Report of the Netherlands

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Summary

Introduction
The report consists of two parts. In the first part a description is provided of the Dutch method of qualifying entities as either transparent or non-transparent (opaque) for tax purposes. A division is made between domestic and foreign entities. In the second part a series of case studies are analysed in which the effects of differences in the qualification of entities in treaty situations are considered from the perspective of the Netherlands. This second part is preceded by several general remarks about the Netherlands approach in such cases.

Qualification of domestic entities
The Netherlands levies a corporate income tax from entities recognized as taxpayers under the Corporate Income Tax Act 1969 (CITA). The treatment of domestic entities as either opaque or transparent for Dutch tax law purposes depends on an explicit reference in Art. 2, par. 1, of the CITA to a series of different legal forms recognized in Dutch company law: public and private companies, cooperatives, associations and foundations and, under very specific circumstances, certain open partnerships.
Most entities are deemed to conduct business activities by means of their total asset base. Hence, all income of these entities is taxable under the CITA. Furthermore, the entities listed in Art. 2, par. 1, CITA must be resident in the Netherlands to be liable to tax on their entire worldwide income. However, the entities mentioned in Art. 2, par. 1, CITA that are established under Dutch company law are deemed to be resident in the Netherlands (Art. 2, par. 4).

Foreign entities
'Foreign entities', as relevant for the direct taxation rules in the Netherlands, are all entities (worldwide) which are not established under Dutch company law. Foreign entities that are recognized for Dutch tax purposes are treated as resident or non-resident taxpayers. A resident taxpayer is taxed on the worldwide income; a non-resident taxpayer only on income sourced in the Netherlands. To determine whether an entity is to be considered resident in the Netherlands, it is generally required that the place of effective management of the entity is in the Netherlands.
To determine whether a foreign entity can be classified as a taxable entity (whether the entity is regarded as transparent or non-transparent), the legal characteristics of the entity must be compared with those of the domestic entities that are treated as transparent or non-transparent for Dutch tax purposes. Generally, it can be concluded that the foreign entity will be treated in the same way as the Dutch 'counterpart' entity with which it has the most similarity. There is no 'hard' law on how this 'resemblance test' should be applied. Guidance in this respect can be obtained from some case law and in addition to that from a decree from the Ministry of Finance setting out the relevant criteria. These criteria are generally considered to (roughly) reflect the approach by the Supreme Court.
The decree provides questions based on which a decision about transparency or non-transparency is to be made. Those questions refer to who formally owns the assets, the extent of the liability of participants, whether the capital of the entity is divided in shares and what conditions exist for replacement and entry of participants.
A list of foreign entities is published by the Ministry of Finance. This list includes examples of foreign entities which have been considered and assessed by the tax administration though the list is merely indicative. The tax status of the foreign entity in the country in which it is established is not relevant. There is also no such thing as an optional system in the Netherlands that offers foreign entities a choice between being treated as transparent or non-transparent. There is no specified system for advance rulings on transparency or non-transparency in the Netherlands. It is however part of the general approach by the tax administration in the Netherlands that certainty in advance will be granted by the tax inspectors in 'bona fide' cases.

Preliminary remarks and summary of case studies dealing with treaty application
It should be emphasized that the Netherlands has made quite fundamental observations with regard to the OECD Model Tax Convention approach with regard to partnerships and conflicts of qualification (observation 27.1 on Article 1 and observation 80 on Articles 23 A and 23 B). The main result of these observations is that in principle in every situation the Netherlands will follow its own qualification of a foreign entity and apply a treaty in line with that qualification. A different approach must be applied if a specific treaty states that the Netherlands has to deviate from its domestic qualification or as a result of a mutual agreement procedure. Furthermore, under certain conditions the Netherlands will unilaterally grant treaty benefits to partners of a partnership that is treated opaque for Dutch purposes but is not regarded a resident for treaty purposes as a result of the transparant treatment by the other state.

It should be noted that in fiscal literature it has been argued based on the principle of effectiveness that even despite these observations, the Netherlands may in specific cases have to follow the approach, in particular, illustrated in the paragraphs starting from number 2 of the Commentary on Article 1 of the OECD Model Tax Convention.

In addition it may be relevant that the Netherlands does have a withholding tax on dividends, but does not levy a withholding tax on interest or royalties. Only in a few specific situations will the Netherlands levy income tax or corporate income tax on interest or royalties received by non-resident individuals or non-resident non-transparent entities, paid by a Dutch resident. As a result, the practical relevance of which treaty to apply in several of the case studies where the Netherlands would be the source state is minimal and therefore the actual experience therewith is minimal too.

I. ENTITY QUALIFICATION IN DOMESTIC TAX LAWS/THE NETHERLANDS

Domestic entities

The Netherlands levies a corporate income tax from entities which are recognized as taxpayers under the Corporate Income Tax Act 1969 ('Wet op de vennootschapsbelasting 1969', hereafter the CITA). In this document, an analysis is made which is grounded in the CITA. It should be noted that, for the entities recognized as taxpayers under the CITA, which have a capital divided into shares, the other tax relevant for purposes of this report is the dividend withholding tax (based on the 'Wet op de dividendbelasting 1965'; hereafter the DWHT). The Netherlands does not levy an interest or royalty withholding tax.

Entities governed by Dutch company law are considered to be domestic entities from a company law perspective, regardless of their place of management or registration. The Netherlands applies the incorporation theory in company law.

List of taxable entities

The treatment of domestic entities as either opaque or transparent for Dutch CITA (that is: tax law) purposes depends on an explicit reference to a number of different legal forms which are recognized in company law. Art. 2, paragraph 1, CITA, provides a detailed list of the entities that are considered liable to tax on their worldwide income if they are resident in the Netherlands.[1] Most of the list is comprised of legal entities established under Dutch company law which includes public and private companies ('naamloze vennootschap' and 'besloten vennootschap', NV and BV), cooperatives and associations operating on a cooperative basis, mutual insurance associations and other mutual associations acting as insurance or credit organizations, associations and foundations qualified under the Housing Act ('Woningwet') as institutions working in the interests of housing ('volkshuisvesting'), and foundations and associations.[2]

For the sake of practical relevance, it is important to note here that, of the list of entities included in Art. 2, the BV is by far the most regularly used legal form. In 2012 1,247,445 businesses were registered in the Netherlands. Some 693,655 of these were conducted directly by an individual (and are thus outside the scope of this report), 152,185 were conducted through a general partnership (and are therefore also outside the report's parameters) and 303,150 were conducted through a BV.[3]

In addition to the legal entities mentioned, certain general and limited partnerships (which under Dutch company law have no legal personality) and other contractual agreements of cooperation (such as mutual investment funds) are included in the list.

