UPDATE ON THE DUTCH FISCAL UNITY IN M&A CONTEXT

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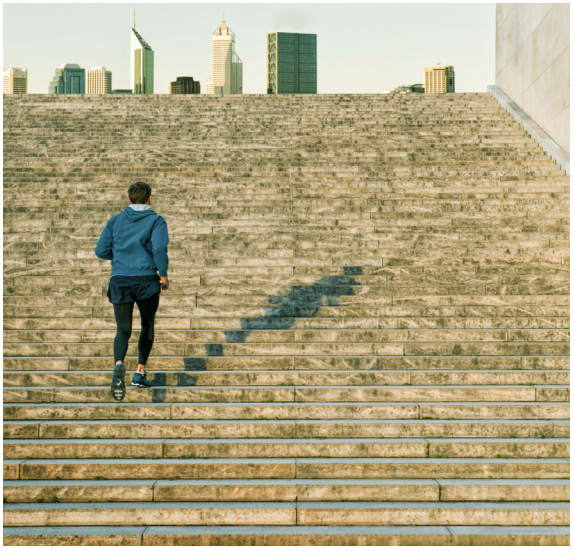
This article highlights the current views of the Dutch State Secretary of Finance set forth in a revised fiscal unity Decree (no.2018/121069), hereinafter "Decree", in particular with respect to the statutory ownership requirement to apply the Dutch fiscal unity regime.

Structured (un)leveraged corporate M&A transactions in the Netherlands involving Dutch resident corporate income tax payers often benefit from a statutory tax facility provided by Dutch tax laws that allows a consolidation for Dutch corporate income tax purposes. Explanatory guidance available to taxpayers of this tax consolidation facility, also known as the fiscal unity, is provided by the Dutch State Secretary of Finance in the Decree. The Dutch State Secretary of Finance issued the Decree on 20 August 2018, which partially amends the existing fiscal unity "Decree" of 14 December 2010 (no. DGB2010/4620M). Below an overview of the highlights.

Fiscal unity

Under Dutch tax law it is possible for corporate income taxpayers upon request to create a fiscal unity (tax consolidated group), in which inter alia inter-company transactions are eliminated for Dutch corporate income tax purposes. A statutory condition is that the ownership – and voting right requirement as referred to article 15, section 1 Dutch corporate income tax act 1969, must be met. This presupposes that there should be a full legal and economic ownership of at least 95% of the shares in the nominal paid-up capital, that this ownership must represent at least 95% of the statutory voting rights and must in all situations represent an entitlement of at least 95% of the profits and equity.



This is a continuous test. Not meeting the ownership requirement results in a termination of the fiscal unity and deconsolidation which often results in adverse tax consequences, such as deemed disposal rules and claw-backs becoming effective.

According to the Decree it is possible in certain situations in which the ownership requirement is not fulfilled, to continue or create a fiscal unity.

Share options

In the view of the Dutch State Secretary of Finance granting share options with respect to the shares of a fiscal unity subsidiary would in principle cause that the ownership – and voting right requirement is not met, because the share option holder becomes (economically) entitled to the assets of the fiscal unity subsidiary and as a result thereof the option grantor does not meet the ownership requirement (anymore).

The Dutch State Secretary of Finance however approves that the granting of share options shall not preclude the creation or continuation of a fiscal unity, provided that the cumulative conditions as prescribed below are met;

- the share option relate to new shares which will be issued by the fiscal unity subsidiary, unless these share options are granted to an employee of the fiscal unity subsidiary;
- the granting of the shares option relate to the business activities of the fiscal unity and is not motivated by other than business reasons;
- uncertainty with respect to the exercise of the share option;
- after granting the share options, the fiscal unity parent company continues to exercise its shareholder rights in the fiscal unity subsidiary and all other requirements to apply the fiscal unity regime are met.

Creating a share pledge

In (un)leveraged transactions when shares are pledged it is essential to analyse the terms of the share pledge as it may jeopardise the voting rights requirements that could result in a deconsolidation.

According to the Dutch State Secretary of Finance the legal ownership – and voting right requirement is not met if a pledgor formally retains the voting rights, but may only exercise the voting rights for certain acts or decisions after consultation with or having obtained approval from the pledgee. The inclusion of such provisions on consultation or approval when establishing a pledge prevents the establishment of the fiscal unity, regardless of whether consultation or approval actually takes place.

The State Secretary of Finance approves that a right of pledge on shares not preclude the creation or continuation of a fiscal unity, provided that the pledgor when exercising the voting rights attached to the shares solely need the consultation or approval of the pledgee with respect to decisions which are solely aimed on maintaining (the value of) the shares as security for the pledgee. Although not ex-haustive the Dutch State Secretary of Finance provides a list of approvals in which the mandatory consultation or approval of the pledgee will not cause the fiscal unity to be discontinued, that is;

- the sale of shares;
- the establishment of (new) security rights for others than the pledgee;
- amendment of the articles of association or liquidation;
- the granting of option rights on the shares;
- issue of new shares;
- redemption of the nominal value of share capital;
- repurchase of shares; or
- merger and demerger of the fiscal unity subsidiary.

Closing and completion mechanisms

When closing a corporate transaction, that is signing of a sale and purchase agreement (“SPA”), and completion, that is transfer of shares, are not scheduled simultaneously, it is customary for parties to negotiate arrangements to ensure e.g. that the buyer acquires control over the target or to manage potential re- or devaluation of the shares. These arrangements often result in a restriction of the ownership – and voting rights of the seller (fiscal unity parent company). As a consequence it may be that the seller will not meet the ownership – and voting right requirement (anymore) which results in a deconsolidation of the target from the fiscal unity.

In the Decree the Dutch State Secretary of Finance acknowledges the aforegoing and aims to address the key issue by providing an approval for this specific situation. The Decree approves a restriction of the voting rights of the seller in case the consultation or approval of the buyer is required, while pending the actual transfer of shares, with respect to certain legal transactions (e.g. dividend distributions and the hiring or dismissal of directors).

This means that the signing of the SPA and preparing interim arrangements by both parties do not jeopardise the continuation of the fiscal unity, however, in order to apply this approval either the fiscal unity parent company (seller) and the fiscal unity subsidiary has to within two weeks after signing the SPA submit a written request with the competent tax inspector.

Any approval granted is in principle valid up to a maximum of three months, however, by means of a written request during this approval period, the period could be extended in case of exceptional circumstances.

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