

## **Direct taxation: The European Commission formally requests the Netherlands to stop the discriminatory taxation of non-resident charities holding substantial interests in companies established in the Netherlands**

*The European Commission has formally requested the Netherlands to change tax rules which a) exempt charities which are resident in the Netherlands but which do not carry on an enterprise from corporation tax on their income from substantial participations in Dutch companies, while taxing such income of foreign charities which do not carry on an enterprise and b) exempt Dutch charities from taxation on interest they receive from debt claims on companies in which they hold a substantial interest, if they are not carrying on an enterprise while taxing such income of foreign charities, irrespective of whether they carry on an enterprise. The Commission considers these rules contrary to the freedom of establishment and to the freedom of movement of capital.*

Article 2.1.e. of the Corporate Income Tax Act 1969 (CITA) stipulates that charities which are resident in the Netherlands are only taxable in so far as they carry on an enterprise. On the basis of Article 3 of the CITA, charities resident outside the Netherlands are taxable as non-resident taxpayers in so far as they earn Dutch income. On the basis of Article 17a.1.c CITA debt claims of a company resident in the Netherlands are deemed to constitute part of an enterprise carried on in the Netherlands (the income of which is taxable in the Netherlands, in accordance with article 17.3.a CITA) in case the non-resident entity owning the debt claims has a substantial shareholding within the meaning of article 17.3.b CITA. On the basis of Article 13 CITA, domestic entities which are subject to corporation tax are exempt from taxation on the benefits which they receive from their participation, if they hold 5% or more of the shares. The participation exemption is not applicable to non-resident taxpayers with a substantial participation, on the basis of Article 18 CITA.

On the basis of these provisions charities which are resident in the Netherlands but which do not carry on an enterprise are not subject to corporation tax. By contrast, foreign charities which do not carry on an enterprise will pay corporation tax on their income from substantial participations in Dutch companies.

The same difference in treatment exists for charities receiving income from debt claims in respect of the company in which they hold a substantial participation. Dutch charities are exempt from taxation on interest they receive from debt claims on companies in which they hold a substantial interest, if they are not carrying on an enterprise. Foreign charities are taxed on such income, irrespective of whether they are carrying on an enterprise.

The Commission considers that the exemption of domestic charities from taxation on income from substantial participations while taxing such income when received by foreign charities restricts the freedom of establishment of Articles 49, 54 TFEU and 31 and 34 EEA. The Commission considers that it also restricts the freedom of

capital movement of Articles 63 TFEU and 40 EEA, because it is not limited to cases where the participation gives the shareholder a controlling interest in the sense of paragraph 22 of *Baars*, Case C-251/98 of 13 April 2000. The exemption of domestic charities for interest they receive on debt claims in respect of companies in which they hold a substantial participation, whereas charities established elsewhere in the EU or EEA/EFTA States are taxed on such interest also constitutes a restriction of the freedom of capital movement.

#### Background

The request takes the form of a reasoned opinion (the second step of the infringement procedure provided for by Article 258 of the Treaty on the Functioning of the EU (TFEU)). If there is no satisfactory reaction to the reasoned opinion within two months, the Commission may decide to refer the matter to the Court of Justice of the European Union.

The Commission's case reference number is 2008/4577.