



BDO Seidman, LLP  
Accountants and Consultants

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## Subject:

### Proposed Dutch Corporate and Individual Tax Cuts

# International Tax Alert

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## Issue:

The Dutch government has issued proposed corporate and individual tax cuts under its 2007 budget.

## Affecting:

Potentially, U.S. corporations and their shareholders doing business in the Netherlands could be affected.

## Details:

Effective January 1, 2007, the proposed tax reduction will impact corporations, businesses and individuals through a tax rate decrease. The total monetary impact of the tax cut is estimated to be 1 billion Euros. The tax cut offers the income tax rate decrease from 29.1% to 25.5% for profits exceeding Euros 60,000 and a decrease in the dividend withholding rate from 25% to 15% for corporations. The proposed corporate income tax cuts would also apply a 20% rate on annual profits of up to Euro 25,000 and a 23.5% rate on annual profits of between Euro 25,000 and Euro 60,000. For individuals, the plan will offer a reduced tax rate for those who file under the first bracket.

The Dutch government hopes that ultimately, the tax rate reduction will not only increase purchasing power for individuals but also improve the competitiveness of domestic companies, as the proposed corporate income tax rate for 2007 will provide a lower income tax rate than the European average tax rate.

In addition to the reduction in tax rates, the proposed tax reform includes several changes to the participation exemption, including a strict minimum shareholding requirement set at 5%. The current separate tests of the participation exemption will be replaced by a single test, dropping the so-called portfolio test and subject-to-tax test, for both domestic and foreign shareholders. This allows active

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subsidiaries in low and even no-tax jurisdictions to benefit from the participation exemption.

The participation exemption will not apply to low-taxed investment subsidiaries, for which the assets of the company consist of more than 50% of investment and the effective tax rate is less than 10%, calculated under Dutch standards. The investment includes assets used in the financing of group companies and business assets put at the disposal of group companies unless the activities of the subsidiary qualify as active financing. To avoid the double taxation, the parent can obtain a deemed 5% credit for foreign taxes, given that the subsidiary is not fully exempt from local tax. In the case of EU subsidiaries, the taxpayer can opt for a credit for the actual underlying tax on profit when the tax rate is higher than 5%.

The exception for low taxed investment companies would not apply to a subsidiary that has 90% or more of its assets invested in real estate.

An annual revaluation requirement is introduced in case the parent owns 25% or more in a passive investment subsidiary. A passive investment subsidiary is a subsidiary of which 90% or more of the assets consist of investments and the effective tax rate is less than 10%.

In addition, the participation exemption also relaxes the rules relating to liquidation losses. The loss that arises upon the liquidation of a subsidiary remains tax deductible and the anti-abuse conditions related to liquidation of foreign subsidiaries are greatly simplified. Now, for both domestic and foreign subsidiaries, a liquidation loss is tax deductible in the case where 5% or more was held and the minimum holding period requirement does not apply. However, there are still anti-abuse rules related to tax base cost restrictions for transfers within the group.

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