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[1] Art. 3, CITA regulates limited tax liability in the Netherlands and is applicable to entities which are not considered to be resident in the Netherlands for tax purposes but are only taxed on the income that is sourced in the Netherlands. In this article, descriptions are used that refer to an association, a body corporate, an open limited partnership and any other company whose capital is wholly or partially divided into shares but which does not have a legal personality or special purpose funds. Domestic entities are deemed to be resident in the Netherlands based on Art. 2, par. 4, CITA.

[2] For foundations and associations, an additional condition applies which is addressed in the next subsection.

[3] Figures derived from the official website of the Dutch institution for statistics - the Centraal Bureau voor de Statistiek (CBS): http://statline.cbs.nl. Please note that the term 'businesses' is defined as organizations that actually conduct their business in an autonomous way. In this sense a business can consists of several branches and/or legal entities. The number of other (legal) entities is relatively small. Only 995 NVs, 1,605 cooperations and 6,825 limited partnerships were registered. From the figures available, it is not possible to establish a distinction between closed and open limited partnerships.

General partnerships (the Dutch 'vennootschap onder firma' and 'maatschap') and limited partnerships ('commanditaire vennootschap') are recognized as separate entities under Dutch company law but are generally not considered taxable entities for CITA purposes. However, an exception is made for partnerships which have certain characteristics which are largely similar to those of an NV and a BV. The open limited partnership is of particular relevance here. An open limited partnership is a limited partnership in which the limited partners can be admitted or substituted without the (prior) consent of all the partners, both limited and general, for reasons other than those of inheritance or legacy.[4] According to the Supreme Court, this requirement is met even if the consent of only one or a few partners but not of all partners is required.[5] The open limited partnership has a hybrid character for Dutch CITA purposes; its status as a taxpayer for CITA purposes is limited to the part that can be allocated to the limited partners. General partners in either an open or closed Dutch limited partnership are taxed directly on their own account.[6]

Mutual investment funds ('fondsen voor gemene rekening') are not recognized as legal entities under Dutch company law. A mutual fund is based on a contractual agreement drawn up between investors and a manager, with the aim of investing and managing, for joint account and risk, the contributions of the investors to the fund. Whether a mutual fund is regarded as transparent or opaque for Dutch CITA and DWHT purposes depends on the conditions for the transferability of the participations. A mutual fund is regarded as opaque and treated as an entity for Dutch CITA purposes if it is possible to dispose of the participations without the consent of all the investors, taking into account that the participations will be considered to be non-transferable if they can only be transferred to the fund itself or to the relatives of the investors connected by blood or affinity in the direct line (Art. 2, par. 2, CITA).

Therefore, the tax status of limited partnerships and mutual funds depends on the internal provisions of the specific legal form in regard to the transferability of the partnership rights. If the partnership rights or the participations in the mutual fund are not freely transferable, the entity is considered transparent. This means that, in practice, for these forms only, it is possible to choose between transparency and non-transparency, even though the Netherlands system is based on the list under Art. 2 and these entities are not offered an optional regime that would allow a choice to be made between transparency and non-transparency.

Business activities in relation to qualification as a *taxable entity*

Apart from the foundation and the association, all the other entities are deemed to conduct their business activities by exploiting their total asset base (Art. 2, par. 5, CITA). Hence, all their income is taxable under the CITA. The foundation and the association are liable to Dutch corporation tax if, and to the extent that, business activities are conducted. Hence, these entities are only partially liable to corporate income tax. Separate rules for business activities conducted by public bodies also exist, but in general, these activities are not liable to tax; there are, however, certain specified business conducted by public legal entities which are regarded as taxable entities (Art. 2, par. 1, sub g, CITA).

Residency requirement

As mentioned, the entities listed in Art. 2, par. 1, CITA must be resident in the Netherlands to be liable to tax on their worldwide income. As a general rule, an entity is considered to be resident in the Netherlands if it is effectively managed from the Netherlands.[7] However, the

[4] Art. 2, par. 3, sub c, General Tax Act ('Algemene wet inzake rijksbelastingen': hereafter GTA). Supreme Court 24 November 1976, No. 17.998, BNB 1978/13. The issue of free transferability is dealt with in the Decree of 11 January 2007, No. CPP2006/1869M.
[5] Supreme Court 27 February 2009, No. 43.388, BNB 2009/120. In fiscal literature, it is generally acknowledged that this rule should apply in a similar manner to other entities operating under the same conditions.
[6] Supreme Court 7 July 1982, No. 20.655, BNB 1982/268.
[7] Art. 4, par. 1, GTA.

domestic entities listed under Art. 2, par. 1, CITA are deemed resident in the Netherlands (Art. 2, par. 4, CITA). The same applies to European Companies ('Societas Europeae') that are established under Dutch company law. Thus, residency in the Netherlands based on the factual circumstances with particular regard to the effective management is, in fact, under domestic laws only relevant for foreign entities.[8]

No other requirements

As explained, the list in Art. 2 is decisive in establishing the status of an entity for corporate income tax purposes. Subjective exemptions (e.g. the exemption for pension funds), objective exemptions (e.g. the participation exemption) and other specific regimes (e.g. the 0% tax rate for certain investment institutions) do not affect the status of an entity as a taxable entity. Furthermore, being part of a fiscal unity – a group of taxable entities consolidated for tax purposes – does not affect the subjective status of the entities listed under the CITA.

Registration with the tax administration, or other regulatory approvals, is not constitutive for recognition as a taxable entity for CITA purposes. The liability to CITA of entities established under Dutch company law commences on the date of their establishment (through the deed of incorporation of a BV or NV or the conclusion of an agreement on a partnership, mutual fund etc.). Associations and foundations are liable to corporate income tax from the date they conduct a trade or business. The liability for Dutch corporate income tax ends on the date of the entity's dissolution, on the date on which the entity ceases to be resident in the Netherlands for purposes of the CITA or a double tax treaty, when an association or foundation no longer conducts a trade or business or when the internal regulations of a limited partnership or mutual investment fund are changed in such a way that they no longer meet the requirements of non-transparency.

[8] Please note that it is necessary for an NV or BV to be effectively managed in the Netherlands or to have a permanent establishment in the Netherlands to be part of a fiscal unity for Dutch corporate tax purposes (Art. 15, par. 3 and 4 CITA).

Foreign entities

'Foreign entities', in relation to the direct taxation rules[9] in the Netherlands, are all those entities (worldwide) which are not established under Dutch company law. The registration of the entity is not a relevant criterion for making the distinction between foreign and domestic entities.

