

## Israel Desk E-mail Bulletin

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28 March 2008

### **New guidelines on the application of the participation exemption**

The Ministry of Finance published a long awaited decree (the "Decree") on certain topics related to the application of the Dutch participation exemption rules. The Decree has retroactive effect as of 1 January 2007. The Decree provides for guidance on certain issues which have led to discussions between taxpayers and the Revenue Service on the scope of the participation exemption since the amendment of the participation exemption regime as per 1 January 2007. Most topics addressed in the Decree reiterate statements made by the Ministry of Finance during legislative hearings. This flash summarises only recently issued guidance.

### **Asset Test**

The Dutch participation exemption provides for a full exemption of all benefits (dividends and capital gains) derived from a qualifying shareholding in a subsidiary. A shareholding in a subsidiary generally qualifies for the participation exemption if it represents 5% or more of the nominal issued paid-up capital of the subsidiary, unless the subsidiary is a "low-taxed passive investment company" ("LTPIC"). A subsidiary is not an LTPIC if, amongst others, its assets, together with the assets of any lower-tier subsidiary, qualify for 50% or less as passive investments (the "Asset Test"). For purposes of this test, (the pro rata part of) all assets of all (first-tier, second-tier, etc.) subsidiaries in the chain of ownership must be added, and must be earmarked as either active or passive. The Decree clarifies that for purposes of this test:

- real property owned by a subsidiary and leased to an affiliate engaged in an active trade or business, is not a passive investment, provided the lessor directly or indirectly owns the lessee or vice versa or both are held, directly or indirectly, by the (lower-tier) subsidiary;
- a receivable held by subsidiary A on affiliate B is not a passive investment if such receivable is matched by an intra-group loan from another affiliate, C, provided A directly or indirectly owns C or vice versa and both are held, directly or indirectly, by the (lower-tier) subsidiary;
- trade receivables with a term of less than 3 months arising in the conduct of an active trade or business are not passive investments.

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The experience of the members as regards the Israeli market is combined with their extensive knowledge of international tax law, corporate structuring, banking and securities law, regulatory law, employment law. In addition to being part of the Israel Desk, the members also participate in Loyens & Loeff teams that focus on specific industries and sectors, such as energy, real estate, private equity, fund structuring, corporate finance, and financial products.

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### **Real property holding companies**

A “real property holding company” is not an LTPIC. Hence, a shareholding of 5% or more in such entity will generally qualify for the participation exemption. A subsidiary is considered a “real property holding company” if its assets on a consolidated basis (including the assets owned by lower-tier subsidiaries, other than assets held by subsidiaries that qualify as Dutch REITS) consist for 90% or more of “real property”. It has now been clarified that “real property” includes (i) certain rights on real property such as long leases, building rights and rights of servitude and comparable rights under foreign law, and (ii) the full economic ownership of a real property.

### **Final remarks**

The guidance provided in the Decree provides for certainty and clarity for Dutch holding structures, including real property holding structures. The Decree indicates that the Revenue Service is willing to enter into preliminary consultations in respect of any other issues that may arise.

Members of the Israel Desk visit Tel-Aviv on a regular basis. If you would like to make an appointment or would like to receive more information with respect to the above, please feel free to contact <mailto:jeroen.ianssen@loyensloeff.com> or any other member of the Israel Desk.