty for the taxpayer. The aim of the proposed amendment is to eliminate the difficulties and uncertainty.

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### *Motive test*

Under the proposed improvements, the subjective “motive test” (from the pre 2007 regime) is re-introduced as the main rule: if a qualifying participation is not held as a passive investment by the tax payer, the participation exemption applies. A qualifying participation is held as a passive investment if it is held for the purpose of earning a return on investment which can be expected from ordinary asset management. Only if the motive test can not be met, the taxpayer should support its position that a qualifying participation is not an LTPIC. According to the Memorandum of Explanation to the 2010 Budget plan, a qualifying participation is deemed not to be held as a passive investment if:

- the active business of the participation is in line with the active business of the tax payer,
- or
- the tax payer is an intermediary or top holding company which fulfills a real function for the benefit of the business of the group. A top holding company will be considered to fulfill a real function if it is actively involved in the management, policy making and/or financing of the group. An intermediary holding company will be considered to fulfill a real function if there is a connection between the business of the parent of the tax payer and the business of the participation(s), or if the parent company is a top holding company which fulfills a real function (involvement in management, policy making, financing) for the benefit of the group, and the tax payer holds a participation in a company with an active business. This also applies if the tax payer is not held immediately by the top holding company, but through another intermediary holding company.

If the tax payer is a venture capitalist (e.g. private equity fund or hedge fund) it will have to be determined whether the taxpayer itself has an active business. For this purpose it will have to be tested whether the activity of the taxpayer exceeds ordinary asset management. An important criterion is whether the venture capitalist is a member of the board of its participations and as such can exercise managerial, policy making, and financial influence. A participation in a group captive insurance company will, under certain circumstances, not qualify for the participation exemption if it is – de facto – engaged in passive investment.

#### Participations are deemed to be held as passive investments if:

- The participation’s assets consist, for more than 50%, of <5% participations, or
- The participation’s activity consists, alone or together with its direct or indirect >5% participations, for more than 50%, of group financing.

Participations which do not meet the motive test, or which are deemed to be held as passive investments, may still qualify for the participation exemption if they meet either the (amended) asset test or (amended) subject to tax test.

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### *Subject to tax test*

The amended subject to tax test effectively requires a general comparison of the profits tax regime of the country where the participation is established with the Dutch corporate income tax regime. The subject to tax test is met if:

- The statutory rate of the profits tax is at least 10% and there are no significant differences in tax base, or
- The statutory rate of the profits tax is at least 10% and there are significant differences in tax base but these do not result in an effective tax burden of less than 10%, or
- The statutory rate of the profits tax is less than 10% but it is probable that the effective tax burden is at least 10%.

Differences in e.g. asset depreciation or investment incentives, loss compensation, should not be considered significant differences. Neither should, in principle, differences in tax grouping regimes be considered significant differences. However, tax holidays, substantial deemed deductions or exemptions, or too generous participation exemptions will be considered significant differences.

### *Asset Test*

The asset test is met when the aggregated assets of the participation do not consist, for more than 50%, of *low taxed* free passive assets. The following assets are deemed not to be low taxed passive assets:

- Assets the income of which is subject to levy of profits tax which is considered “real” by Dutch standards (reference is made to the subject to tax test).
- Real estate (including rights which relate directly or indirectly to real estate).
- Low taxed passive assets which do not form more than 30% of the total assets of the participation owning the low taxed passive assets.
- Group receivables or receivables from providing assets intragroup, provided that the participation owning such receivables meets the strict conditions for “active group financing companies” or provided such receivables have been externally financed (legally and in substance) for at least 90%.

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## *EVOLUTION OF THE “PATENT BOX” TO A MORE GENEROUS “INNOVATION BOX”*

From 2007, Dutch tax payers can elect to have income generated from self developed patented assets included in the so called patent box taxed effectively at 10%, after the development costs have been recovered. The conditions for the patent box regime were considered rather restrictive, as a result of which very few tax payers elected to apply the patent box regime. Therefore, as from 2008, the scope of the patent box was extended to also include income from assets created by qualifying research and development activities (e.g. computer software). Furthermore, as from 2009 losses incurred from qualifying R&D assets can be offset against the statutory rate of 25.5% (rather than against the reduced rate). However, such losses will be considered development costs which will first have to be recovered before the reduced rate will be applied to income from qualifying assets. Following the current legislative proposals, from 2010 the patent box will be renamed into “innovation box”, the effective tax rate of the innovation box will be reduced to 5% and, very importantly, the maximum on the amount of income to be earned under the 5% rate will be abolished.

## *ACCELERATED LOSS COMPENSATION FOR LOSSES INCURRED IN 2009 AND 2010*

As a one-off tax benefit to alleviate the impact of the financial crisis, losses incurred in 2009 and 2010 may (at the request of the tax payer) be carried back to the three preceding years, in stead of the current one preceding year. However, the carry back of losses to the second and third preceding year is capped at a maximum of EUR 10 million in each of these years. In exchange for the accelerated loss compensation, the loss carry forward period will be reduced from nine years to six years.

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## *DIVIDEND WITHHOLDING TAX EXEMPTION TO QUALIFYING EEA SHAREHOLDERS*

Following two recent ECJ decisions, the Dutch dividend withholding tax act is amended as follows.

The exemption from withholding dividend tax in relation to shareholdings of 5% or more in Dutch companies will apply to Norwegian and Icelandic companies (not to Liechtenstein, for lack of an exchange of information agreement between Liechtenstein and the Netherlands). Norwegian and Icelandic qualifying tax exempt entities (e.g. pension plans) which are comparable to Dutch tax exempt entities, are eligible for a refund of Dutch withholding tax. The exemption and refund do not apply to Norwegian and Icelandic entities which are comparable to the Dutch fiscal investment company ("FBI") and exempt investment company ("VBI"). And finally:

1. the foreign shareholder is no longer required to have a legal form as mentioned in the annex to the Parent-Subsidiary directive,  
  
and
2. the foreign shareholder is no longer required to be subject – without choice or exemption - to a profits tax as mentioned in the directive.

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## IMPROVEMENT OF THE TONNAGE TAX REGIME

Following an approval from the EC, the basis for determining the profit of large vessels is substantially reduced: vessels with a tonnage per day exceeding 50,000 net tonnes will be set at only EUR 0.50 per day per 1000 net tonnes in excess of such 50,000 net tonnes (the lowest rate used to be EUR 2.27 per day per 1000 net tonnes in excess of 25,000 net tonnes). This measure has become effective with retroactive effect, from 1 January 2009, but must be reevaluated by the EC after 10 years.

The 2010 Budget Plan proposed to extend the tonnage tax regime to income from *shipping* services performed by cable and pipe laying vessels, research vessels and crane vessels. The enactment of the proposed amendments is subject to approval from the EC. If the approval is obtained after 1 January 2010, the amendments will become effective with retroactive effect from 1 January 2010 if such retroactive effect is allowed by the EC.

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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