Tax treatment of non-transparent foreign entities

Foreign entities that are recognized for Dutch tax purposes are treated as either resident or non-resident taxpayers; to determine this status the '(actual) circumstances' are decisive. This is as literal a translation as possible of Art. 4, par. 1, GTA. Clearly, this is a general rule. It has not been defined which facts are considered relevant, or how to weigh the different relevant circumstances. From substantive case law, however, one can deduce that the effective management of an entity is the most decisive factor in determining its location.[10] The effective management of an entity is generally regarded to be with the board of directors of the company. Thus, the place of actual management coincides with the place in which the board of directors performs its executive functions.[11] If the actual management is located in the Netherlands, then the entity is considered to be domestic and is a resident of the Netherlands. However, if the contribution made by a board of directors in the Netherlands in a specific and exceptional situation was limited to a rubber stamping exercise, then the place of actual management is considered to be located where the decision taking is actually conducted.[12] Although the place of actual management is of a decisive nature in determining the place of residency, other circumstances are considered relevant as well, especially as a means of assessing where the actual management is located. One might think here of the factual circumstances, like the place of residence of the (members of the) board of directors and of the supervisory board, in certain cases one might also consider where the shareholders are based, where other (senior) personnel perform their duties, where the bookkeeping is done and the location of bank accounts etc.

As one can see, the classification of foreign entities for Dutch tax purposes is particularly relevant for the application of resident or non-resident taxation.[13]

Qualification of foreign entities as transparent or non-transparent

To determine whether a foreign entity can be classified as a taxable entity, (i.e. whether the entity is regarded as transparent or non-transparent), the legal characteristics of the entity must be compared with those of the domestic entities that are treated as transparent or non-transparent for Dutch tax purposes. Generally, it can be concluded that the foreign entity will be treated in the same way as the Dutch 'counterpart' entity with which it has the most similarity. Thus, one could speak of a 'resemblance test' for foreign entities (instead of the more formal legal forms test which is used for domestic entities), in order to establish whether or not the foreign entity is liable to tax in the Netherlands. This resemblance test also relies on

[9] Direct taxation, for the sake of this analysis, consists of – in order of relevance – the Dutch CITA, the DWHT, individual income tax and wage tax. In this part of the report the text starts with these four, main direct taxes for which entity qualification may be necessary. In the following part of the text the content focuses more specifically (again) on just the CITA and the DWHT.

[10] For example: Supreme Court 1 July 1987, No, 23.877, BNB 1978/306, and Supreme Court 27 April 1988, No. 24.252, BNB 1988/181.

[11] Supreme Court 23 September 1992, No. 27.293, BNB 1993/193.

[12] Supreme Court 23 September 1992, No. 27.293, BNB 1993/193.

[13] The CITA liability for foreign entities, which are considered to be tax residents in the Netherlands, is based on Art. 2, CITA. The article speaks, in particular, of a company whose capital is wholly or partially divided into shares or other non-public legal entities to the extent to which they conduct a business. Art. 3 CITA applies to foreign entities, which are not considered to be tax residents in the Netherlands, but who are only taxed on the income that they have sourced in the Netherlands. In this article, descriptions are used that speak of an association, a body corporate, an open limited partnership and any other company which does not have a legal personality, whose capital is wholly or partially divided into shares, and special purpose funds. Entities that are comparable with associations and foundations established under Dutch company law are considered taxable entities to the extent they conduct a business (Art. 3, par. 2, CITA).

company law as it focuses on the characteristics of an entity, which are determined based on its foreign establishment or incorporation statutes or contracts. For the sake of clarity: even if a foreign entity has characteristics which are very similar to a (specific) Dutch legal form, the entity formally remains 'foreign'. Depending on the 'actual circumstances', as described before, it could, however, become a Netherlands tax resident if the effective management is performed in the Netherlands.

There is no 'hard' law that prescribes how to make a distinction between transparent and non-transparent foreign entities, and little guidance is provided in the case law on this matter. The approach of the Supreme Court which can be deduced from the available case law is generally considered to be (roughly) reflected in a decree published by the Ministry of Finance which sets out the relevant criteria. The most recent version of this decree is dated the 11th of December 2009.[14] Hereafter we will briefly discuss the relevant case law and subsequently focus on the decree. It is relevant to note that the classification of foreign foundations, associations, mutual funds, trusts and comparable entities is not included in the scope of this decree. The classification of these types of entities is dealt with separately.

The first test to be considered according to the Supreme Court, relates to the entitlement of the profits and losses of the business activities conducted by the entity: who owns the rights and obligations from the conduct of the business and, hence, is (directly) entitled to the profits? [15] The Supreme Court appears to make this assessment using the following criteria:[16] the liability of the participants is limited to their (capital) contribution in the entity;[17] the business is legally owned by the entity and is not actually being conducted on the account and at the risk of the participants in any other way. If, based on these criteria, it can be concluded that the rights and obligations from the conduct of a business are owned by the entity, the entity is classified as a body corporate for Dutch tax purposes. A body corporate such as this, which is comparable with a Dutch NV or BV, will be regarded as opaque if the capital is wholly or partly divided into shares.[18] However, if the participants are directly entitled to an entity's profits (and in that respect the entity resembles more – generally speaking – a partnership than a limited liability company), then, in a limited number of situations, a second test is applied which assesses whether the internal regulations imposed on the relationship between the entity and the participants resemble those of an open limited partnership or a partnership with capital divided into shares. The distinctive criterion in this respect (as previously discussed re. domestic entities) is whether the participations in the entity are freely transferable.

The decree of the State Secretary uses a slightly different method to that of the Dutch Supreme Court and formulates four questions - the answers to which are then used to decide whether an entity is transparent or non-transparent. These four questions are:[19]
1. Is it possible for the entity to legally own the assets with which it performs its activities?
2. Are all participants in the entity only legally liable, to a limited extent, for the debts and

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[14] Decree of the State Secretary of Finance, 11 December 2009, CPP2009/519M. It is important to note that a decree as such has no legally binding power. It is an interpretation made by the State Secretary of Finance in his role as the person in charge of, and responsible for, the entire Dutch tax administration. The tax administration will follow this decree and generally, based on the principle of 'legitimate expectations' ('vertrouwensbeginsel'), tax payers can rely on its application by the tax administration. Formally however a tax payer can object to its application although the courts, in practice, will often follow the interpretation published by the State Secretary. Even though one should be careful about making generalizations, it seems safe to say that the decree mentioned reflects an analysis of transparency and non-transparency that is and will in most cases be in line with how Dutch courts will decide in individual cases.
[15] Supreme Court 31 December 1924, B. 3569 and 7 June 1939, B. 6925.
[16] Supreme Court 2 June 2006, No. 40.919, BNB 2006/288.
[17] In Supreme Court 23 September 2011, No. 10/03724, BNB 2012/12 it was decided that, whether the liability of the participants is limited or not, in principle it depends on the company law that governs the relationship between the entity and the partners.
[18] Supreme Court 16 March 1994, No. 27.764, BNB 1994/191. The capital of an entity is divided into shares if the capital consists of contributions made in exchange for participations and if each participation entitles its owner to a proportionate part of the capital (Supreme Court 4 March 1970, BNB 1970/131).
[19] There is no formal translation of this decree in English. The translation here is as precise as possible, but it is inevitable that a few of the nuances are not exactly reflected in English. That argument is obviously relevant to several aspects of this report, but it may be particularly relevant for this decree.

other obligations of the entity to third parties? The extent that is meant in this context is the amount that is contributed to the entity for the participation rights or that is agreed to be contributed for that same reason.
3. Does the entity have capital divided into shares for company law purposes, or can the capital be regarded as having been divided into shares?
4. Is the entry of new, or the replacement of existing, participants possible without the consent of all participants, except in cases of inheritance or legacy?

