Netherlands; Brazil; Switzerland

Dutch Supreme Court: Term `Managing Director' Under Tax Treaty with Brazil Must Be Interpreted Formally

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The Dutch Supreme Court (*Hoge Raad der Nederlanden*, the Court) has ruled in Case No. 21/05170 on 21 April 2023. The Court held that the term managing director under the Brazil - Netherlands Income Tax Treaty (1990) must be interpreted formally, meaning that it only applies to individuals who are appointed as statutory directors. Furthermore, the allocation of bonuses to various countries under a salary split requires a direct relationship between the bonuses and the activities carried out in the given countries. Details of the decision are summarized below.

(a) Facts. The taxpayer was a resident of the Netherlands in 2017. From 1 October 2005 until 30 September 2010, he worked for an international group. He was, amongst other things, the managing director of a Dutch holding company ("holding") of that group and of group companies in Singapore, Spain and Switzerland. The taxpayer carried out functions as chairman of a board of directors, CEO, and 'co-managing director' of the holding. The taxpayer performed trading activities in Europe and Asia and attended meetings of company K, an entity responsible for trading activities in South America. He also participated in the weekly meetings of company K online.

The taxpayer received a bonus based on net-results for the activities of company K. The holding paid the bonuses to the taxpayer in 2017 and withheld wage tax and social security contributions.

The holding paid the full amount of the remuneration, the wages which the taxpayer received during his employment and were related to work performed for the group companies in the Netherlands, Singapore, Spain and Switzerland, which were divided over those countries based on a salary split.

(c) Legal background. Article 17 of the Argentina - Netherlands Income and Capital Tax Treaty (1996) and article 16 of the treaty with Brazil provides that directors' fees or other remuneration derived by a resident of a contracting state in his capacity as a member of the board of directors of a company which is a resident of the other contracting state may be taxed in that other state.

Article 17 of the Netherlands - Switzerland Income Tax Treaty (2010) (as amended through 2019) provides that directors' fees received by the members of a board of directors or supervisory board in that capacity from a company resident in Switzerland may be taxed in Switzerland. Based on article 22(3) of the treaty, the Netherlands grants a credit for the avoidance of double taxation for those fees. Article 29(3) of that treaty provides that the former of treaty 1951 continues to have effect for taxable years and periods expired before the time at which the provisions of the new treaty are effective.

(c) Issues. The issues were:

- whether the bonuses received from the Dutch holding for the activities for group company K relate to managerial activities carried out for the companies established in Argentina, Brazil or Switzerland;
- whether those bonuses (partially) can be allocated to the managerial activities in Singapore, Spain and Switzerland based on the salary split; and
- whether those bonuses (partially) can qualify as a compensation for the managerial activities for the Brazilian company controlled by company K.

(d) Decision. The Court of Appeal of the Hague had held that the provision on director fees under the treaty with Argentina and Brazil must be interpreted formally. This means that the taxpayer was not entitled to avoid double taxation, because he was not appointed as a statutory director of the Argentine and Brazilian companies in 2009 and 2010.

The Court also ruled that the taxpayer was not entitled to tax credit for part of the bonuses under the treaty with Switzerland as he could not prove that he has paid taxes in Switzerland. In addition, the Court found that the 2010 treaty with Switzerland applied because the bonuses were paid in 2017.

Finally, the Court decided that the bonuses related to company K cannot be regarded as salary received for activities in Singapore, Spain and Switzerland because there was no sufficient direct link between those bonuses and the activities in the given countries. The taxpayer was not able to prove that the costs of those bonuses were passed on to the companies in those countries.

Consequently, the Supreme Court decided in favour of the tax administration. The text of the Court's decision can be found here (in Dutch only).

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