taxnotes® international

Volume 119, Number 8 ■ August 25, 2025

Dutch Tax Changes Murky on Hybrid Mismatches and Real Estate PEs

by Ashley Peeters and Michael Molenaars

Reprinted from *Tax Notes International*, August 25, 2025, p. 1155

Dutch Tax Changes Murky on Hybrid Mismatches and Real Estate PEs

by Ashley Peeters and Michael Molenaars

Ashley Peeters

Michael Molenaars

Ashley Peeters is a senior associate with Stibbe London, and Michael Molenaars is a partner with Stibbe in Amsterdam.

In this installment of In Step With Stibbe, Peeters and Molenaars review recent developments regarding the lucrative interest regime, explain potential difficulties with the government's new classification rules, and examine discrepancies between pillar 2 and tax treaties over real estate permanent establishments.

Even though the summer is already well underway, new tax developments continue in the Netherlands. This column reviews the important tax developments for investments in the Netherlands.

First, we focus on a Dutch Ministry of Finance research report and a motion adopted by the lower house of the Dutch parliament (Tweede Kamer) on July 3 to change the lucrative interest regime.

Further, in June the MOF published a letter on unintended tax consequences for Dutch funds for joint account following the recent introduction of new entity classification rules. Lastly, we focus on a development regarding the pillar 2 rules application on real estate permanent establishments.

Lucrative Interest Regime

The Netherlands has a special tax regime for the direct or indirect holding of qualifying lucrative interests. The interests can take the form of shares, receivables, or property rights if they are intended as remuneration for activities performed by the holder and offer the holder the opportunity to earn a return with a limited investment that is disproportionate to the capital invested or the risks to be incurred (the leveraged effect).

Lucrative interests are usually obtained as part of a management incentive plan with a "sweet" element that creates the leveraged effect. An example of a lucrative interest is a situation in which there are two classes of shares, of which one (the lucrative class) is subordinated and represents less than 10 percent of the total issued share capital. There may be many other forms of lucrative interests. For example, a lucrative interest is present when property rights are "economically similar or comparable" to the subordinated classes of shares under the catchall category of the regime.

This special tax regime allows for the option, if the lucrative interest is structured indirectly via a substantial shareholding (that is, an interest of at least 5 percent of the shares — or a class of the shares — in an entity holding the lucrative interest), to have income and capital gains taxed under the substantial shareholding regime at a flat rate of 31 percent (2025) (the Box 2 option). Direct

lucrative interests are taxed as ordinary income against progressive Dutch personal income tax rates of up 49.50 percent (2025) (the Box 1 option).

The Box 2 option is often used by private equity managers. In April 2024 the Tweede Kamer adopted a motion urging the government to amend the scheme following a call for equal treatment of private equity managers and individuals whose employment income is generally taxed under Box 1.[1] In response to the motion, the MOF initiated a study of the scheme. It published its findings in the report "Research Lucrative Interest" (Onderzoek Lucratiefbelangregeling) (the report) on February 13.[2]

The report discusses the potential consequences of abolishing the Box 2 option and two alternatives for the lucrative interest regime.

Abolishing the Box 2 Option

The report emphasizes the benefits of the current regime — providing legal certainty and its importance for the Dutch investment climate. A comparison is also made with other jurisdictions surrounding the Netherlands, demonstrating that the overall tax burden is in line with those regimes.

According to the report, abolishing the lucrative interest regime would disrupt the government's well-functioning and collaborative administrative practice, and may result in more taxpayer-tax authority discussions creating uncertainty.

Under its current double tax treaties, the Netherlands can tax income from lucrative interests because it falls under the scope of the article on dividends and capital gains. However, if the regime were abolished, the income would become ordinary income. It is uncertain whether the Netherlands would have the right to tax this income in the case of a non-Dutch manager holding the lucrative interest because it would fall under the scope of income from employment (assuming the employment is carried out in the other jurisdiction). The report therefore concludes that abolishment would not be preferable at this time.

Alternatives

The report discusses two alternatives. The first proposes to embed lucrative interest income in the Dutch wage tax regime. If lucrative income is connected to the employment relationship of individuals, it will be taxed as employment income. If there is no employment relationship, it will be included as deemed income from other activities (*resultaat uit overige werkzaamheden*). Both will be taxed in Box 1 under the higher progressive rate of 49.50 percent (2025). The latter is the main rule for a direct lucrative interest and effectively abolishes the indirect lucrative regime option. It would not be possible to receive income from a lucrative interest in Box 2 or as income from savings and investments.

The second alternative proposes a higher personal income tax rate for indirect lucrative interests. This rate would be in between the current rates of 31 percent and 49.50 percent. The report notes that a higher general rate for all substantial interests (that is, including those that are not lucrative) would be undesirable.