In general the decree states that if the answer to three out of four of the questions is affirmative, then the entity is considered to be non-transparent. Additionally, an entity is non-transparent if (a) the liability of all participants is limited to the amount they have contributed to the entity (or have agreed to contribute), (b) the enterprise in operation is owned by the entity and (c) the enterprise is not operated at the risk and on the account of the participants in any other way. This added variation reflects the decision made by the Supreme Court mentioned above.[20]

Furthermore, the decree states that even though an entity might be considered to be transparent based on the above rules, it could nevertheless be treated as non-transparent if it was comparable to a specified Dutch legal entity called the 'commanditaire vennootschap', which is itself, in fact, partly treated as transparent and partly as non-transparent under the domestic tax laws of the Netherlands, as explained earlier. Along these same lines, there is another exception that states that the decree is not decisive for foreign entities that are comparable with a few specifically mentioned and generally not very common Dutch legal forms of entities.[21]

For the sake of clarity: the tax status of the foreign entity in the country in which it is established is not relevant. There is also no such thing as an optional system in the Netherlands that offers foreign entities a choice between being treated as transparent or non-transparent.[22]

Besides, the text of the decree suggests that mandatory rules in the relevant country on the establishment of entities might clarify whether the conditions are met in a specific case, but it is also possible, within the scope of the foreign rules, for variations to occur and for entities to have different organisational regulations in their specific establishment agreements. In that case, the specific conditions of that particular entity are decisive in determining transparency or non-transparency.

Reference is made in the decree to a list of foreign entities published by the Ministry of Finance on its website. This list includes examples of foreign entities which have been considered and assessed by the tax administration of the Netherlands. The list is merely indicative, however, and the conditions still have to be met and assessed in each individual case.

As mentioned, foreign foundations, associations, mutual funds, trusts and comparable entities are not included in the scope of the decree. Thus, for the classification of these entities for Dutch taxation purposes, the resemblance test should be applied. It should be assessed whether the foreign legal forms – based on their domestic company law – are or are not

[20] Supreme Court 2 June 2006, No. 40.919, BNB 2006/288.
[21] Mentioned are: cooperatives and associations operating on a cooperative basis, mutual insurance associations and other mutual associations acting as insurance or credit organizations. It is relevant to note that with regard to these entities and the 'commanditaire vennootschap', additional aspects are mentioned in the decree, but due to their specificity and relative exceptionality these aspects are not addressed here.
[22] In practice for some partnerships like the 'commanditaire vennootschap' or the 'fonds voor gemene rekening', which are more or less specific variations of personal partnerships and collective investment associations respectively, the way the establishment agreement is given form with regard to, in particular, the entry and replacement of participants, makes it possible (nearly) to choose between transparency and non-transparency. This is, however, the exception to the rule that there is no optional system. See also the earlier explanation in the part about domestic entities.

comparable with the domestic entities which are treated as opaque for CITA purposes.[23] When resident in the Netherlands, such foreign entities should be compared with the entities listed in Art. 2, par. 1, CITA. Non-resident foreign mutual funds, trusts and comparable entities could be regarded as special purpose funds ('doelvermogens'), mentioned in Art. 3, par. 1, CITA. According to the Supreme Court, a special purpose fund is made up of assets that are separate from a legal person or individual and cannot be regarded as a legal person in themselves, but are treated as a separate taxable entity.[24] An irrevocable trust, for example, is considered to be a special purpose fund. However, the exact scope of the term 'special purpose fund' is far from clear.

There is no specified system for obtaining advance rulings on the transparency or non-transparency of entities in the Netherlands. However, part of the general approach taken by the tax administration in the Netherlands, is that certainty, in advance, is granted by the tax inspectors. This certainty is given unless the taxpayer is attempting to receive clearance for a fiscal scheme that borders on using taxation rules in a way that is not in line with the purpose of these rules and is close to tax avoidance. What most commonly happens in Dutch practice is that, in bona fide situations, the tax inspector will be willing to giving advance certainty depending on whether a specific foreign entity is considered to be transparent or non transparent for domestic law purposes. In fact, there is an experienced coordinating team within the Dutch tax administration that functions as a back office handling questions such as these that are submitted to individual tax inspectors all over the country.

[23] For associations, this principle is laid down in Art. 2, par. 2, sub a, GTA. According to this article 'association' includes any other form of cooperation which does not have a legal personality that is generally regarded by society as being comparable with a (formal) association.
[24] Supreme Court 18 November 1998, No. 31.756, 31.758 and 31.759, BNB 1999/35-37.

II. CASE STUDIES ON TAX TREATY ENTITY QUALIFICATION ISSUES

Preliminary remarks

Before any analysis of the case studies, a few preliminary remarks should be made about the Dutch approach as this puts all the answers to the case studies in perspective and enables more succinct responses to be made.

1. Observations with regard to the OECD approach

It should be emphasized that the Netherlands has made some quite fundamental observations to the OECD Model Tax Convention approach to partnerships and conflicts of qualification.

Observation 27.1 on Art. 1 reads: "The Netherlands will adhere to the conclusions on the application of the Convention to partnerships incorporated in the Commentary on Article 1 and in the Commentaries on the other relevant provisions of the Convention only, and to the extent to which, it is explicitly so confirmed in a specific tax treaty, as a result of mutual agreement between competent authorities as meant in Article 25 of the Convention or as unilateral policy."

Observation 80 on Articles 23 A and 23 B reads: "The Netherlands in principle is in favour of solving situations of both double taxation and double non-taxation due to conflicts of qualification between Contracting States, since in the Netherlands view such situations are not intended by the Contracting States and moreover go against the object and purpose of a tax treaty. However, the Netherlands does not agree with the interpretation given in paragraphs 32.4 and 32.6 to the phrase "in accordance with the provisions of this Convention" in Article 23 A and 23 B of the Convention that in cases of conflicts of qualification that are due to differences in domestic law between the State of source and the State of residence, as a rule the qualification given by the State of source would prevail for purposes of the application by the State of residence of Article 23 A or 23 B. The Netherlands wishes to preserve its right to subject a solution and its modalities for a certain conflict of qualification to the circumstances of the cases at hand and to the relationship with the Contracting State concerned. The Netherlands therefore will adhere to said interpretation in paragraphs 32.4 and 32.6 only, and to the extent to which, it is explicitly so confirmed in a specific tax treaty, as a result of a mutual agreement between competent authorities as meant in Article 25 of the Convention or as unilateral policy."

