

Israel Desk E-mail Bulletin Number 20 | 28 October 2010

Dutch developments on the taxation of dividend payments to Israel

Summary

The European Commission has, on 30 September 2010, requested (Request) the Netherlands to change its legislation that treat domestic companies holding a substantial interest in a Dutch company differently than foreign companies holding a substantial interest in a Dutch company. This Request might solve Dutch tax claims on dividend payments to Israeli shareholders.

Frequently used structures

Israeli investors often use a Dutch holding company for their foreign investments. If the structure is set up efficiently, dividend payments by this Dutch holding company to its Israeli shareholder are subject to 5% Dutch dividend withholding tax and capital gains derived on the alienation of the shares in the Dutch Holding company are exempt in Israel (provided that the NL/Israel tax treaty applies).

No 5% Dutch withholding tax

In order to improve the tax efficiency of the structure a Dutch Coop (coöperatie) is often used as holding company. A Coop is not subject to Dutch dividend withholding tax. Consequently, a Coop can distribute its profits without dividend withholding tax to its Israeli shareholder. However, the Israeli shareholder could be subject to Dutch corporate income tax for dividends it receives from Coop ("foreign taxation"). The Dutch corporate income tax is levied over the net income against a rate of 25.5 per cent.¹ If the NL/Israel tax treaty applies, the taxation is limited to 5 per cent over the gross dividend income. Due to this "foreign taxation" the structure could still face a tax burden of 5 per cent on dividend payments to Israel even if a Coop is used as a holding company.²

Request of the European Commission

The question is whether the taxation of foreign residents in situations that under domestic rules the participation exemption applies is incompatible with EU law. The European Commission considers the Dutch tax rules in question to breach EU rules on:

- (i) the free movement of capital (Article 63 of the Treaty on the Functioning of the European Union - **TFEU**);
- (ii) the freedom of establishment (Article 49 of the TFEU); and
- (iii) the Parent-Subsidiary Directive (2003/123/EC).

The Request is in the form of a "reasoned opinion" under an EU infringement procedure, giving the Netherlands two months to comply. If there is no satisfactory reply within this deadline, the European Commission may refer the Netherlands to the EU's Court of Justice.

1 The Dutch corporate income tax rate will be reduced to 25 per cent as of 2011.

2 Please note that there are solutions available to structure the dividend payments in such a way that no Dutch tax is due.

Consequences of the Request

At this moment there is no clarity what the consequences of the Request will be. The Request might result in the abolishment of the taxation of foreign investors with respect to the received dividend payments. If such an abolishment will indeed be introduced, it might be possible for a Coop to distribute dividends to Israel free from Dutch taxation. We will update you on any further developments regarding this issue.

Please contact us should you like to discuss these developments further.

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 jeroen.janssen@loyensloeff.com or any other member of the Israel Desk. Please see also the [Israel Desk web page](#) for more information.

Colophon

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