The report concludes that given the potential uncertainty and additional costs, the (indirect) lucrative interest regime should not be changed at this time.

Despite the report's clear conclusions, a member of the Tweede Kamer on June 25 proposed a motion (adopted July 3) to submit a bill as part of the Dutch tax plan 2026 imposing higher taxes on benefits earned by private equity managers that fall under the Box 2 option.[3] The motion refers to the report and the second alternative (described above) and proposes its implementation. A tax rate of 36 percent is proposed to align it with the Box 1 option tax rate. On July 1 the MOF published a letter showing alternatives for the lucrative interest regime.[4] According to the MOF, the motion is "untimely" because amending the lucrative interest regime as of January 1, 2026, would mainly be a political

[1] Motion 25 087, Folkert Idsinga (Apr. 4, 2024) (in Dutch).

[2] Dutch MOF, Research Lucrative Interest (Feb. 2025) (in Dutch).

[3] Amended Motion 25 087, Folkert Idsinga (July 3, 2025). This motion is in line with a motion adopted on Apr. 9, 2024.

[4] Letter from the MOF to the Tweede Kamer (July 1, 2025) (in Dutch).

choice not for the current caretaker government, but for the new government after the elections.

It is uncertain whether the second alternative will be implemented. Although it will likely be part of the Dutch tax plan 2026, it would still need to be adopted by parliament. Elections are planned for October, which will follow publication of the tax plan 2026 in September. It is up to a newly elected parliament and government to decide on whether the current lucrative interest regime will be changed. The expectation is that this will not happen before January 1, 2026. However, it cannot be fully ruled out that as of January 1, 2026, a higher rate of 36 percent may apply to indirect lucrative interests.

Update Dutch Funds for Joint Account

As discussed in our earlier column, new entity classification rules for foreign entities — Dutch limited partnerships (commanditaire vennootschap, or CVs) and funds for joint account (fonds voor gemene rekening, or FGRs) — entered into force on January 1.[5]

According to the new rules, if a foreign entity meets the definition of a nontransparent FGR, no other classifications apply. The foreign entity is then treated as nontransparent for Dutch tax purposes. This means that a foreign limited partnership (for example, a U.S. limited partnership) that is comparable to a Dutch CV (which is tax transparent for Dutch tax purposes, in line with the tax treatment in the foreign jurisdiction) could also meet the definition of an FGR and thus still be treated as nontransparent for Dutch tax purposes (because the FGR classification prevails over the CV classification). Consequently, a hybrid mismatch would still occur, despite the fact that the purpose of the new classification rules is to prevent hybrid mismatches.

This unintended consequence, along with two other unintended consequences that will not be discussed in this article,[6] was already signaled during the discussion of the draft bill on the new entity classification rules. As a result, the Tweede Kamer adopted a motion in December 2024 to further investigate the unintended consequences and look for possible solutions.

Following a public consultation and a roundtable discussion with respondents to the consultation, on June 12 the MOF published a letter in response to the adopted motion (FGR letter).[7]

The FGR letter confirms that the potential for hybrid mismatches involving foreign limited partnerships that qualify as an FGR is not in line with the intention of the new entity classification rules. In response, the MOF reviewed extending the new classification's transitional rules to FGRs to give certain funds more time to restructure, as well as other possible alternative solutions.

One proposed solution is to amend the FGR definition in such a way that foreign limited partnerships could never qualify as FGRs, making hybrid mismatches with FGRs impossible. However, according to the FGR letter, this solution may have adverse consequences for the Dutch tax authorities. The FGR letter describes the situation of a (foreign) investment fund with Dutch real estate that would be transparent because it would not fall under the FGR definition. The Dutch tax authorities would have to tax the participants of these investment funds on Dutch real estate income, but identifying the individuals and their tax position may be challenging. It is noted in the letter that excluding foreign limited partnerships from the FGR definition could also affect the commercial attractiveness and administrative feasibility of larger investment funds because participants would be individually liable for their proportional share in the Dutch real estate and would be required to file a Dutch tax return.

[5] *See* Ashley Peeters and Michael Molenaars, "Update on Dutch Entity Classification and Anti-Base-Erosion Rules," *Tax Notes Int'l*, Dec. 23, 2024, p. 1901.

[6] The other unintended consequences are (i) that by referring to certain definitions in the Dutch Financial Supervision Act, a too-narrow definition of investment fund is created under the entity classification rules; and (ii) that the "investment criterion" (relevant for qualification as an investment fund) depends too much on the underlying facts and circumstances and could therefore result in uncertainty as to whether an investment fund qualifies as a nontransparent FGR.