The consequences of these observations for the case studies are quite significant. The main result is that, in principle, in every situation the Netherlands will follow its own qualification of a foreign entity and apply the treaty which is in line with that qualification. A different approach must be applied if a specific treaty states that the Netherlands has to deviate from its domestic qualification (which is the case in only a limited number of situations in a limited series of Netherlands treaties; see under 4. below) or as a result of a mutual agreement procedure. Furthermore, under certain conditions the Netherlands will unilaterally grant treaty benefits to partners of a partnership that is treated opaque for Dutch purposes but is not regarded a resident for treaty purposes as a result of the transparant treatment by the other state.[25]

It should be noted that in fiscal literature it has been argued based on the principle of effectiveness that even despite these observations, the Netherlands may in specific cases have

[25] Decree of 19 March 1997, No. IFZ97/204.

to follow the approach, in particular, illustrated in the paragraphs starting from number 2 of the Commentary on Article 1 of the OECD Model Tax Convention.[26]

2. *Just dividend withholding tax, no withholding tax on interest and royalties*

One should also note that the Netherlands has a withholding tax on dividends, but no withholding tax on interest or royalties. Only in a few specific situations will the Netherlands levy income tax or corporate income tax on interest or royalties received by non-resident individuals or non-resident non-transparent entities, which are paid by a Dutch resident. As a result, in several of the case studies in which the Netherlands is the source state, the practical relevance of which treaty to apply is minimal and therefore the actual experience thereof is minimal too.

3. Limited experience in practice

One should be aware that none of the cases covered by the case studies have been decided in court or publicly addressed in decrees etc. Even though it is possible to draw probable conclusions about the way in which these cases will be addressed by tax practitioners in the Netherlands, discussion in a number of the cases is possible. It is fair to note in this respect that several articles have been published on qualification issues by different scholars.[27] Obviously, the views expressed in these articles do not provide firm conclusions for all the case studies and have sometimes approached qualification issues in a more general way (or sometimes a more specific way, focusing on specific treaty provisions), they have nevertheless been taken into account in preparing this report. The focus in the case studies is, however, on the probable applications in practice (and not on the various possible theoretical approaches).

4. Specific provisions in treaties concluded by the Netherlands

Because of the observations made by the Netherlands with regard to the OECD approach, the Netherlands State Secretary has stated that he prefers to solve issues with regard to differences in qualification of 'hybrid entities' and 'hybrid instruments'. He intends to do so in specific cases (on the basis of mutual agreement procedures) and in treaty negotiations.[28] In some treaties this approach has led to the creation of provisions dealing with qualification issues. Looking at it from a general perspective, one could say that these provisions provide rules and/or solutions primarily in cases where double taxation or taxation which does not conform to the intention of the treaty could occur. In addition they seem to address some cases where double non-taxation might be involved. The most prominent examples in the treaties between the Netherlands and the United States, the United Kingdom and Japan are quoted below without any further analysis. Some of those provisions address similar situations. All three treaties have entered into force. The alternative text used in the new treaty between the Netherlands and Germany is also included. This treaty has not entered into force and has – unlike the other texts – an official translation in English. The variation in the treaty between Germany and the Netherlands includes only one specific situation and adds a more general rule for approaching this type of issue in future cases.

4.1. Treaty Netherlands – United States (1992), Art. 24

Article 24
Basis of taxation
(…)

[26] F.A. Engelen, Fiscaal Verdragbeleid en het OESO-Modelverdrag, WFR 2011/549 and Frank P.G. Pötgens and Lucas J. de Heer, The International Public Law Efectiveness Principle and Qualification Conflicts from a Dutch Perspective, Intertax, 2012, No. 1, blz. 54.
[27] Although this is not a comprehensive overview, reference is nevertheless made to A.J.A. Stevens, A.W.G. Lamers and G.K. Fibbe, De Nederlandse behandeling van hybride entiteiten onder belastingverdragen, MBB 2011, No. 5 and G.K. Fibbe, Enkele observaties bij de bepaling inzake hybride entiteiten in het belastingverdrag met het Verenigd Koninkrijk, MBB 2013, No. 03.
[28] Note on tax treaty policy 2011, Chapter 2.3 (Kamerstukken II 2010/2011, 25087, No. 7).

4. In the case of an item of income, profit or gain derived through a person that is fiscally transparent under the laws of either State, such item shall be considered to be derived by a resident of a State to the extent that the item is treated for the purposes of the taxation law of such State as the income, profit or gain of a resident.

Memorandum of understanding (2004), relevant for the treaty Netherlands – United States (1992)
XIV. In reference to paragraph 4 of Article 24 (Basis of Taxation)
a. It is understood that, where, by virtue of paragraph 4 of Article 24 (Basis of Taxation) an item of income is considered by a State to be derived by a person who is a resident of that State, and the same item is considered by the other State to be derived by a person who is a resident of that other State, the paragraph shall not prevent either State from taxing the item as the income of the person considered by that State to have derived the item of income.

The following example demonstrates the application of the preceding paragraph:
Individual Z, a resident of the Netherlands, is the sole member of Y, a U.S. limited liability company (LLC). Y owns X, a U.S. corporation. Y has elected under the U.S. entity classification rules to be taxed as a U.S. corporation. Under Netherlands law, however, Y is treated, in this situation, as a fiscally transparent entity. On date A, X distributes a $100 dividend to Y. On date B, Y distributes a $100 dividend to Z. Under Netherlands law, the dividend from X to Y is considered to be derived by Z. The two States agree that, in these circumstances, the United States is not prevented from exercising full taxing jurisdiction over Y (which is treated as a U.S. corporation) and, accordingly, the United States may tax the dividends from X to Y and from Y to Z in accordance with its domestic law. However, with respect to the dividend from Y to Z, the rate of tax applicable to the dividend shall be determined in accordance with Article 10.

b. The competent authority of a State may grant the benefits of the Convention to a resident of the other State with respect to an item of income, even though it is not treated as income of the resident under the laws of that other State, in cases where the income would have been exempt from tax if it had been treated as the income of that resident.

