

Tax Alert: expansion of the substance requirements for Dutch resident financial service companies

Oct. 13, 2020

Introduction

Effective as of 2014, The Netherlands applies by means of a decree (*Uitvoeringsbesluit internationale bijstandsverlening bij de heffing van belastingen*, hereinafter: the Decree) certain minimum substance requirements for so-called financial service companies - i.e. Dutch group financing companies, which are deemed to be predominantly engaged in intra-group financing, lending and/or licensing activities. On 28 November 2019, the Dutch State Secretary of Finance stated that the minimum substance requirements will be expanded in an amendment to the Decree, which has been reaffirmed in the Tax Plan Package 2021 on 15 September 2020.

Insofar these measures are not met, the following may ensue:

- spontaneous exchange of information to foreign tax authorities;
- disallowance of tax treaty benefits;
- a penalty being imposed up to a maximum EUR 21,750 (2020) in case of wilful intent or gross negligence (if not reported correctly).

Furthermore, these substance criteria are also of importance for:

- obtaining a Dutch tax residency certificate;
- compliance with anti-abuse measures in the Dutch dividend withholding tax act and Dutch corporate income tax Act;
- Obtaining an APA/ATR, although *economic nexus* has replaced the current substance requirements in this regard.

Current relevant substance requirements

Pursuant to article 3a of the Decree, the current relevant substance requirements for Dutch resident financial service companies are:

1. At least 50% of the statutory (and competent) directors of the Dutch company must be residents of the Netherlands;
2. The Dutch resident directors have the required professional knowledge to perform their duties satisfactorily. The directors should exercise their own discretionary authority with respect to the conclusion of transactions entered into by the company, and should take responsibility for the proper implementation of such transactions;
3. The Dutch company should have qualified personnel in order to fulfil and administer the transactions entered into by the company satisfactorily;
4. Decisions of the board of directors must be taken in the Netherlands;
5. The most important bank accounts of the Dutch company are held in the Netherlands;
6. The Dutch company actually performs its bookkeeping in the Netherlands (under certain conditions shared service centres are accepted);
7. The registered address of the company must be in the Netherlands;
8. The Dutch company should, to its best knowledge, not be considered a tax resident of another country;

9. The Dutch company should bear economic risk related to its financing, licensing, rental or leasing transactions; and
10. The Dutch company holds sufficient equity relative to the risk as described in point 9.

New relevant substance requirements

Besides the ten aforementioned already existing Dutch substance criteria, two additional criteria should be fulfilled by financial service companies:

- a minimum of EUR 100,000 labour costs relating to the relevant holding activities should be incurred by this shareholder;
- an office space must be owned or rented by this shareholder, from where the business activities are performed for at least 24 months.

Expected implementation

The expansion of the Decree was published in the Government Gazette on December 27, 2019, and the policy is expected to take effect on January 1, 2021 (simultaneously with the proposed conditional withholding tax on interest and royalties).

Substance in light of COVID-19

The COVID-19 crisis most likely also impacts the possibility to comply with substance requirements. It may be difficult to comply with requirements that at least half of the total number of directors and other persons with decision-making power qualifies as tax resident in the Netherlands (or abroad) and that management decisions are taken in the Netherlands (or abroad).

In accordance with the OECD, the Dutch government has taken a willing approach that travel restrictions imposed due to the current COVID-19 pandemic should not affect the tax residency of companies, the recognition of permanent establishments and the application of substance requirements (as set forth above).

Should you have any questions on how the changes in substance requirements for financial service companies will affect your business, please do not hesitate to contact us.

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13 October 2020