[7] Letter from the MOF to the Tweede Kamer (June 12, 2025) (in Dutch).

Because the need to tax every participant individually would create new issues and complications, further research is needed, and the letter notes that short-term entity qualifications should be avoided. Although not addressed by the FGR letter, this avoidance may pertain to the prevention of abusive situations in which a taxpayer temporarily opts for transparency to sell underlying investments to ensure that the taxable event takes place at the level of either participants or funds, whichever is more beneficial.

The next step is further research into the opt-in alternative, and an online consultation will be published in the autumn. The FGR letter acknowledges that the current legislation is complicated and that any material changes should not be rushed. Therefore, new legislation is not expected to come into force until January 2027 at the earliest.

Although recognizing the difficulties that arise in practice is a good first step, it seems there is no clear solution and it may take a while before the uncertainty surrounding the qualification of (foreign) limited partnerships and the FGR definition is resolved.

Pillar 2 and PEs

On June 18 Dutch tax authorities published a Knowledge Group Position[8] regarding a Dutch entity that owns foreign real estate leased to a third party. The question is whether the foreign real estate qualifies as a PE for pillar 2 purposes.[9] If there is no PE under pillar 2, the Netherlands will be able to levy a pillar 2 top-up tax. This will not be possible if the foreign real estate is a PE.[10]

In this situation the leasing of real estate to a third party is considered a passive rental investment (the return will not exceed normal asset management). Under the applicable double tax treaty, there is no PE present because passive rentals do not qualify as a PE under the treaty. Therefore, under pillar 2 rules (as implemented in the Netherlands) the entity also, in principle, does not fall under the general definition of a PE because the treaty is based on the OECD model tax treaty. The PE definition under Dutch pillar 2 rules contains a so-called catchall clause that is broader than the definition in the OECD model tax treaty.[11]

In the Knowledge Group Position, it is assessed whether passive rental could result in a PE under the pillar 2 rules' catchall category. The Knowledge Group concludes that passive rental, by its nature, does not involve the carrying out of activities by the group entity in the jurisdiction in which the property is located via a PE or similar establishment. Mere property ownership, when the real estate is leased to a third party, without any other activities in the state in which the real estate is located, cannot be considered as a business establishment and thus does not create a PE.

Because from a Dutch perspective there is no PE in the other jurisdiction under the pillar 2 rules, the Netherlands has the right to impose a top-up tax on the rental income in the other jurisdiction at the level of the Dutch entity. However, this would appear to infringe the common concept that under a double tax treaty only the jurisdiction in which the real estate is located has authority to tax the income. For real estate located in the Netherlands, this may also apply if another jurisdiction applies the pillar 2 rules to a domestic entity holding Dutch real estate. There seems to be a discrepancy between the pillar 2 rules and the treaty application for real estate and the consequences of passively held real estate not qualifying as a PE. This may result in infringements of taxing rights allocation between jurisdictions over real estate.

For now it is important to note that, according to the Dutch tax authorities' Knowledge Group Position, when a Dutch entity is in scope of pillar 2 and holds real estate as a passive investment in another jurisdiction, a potential top-up tax may be applied.

[8] KG:911:2025:2. Within the Dutch tax authorities there are several so-called knowledge groups (kennisgroepen) that specialize in different aspects of Dutch tax law. Tax inspectors may submit cases to these knowledge groups, which then can take a position.

[9] *See* Peeters and Molenaars, *supra* note 5.

[10] The EU minimum tax directive (Council directive (EU) 2022/2523 of Dec. 14, 2022), which was implemented in the Netherlands in 2024 (Wet minimumbelasting 2024).

[11] An informal translation of this catchall category is: a business or similar establishment, other than those referred to in the rest of the definition, through which activities are carried out outside the state in which the entity that includes the net profit or loss in its annual accounts is established, provided that that state exempts the income attributable to those activities (translated from Dutch by the authors).

Conclusion

The Dutch MOF is of the view that the lucrative interest regime does not need to be changed. However, to accommodate the call by some members of parliament for equal treatment of private equity managers, there may be a higher tax burden for lucrative interest in the near future.

Although the new Dutch entity classification rules have provided some certainty to prevent hybrid mismatches, there are unintended consequences for Dutch funds in a joint account that can create new hybrid mismatches. Because of the complex set of rules that apply in this situation, further consideration will be given by the MOF before any changes are made to these rules. This unfortunately results in a longer period of uncertainty for some investment funds.

Lastly, there seems to be a discrepancy between the tax treatment under pillar 2 and under double tax treaties of passively held real estate. This could result in pillar 2 top-up taxes being due in the case of a Dutch entity holding foreign real estate. ■