The following example demonstrates the application of the preceding paragraph:
Z is an exempt pension trust within the meaning of Article 35 (Exempt Pension Trusts) that is a resident of the Netherlands for purposes of the Convention. Z is a member of Y, a U.S. limited liability company that has elected to be treated as fiscally transparent for U.S. tax purposes. Because of certain characteristics, Y is non-transparent under Netherlands law. Y owns shares in a number of U.S. companies that pay dividends currently. Under the general rule of paragraph 4 of Article 24 (Basis of Taxation), Z would not be entitled to the benefits of Article 10 (Dividends) because the income derived by Y is not treated by the Netherlands as the income of Z. However, the U.S. competent authority may determine that Z is entitled to benefits because Z would be exempt from tax on the income even if it were treated as having derived the income.

4.2. Treaty Netherlands – United Kingdom (2008), Art. 22

Article 22
Miscellaneous provisions

(…)
2. Where a resident of a Contracting State is a member of a partnership established under the laws of the other Contracting State, nothing in the Convention shall prevent the first-mentioned Contracting State from taxing that resident on his share of any income, profits or gains of that partnership.
3. In the case of an item of income, profit or gain derived through a person that is fiscally transparent under the laws of either State, such item shall be considered to be derived by a

resident of a State to the extent that the item is treated for the purposes of the taxation law of such State as the income, profit or gain of a resident.
4. Where, by virtue of paragraph 3 of this Article, an item of income, profit or gain is considered by a State to be derived by a person who is a resident of that State and the same item is considered by the other State to be derived by a person who is a resident of that other State, that paragraph shall not prevent either State from taxing the item as the income, profit or gain of the person considered by that State to have derived the item of income.
5. The competent authority of a State may grant the benefits of the Convention to a resident of the other State with respect to an item of income, profit or gain, even though it is not treated as income, profit or gain of the resident under the laws of that other State, in cases where such income would have been exempt from tax if it had been treated as the income of that resident.

4.3. Treaty Netherlands – Japan (2010), Art. 4

5. For the purposes of applying this Convention:
a) an item of income:
(i) derived from a Contracting State through an entity that is organised in the other Contracting State; and
(ii) treated as the income of the beneficiaries, members or participants of that entity under the tax laws of that other Contracting State;
shall be eligible for the benefits of the Convention that would be granted if it were directly derived by a beneficiary, member or participant of that entity who is a resident of that other Contracting State, to the extent that such beneficiaries, members or participants are residents of that other Contracting State and satisfy any other conditions specified in the Convention, without regard to whether the income is treated as the income of such beneficiaries, members or participants under the tax laws of the first-mentioned Contracting State;

b) an item of income:
(i) derived from a Contracting State through an entity that is organised in the other Contracting State; and
(ii) treated as the income of that entity under the tax laws of that other Contracting State;
shall be eligible for the benefits of the Convention that would be granted to a resident of that other Contracting State, without regard to whether the income is treated as the income of the entity under the tax laws of the firstmentioned Contracting State, if such entity is a resident of that other Contracting State and satisfies any other conditions specified in the Convention;

c) an item of income:
(i) derived from a Contracting State through an entity that is organised in a state other than the Contracting States; and
(ii) treated as the income of the beneficiaries, members or participants of that entity under the tax laws of the other Contracting State and under the tax laws of the state where the entity is organised;
shall be eligible for the benefits of the Convention that would be granted if it were directly derived by a beneficiary, member or participant of that entity who is a resident of that other Contracting State, to the extent that such beneficiaries, members or participants are residents of that other Contracting State and satisfy any other conditions specified in the Convention, without regard to whether the income is treated as the income of such beneficiaries, members or participants under the tax laws of the first-mentioned Contracting State, provided that the state where the entity is organised has concluded with the first-mentioned Contracting State a convention which contains provisions for effective exchange of information on tax matters;

d) an item of income:
(i) derived from a Contracting State through an entity that is organised in a state other than the Contracting States; and
(ii) treated as the income of that entity under the tax laws of the other Contracting State;

shall not be eligible for the benefits of the Convention; and

e) an item of income:
(i) derived from a Contracting State through an entity that is organised in that Contracting State; and
(ii) treated as the income of that entity under the tax laws of the other Contracting State;
shall not be eligible for the benefits of the Convention.

4.4. Treaty Netherlands – Germany (2012), Protocol Art. I

I. With reference to the Convention as a whole (...)
2) In the case of an item of income, profit or gain derived through a person that is fiscally transparent under the laws of either Contracting State, such item shall be considered to be derived by a resident of a State to the extent that the item is treated for purposes of the taxation law of such State as the income, profit or gain of a resident.
In other situations where entities are considered to be transparent by one of the Contracting States and are considered to be non-transparent by the other Contracting State, and this leads to double taxation or taxation not in accordance with the provisions of this Convention, the competent authorities of the Contracting States shall find solutions pursuant to Article 25 in order to avoid double taxation or taxation not in accordance with the Convention and, at the same time, to prevent that, merely as a result of the application of the Convention, income is (partly) not subject to tax. The competent authorities of the Contracting States may publish such mutually agreed solutions.

5 Treaty entitlement of transparent mutual investment funds

As described in part I of this report, certain mutual investment funds are regarded transparent for Dutch tax purposes and thus not liable to tax for purposes of Art. 4 OECD MC.[29] Under the Netherlands tax treaty policy, the Netherlands intends to reach agreement with other countries establishing that both countries will treat such fund as transparent and the fund can claim treaty benefits on behalf of its participants. Such agreements have recently been established with the United States, Canada and Norway and this approach is included in the new tax treaty with Germany.

[29] Note on tax treaty policy 2011, Chapter 2.4 (Kamerstukken II 2010/2011, 25087, No. 7).

Case Studies

1. Treaty Entitlement

A.

a) If the Netherlands is State S, only the treaty P – S is applicable.

b) If the Netherlands is State R, only the treaty S – R is applicable. The result is that to the extent that State S is allowed to levy withholding tax according to that treaty, the Netherlands will grant a credit if the interest or royalties are included in the basis of taxation in the Netherlands (which would normally be the case, unless the income would be considered to be part of the income of a permanent establishment in State P of the entity that is a resident of State R).[30] The fact that the same income is also taxed in State P and that the same withholding tax is also credited in State P is not relevant.

B.

a) If the Netherlands is State S, the treaty P – S is not applicable as the entity is not liable to tax and thus is not regarded as being resident for treaty purposes. If the interest or royalty would have been part of the taxable income of the partners resident in State R, under certain conditions, the Netherlands will apply the treaty R – S. Given the fact the State R treats the entity as opaque, this will not be the case.[31]

b) If the Netherlands is State P and the interest or royalty is attributed to a permanent establishment in State P, the Netherlands will under certain conditions grant a credit. This policy is laid down in a decree of the State Secretary.[32] According to that decree, the policy is not formally based on the non-discrimination clause of the treaty P – R, but it is the result of a broad application of European non-discrimination rules.[33] The relevant conditions include in particular that a treaty P – R exists (it is not relevant whether or not this treaty includes a relevant non-discrimination paragraph, even though the decree is generally based on the intention of treating Dutch resident entities and permanent establishments in the Netherlands in the same way). The credit is limited to the lowest of the percentages of withholding tax allowed for the relevant type of income in the treaties P – S and R – S.

