

## Tax Alert - Netherlands – Hong Kong Tax Treaty

### **Introduction**

On 22 March 2010, the Netherlands signed a Treaty for the Avoidance of Double Taxation ("**DTA**") with Hong Kong. As a consequence, the Netherlands now ranks among the few countries that have hitherto concluded a tax treaty with Hong Kong. This further underlines the Netherlands' position as one of the world's leading onshore holding jurisdictions.

The DTA offers significant tax benefits to resident entities of both the Netherlands and Hong Kong; most notably through the possibility for tax-free profit repatriation laid down in the DTA. By virtue of the Netherlands' participation exemption and extensive network of tax treaties, it is now possible to tax-free upstream dividends from the source country through the Netherlands to Hong Kong.

The significance of the DTA supersedes the Netherlands – Hong Kong bilateral relationship. Notably, Chinese overseas investments are often structured through Hong Kong. Because the Netherlands on its turn is often used as a hub for investments into Europe, it is expected that by virtue of the DTA Chinese investments into Europe through the Netherlands will significantly increase.

### **Tax-Free Profit Repatriation from the Netherlands**

Under the DTA, the Dutch withholding tax rate on dividend distributions to qualifying Hong Kong residents that are the beneficial owner thereof is reduced from 15% to 0%.

The most notable qualifying residents are:

- (a) a company owning at least 10% of the shares of the Dutch distributing entity, provided that (i) the shares of the recipient are regularly traded on a recognised stock exchange or (ii) at least 50% of the shares of the recipient is owned by a company the shares of which are regularly traded on a recognised stock exchange, provided the latter is a resident of the Netherlands or Hong Kong or of an EU Member State that is entitled to similar or more favourable benefits under a tax treaty with Hong Kong;
- (b) a headquarters company for a multinational corporate group which provides a substantial portion of the overall supervision and administration of the group and which has and exercises, independent discretionary authority to carry out these functions. Guidelines as to the meaning of headquarters company are given in the protocol to the DTA;

- (c) Any other company, provided that the competent authority determines that the establishment, acquisition and maintenance of the company does not have as its main purpose or one of its main purposes to secure the benefits of the reduced withholding tax rate.

Although the inclusion of these comprehensive qualifying resident tests does carve out wholly artificial structures from the benefits under the DTA, in particular the situation under (c) above allows these to be available for genuine business arrangements.

For completeness sake, we note that Hong Kong resident entities not qualifying for the 0% dividend withholding tax rate under the DTA may still enjoy tax-free profit repatriation. In cases where tax-free profit repatriation from the Netherlands is not available by virtue of a tax treaty, it is mostly possible to effectively achieve the same result by interposing a Dutch Cooperative.

The Netherlands does not levy withholding tax on outbound royalty payments or interest payments. This enables Hong Kong residents to route passive income through the Netherlands without source taxation. Hong Kong on its turn also does not impose withholding tax on outbound interest payments. Under the DTA, Hong Kong will furthermore limit its royalty withholding tax to 3%.

### **Additional Benefits**

Non-Dutch resident entities holding more than 5% of the shares in a Dutch company may *inter alia* be subject to Dutch corporate income tax for capital gains realised upon the disposal of the shares of the Dutch company. Under the DTA however, capital gains are solely taxable in the State of which the alienator is a resident. Consequently, Hong Kong resident entities will not be subject to Dutch tax for capital gains upon the disposal of their Dutch resident subsidiaries. Other rules apply for capital gains on immovable property companies. Consequently a disposal of shares in such company result in a Dutch corporate income tax claim, unless (i) the shares being disposed of are quoted on a recognised stock exchange, or (ii) the shares are disposed of within the framework of a reorganisation of such company, a merger, a division or a similar operation, or (iii) such company derives more than 50% of its asset value directly or indirectly from immovable property in which its carries on its business.

The DTA is subject to ratification procedure in the Netherlands. It is expected that the provisions of the DTA will have effect for the Netherlands for taxable years and periods starting on or after 1 January 2011.

*This Tax Alert provides general information with regard to the Netherlands – Hong Kong Tax Treaty only and should not be relied upon without personal advice. For more information please contact Cees-Frans Greeven or Peter Wurzer at +31 70 318 42 00 or e-mail [wurzer@bvvg.nl](mailto:wurzer@bvvg.nl) or [greeven@bvvg.nl](mailto:greeven@bvvg.nl)*

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