Furthermore, it can be argued that the treaty R – S must be applied based on the non-discrimination clause in Art. 24(3) OECD-MC.

According to the Netherlands tax treaty policy, the Netherlands intends to include in its tax treaties a specific provision granting treaty benefits to permanent establishments in the Netherlands that are in a similar position as Dutch residents.[34]

C.

a) If the Netherlands is State S, the treaty P – S is not applicable as the entity is not liable to tax and thus is not regarded as being resident for treaty purposes. If the interest or royalty is

[30] Supreme Court 8 February 2002, No. 36 155, BNB 2002/189 (“Japanese royalties”).
[31] Decree of 19 March 1997, No. IFZ97/204.
[32] Decree of 21 January 2004, No. IFZ2003/558M.
[33] ECJ 21 September 1999, case C-307/97 (Saint-Gobain).
[34] Note on tax treaty policy 2011, Chapter 1.3.5 (Kamerstukken II 2010/2011, 25087, No. 7).

part of the taxable income of the partners resident in State R, under certain conditions, the Netherlands will apply the treaty R – S.[35]

b) The answer is the same as under B. b).

c) The answer is the same as under A. b).

D.

a) If the Netherlands is State S, only the treaty R – S is applicable.

b) If the Netherlands is State P, the treaty P – S is applicable. The result is that to the extent that State S is allowed to levy withholding tax according to that treaty, the Netherlands will grant a credit, if the interest or royalties are included in the basis of taxation in the Netherlands. The fact that the same income maybe also taxed in State R and that the same withholding tax is also credited in State R is not relevant in principle.

E.

a) The answer is the same as under D. a).

b) If the Netherlands is State R, the treaty R – S is applicable. The result is that to the extent that State S is allowed to levy withholding tax according to that treaty, the Netherlands will grant a credit at the level of the entity if the interest or royalties are included in the basis of taxation in the Netherlands (which would normally be the case, unless the income was considered to be part of the income of a permanent establishment in State P of an entity that is a resident of State R).[36] The fact that the withholding tax is levied on behalf of the individual shareholder is not relevant in principle.

F.

a) If the Netherlands is State S, only the treaty R – S is applicable.

b) The answer is the same as under D. b).

G.

a) If the Netherlands is State P, this scenario is treated as a domestic situation.

b) If the Netherlands is State R, the interest or royalties are included in the taxable income in the hands of the shareholders. State R is not obliged to grant a credit as State P does not levy any tax at the level of the shareholders.

H.

a) If the Netherlands is State P, the interest or royalties are included in the taxable income in the Netherlands. The treaty P – R is applicable. The result is that the Netherlands will grant a credit to the extent that State R is allowed to levy (withholding) tax according to that treaty. The fact that the (withholding tax) is levied on behalf of the individual shareholder in State R is not relevant.

b) If the Netherlands is State R, the interest or royalties are included in the basis of taxation in State R. The Netherlands will not grant a credit for tax on the interest or royalties levied by State P at the level of the entity.

[35] Decree of 19 March 1997, No. IFZ97/204.

[36] Supreme Court 8 February 2002, No. 36 155, BNB 2002/184.

2. Distributive Rules

I. Article 10 - Dividends

A.

a) If the Netherlands is State R, the income received by the shareholders is not regarded as a dividend and State R will not grant a credit for the withholding tax levied in State S.

b) If the Netherlands is State R, the entities income will be exempted from tax in State R if and to the extent that the income can be qualified as income mentioned in the Art 6, 7 or 13, par. 1 and 2 of the OECD Model Convention.

c) If the Netherlands is State R, there will be no credit available for the tax levied in State S.

B.

a) If the Netherlands is State R, Art 10 OECD Model Convention is considered to be applicable.

b) If the Netherlands is State R, there will be no credit available for tax levied on the income from immovable property in State S.

II. Article 11 – Interests

A.

a) If the Netherlands is State A, the interest is sourced in State A and Art 11 of the treaty A – C is applicable.

b) If the Netherlands is State B, the interest is sourced in State B and Art 11 of the treaty B – C is applicable.

c) If the Netherlands is State C, it could be argued that the Netherlands qualification of the entity in this case is not of relevance. Pursuant to Art. 11, par. 5, the State of source is the state of which the payer of the interest is a resident. The "payer" is the entity P. Under the domestic legislation of State B, P is liable to tax and thus a resident for treaty purposes. In that case the interest would be source in State B and treaty B – C would be applicable.

However, taking into account the Netherlands approach to follow its domestic qualification of entities for treaty purposes and given par. 8.8 of the Commentary to Art. 4, it seems likely that State B should follow State C's qualification of the entity as transparant.[37] In that case the entity P would not be regarded a resident and the treaty A – C is applicable. Furthermore, if the activities of entity P constitute a permanent establishment in State B, the treaty B – C would be also applicable based on Art 11, par. 1 and 5 as, according to these articles, the interest is deemed to arise in the state in which the permanent establishment is situated, irrespective of the place of residence of the owner of the permanent establishment. The Netherlands would be obliged to grant a credit for the withholding tax levied in A and B.

[37] The Netherlands did not make an observation on par. 8.8 although the Netherlands did make an observation on par. 6.3 of the Commentary to Art. 1 which contains a similar approach.

B.

d) If the Netherlands is State A, the interest is sourced in State A and Art 11 of the treaty A – C is applicable.

e) If the Netherlands is State B, the interest is sourced in State B and Art 11 of the treaty B – C is applicable.

f) If the Netherlands is State C, the treaty B – C is applicable. The Netherlands is obliged to grant a credit for the withholding tax levied in State B as the interest is sourced in State B (the interest is paid by a resident of State B).

C.

g) If the Netherlands is State A, the interest is not paid by a resident of state A and State A would not have any right to levy tax.

h) If the Netherlands is State B, the interest is sourced in State B if the activities of the transparent entity P constitute a permanent establishment in State B and there is an obvious economic link between the interest bearing loan and these activities (Art 11, par. 5).

i) If the Netherlands is State C, the treaty A – C is applicable. According to Art 11, par. 1 and 5 the interest is deemed to arise in State A, irrespective of whether the activities of the transparent entity P constitute a permanent establishment in State B and of whether there is an obvious economic link between the interest bearing loan and these activities. Furthermore, if the activities of entity P constitute a permanent establishment in State B, the treaty B – C is also applicable based on Art 11, par. 1 and 5 as, according to these articles, the interest is deemed to arise in the state in which the permanent establishment is situated, irrespective of the place of residence of the owner of the permanent establishment. The Netherlands would be obliged to grant a credit for the withholding tax levied in both State A and State B.

D.

j) If the Netherlands is State A, the interest is not paid by a resident of State A and State A will not have any right to levy tax.

k) If the Netherlands is State B, the interest is sourced in State B if the activities of the transparent entity P constitute a permanent establishment in State B and there is an obvious economic link between the interest bearing loan and these activities (Art 11, par. 5).

l) If the Netherlands is State C, the treaty B – C is applicable if the activities of the transparent entity P constitute a permanent establishment in State B and there is an obvious economic link between the interest bearing loan and these activities (Art 11, par. 5). In that case the Netherlands is obliged to grant a credit for the withholding tax levied in State B as the interest is sourced in State B. If no permanent establishment can be recognized, the treaty B – C is not applicable as the interest is not paid by a resident of State B (entity P is not liable to tax in B).

E.

a) If the Netherlands is State C, the interest is sourced in State C and Art 11 of the treaty A – C is applied notwithstanding the application of Art. 11 according to State A.

III. Article 13 (4) – Capital Gains

A.

a) If the Netherlands is State R, a sale by a resident of State R of immovable property in State S is perceived. Only Art. 13, par. 1, of the treaty R – S will be applied by the Netherlands.

b) If the Netherlands is State S, a sale by a resident of State R of shares in an opaque entity in State P is perceived. Pursuant to Art. 13, par. 4 of the Treaty R – S, the Netherlands will have the right to tax the gains derived from the sale of the shares.

B.

a) The answer is the same as under A.a).

b) The answer is the same as under A.b).

C.

a) If the Netherlands is State R, a sale by a resident of State R of shares in an opaque entity in State P is perceived. Art. 13, par. 4 of the treaty P – R is not applicable because the immovable property is not situated in State P. Art. 13, par. 5, of that treaty will therefore be applied by the Netherlands. Furthermore, Art. 13, par. 4 of the treaty R – S is applicable because the immovable property is situated in State S.

b) If the Netherlands is State S, a sale by a resident of State R of immovable property in State S is perceived. Only Art. 13, par. 1, of the treaty R – S will be applied by the Netherlands.

D.

a) The answer is the same as under C.a).

b) The answer is the same as under C.b).

IV. Article 15 (2) – Income from Employment

A.

a) If the Netherlands is State R, the entity in State P is treated as opaque and thus is considered to be employer as meant in Art. 15, par. 2.b) of the treaty P – R.[38] We presume that there is an employment contract in effect between the entity and the individual (even though State P treats the entity as transparent).
Please note: Art. 15, par. 2.b) refers to “an employer who is a resident” which would not be the case from the perspective of either State, because in its state of establishment the entity is treated as transparent. Nevertheless, that does not seem important for the answer to the case, because Art. 15, par. 2.b) looks at a potential employer in State R, which is definitely not the

[38] A partnership can be regarded employer according to Supreme Court 30 January 1980, No. 19 434, BNB 1980/88.

case.

When applying Art. 15, par. 2., it seems that the Netherlands will only refrain from taxing the salary related to the employment exercised in State R if the individual is present in State R for less than 183 days, as the remuneration will not be considered to be paid by, or on behalf of, an employer who is a resident of State R, nor does there seem to be reason to consider the remuneration to have been borne by a permanent establishment in State R.

b) If the Netherlands is State P, pursuant to par. 6.2 of the Commentary to Art. 15, par. 2, the Netherlands perceives an individual resident of State P who generates income under an employment contract (as meant in Art. 15) from an employer in State R. The Netherlands as State P will refrain from taxing the salary related to the employment exercised in State R as the remuneration is considered to be paid by an employer who is a resident of State R.[39]

B.

a) If the Netherlands is State R, pursuant to par. 6.2 of the Commentary to Art. 15, par. 2, the Netherlands perceives an individual resident of State P who generates income under an employment contract (as meant in Art. 15) from an employer in State R. The Netherlands as State R will tax the salary related to the employment exercised in State R as the remuneration is considered to be paid by an employer who is a resident of State R.

b) If the Netherlands is State P (and we again presume that there is an employment contract in effect between the entity and the individual), the Netherlands perceives an individual resident of State P who generates income (as meant in Art. 15) from an employer in State P.

The Netherlands as State P would only grant elimination of double taxation if the individual is present in State R for more than 183 days as meant in Art. 15, par. 2.a).

See also the note with regard to case IV. A. a).

IV. Article 16 – Directors' Fees

A.

a) If the Netherlands is State R, a remuneration received by a resident individual may be perceived from activities conducted in State S which do not fall under Art. 16, because the Netherlands does not perceive a resident employer of State S. Whereas Art. 15, par. 1, only requires an employment, Art. 16 requires a remuneration of "a company which is a resident". The Netherlands could not acknowledge the entity's residency in State S, because the Netherlands treats such an entity as transparent and, in that case, it could never be considered to be liable to tax as meant in Art. 4, par. 1.[40] Therefore, in that case, the remuneration would fall under Art. 15.[41]

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[39] This approach is line with Supreme Court 12 October 2001, No. 35 749, BNB 2002/125, in which a transparent partnership seems to be disregarded for purposes of Art. 15, par. 2.c.

[40] Par. 8.8. of the Commentary on Art. 4.

[41] This case, to a certain extent, resembles a decision made by the Supreme Court of the Netherlands on the 4th of December 2009, No. 07/10383, *V-N* 2009/63.17. In this case an individual who was (in fiction) a resident of a foreign State was a director of a Dutch association

However, it could be argued that the Netherlands qualification of the entity in this case is not of relevance. If the entity qualifies as a company as meant in Art. 3, par. 1.b, the question whether this company is liable to tax and thus resident for treaty purposes should be assessed under the domestic law of State S. This would result in an approach that seems to be in line with the object and purpose of Art. 16.

b) If the Netherlands is State S, a director's fee derived by a resident of State R in his capacity as a member of the board of a company which is a resident of State S is perceived. Art. 16 is applicable.

B.

a) If the Netherlands is State R, the remuneration received by the individual resident of State R is not perceived as a director's fee as meant in Art. 16, because the relevant company is not a resident of State S, since State S treats the entity as transparent and the entity is thus not liable to tax as meant in Art. 4, par. 1. Therefore, in that case, the remuneration would fall under Art. 15 (see also case IV. A. a)).

b) If the Netherlands is State S, the answer is the same as under case IV.B. a).

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which was not liable for tax in the Netherlands. Because of this, the court considered the treaty article on income from employment to be applicable and not the article on directors' fees.