

Investment funds in the Netherlands

Update 2011



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Preface

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1.1 The Netherlands as an international business location

The Netherlands is renowned globally as one of the premier locations for international business operations. Important factors that contribute to this reputation include a productive, well-educated, multilingual workforce and an excellent financial, operational and technical infrastructure with world-class support services. In addition, the Netherlands has favorable tax incentives, an extensive tax treaty network, and high regulatory standards combined with the flexibility of a small jurisdiction. The continued success of the Netherlands as an investment location is furthermore supported by the positive approach taken by successive governments and the open-minded, dialogue-based attitude of the tax authorities.

In its publication of the global business environment rankings, the Economist Intelligence Unit has rated the Netherlands number seven worldwide for its overall business environment and number three in Europe for the period 2007-2011.

The Dutch financial services industry has a long and distinguished history. Consistent with the Dutch tradition of promoting international trade, the Netherlands is home to the world's oldest stock exchange and to some of the most prestigious international financial firms.

1.2 Why this brochure?

For several decades now, the Netherlands has been the country of choice for many multinational corporations to establish regional headquarters, a treasury department or a holding company. During the last few years, the Netherlands has increasingly positioned itself also as a preferred location for investment funds. We are witnessing a dramatic increase in fund sponsors and asset managers setting up Dutch vehicles for holding international investments, especially in the alternative assets segment.

A number of recent developments have contributed to this popularity boost:

- ▶ The Netherlands has been at the forefront of the 'taking private equity public' trend. Since 2006, several high-profile private equity funds and hedge funds have launched an IPO on the Euronext Amsterdam stock exchange.
- ▶ A new Dutch Financial Supervision Act was introduced in 2007 that provides for a consolidated and flexible regulatory framework for all financial markets.

Several amendments to the Dutch Financial Supervision Act have been published recently, which will enter into effect on 1 January 2012.

- ▶ The Dutch government launched several initiatives in 2007 in order to boost the role of the Netherlands as a financial center within the international and European markets. Several parties are working on that project in close cooperation. Most importantly, the Dutch government has opened the Financial Markets Office. This office forms a single gateway to the government for the financial sector, providing a rapid and effective response to questions about legislation, policy and general information related to financial markets in the Netherlands.
- ▶ Various tax measures have been taken further to improve the competitiveness of the Dutch tax climate. Most importantly, in 2007 the new Exempt Investment Institution vehicle was introduced and the requirements for the preexisting Fiscal Investment Institution vehicle have been relaxed.
- ▶ In July 2007, the Holland Financial Centre foundation was established. This is a joint initiative of various organizations from the financial sector, including banks, insurers, trading firms, pension funds, asset managers, audit firms (including Ernst & Young), law firms and the government. The main purpose of this foundation is to develop initiatives to help ensure that the Dutch financial sector remains strong, open and able to compete on an international level.

These developments present an excellent occasion for publishing a brochure about fund structuring in the Netherlands. The purpose of this brochure is to provide institutional investors, asset managers, fund promoters and their advisors with a general understanding of the advantages of the Netherlands as a location for investment funds, the types of funds available and the main tax, regulatory and reporting aspects.

As you will see, with a number of different beneficial tax regimes to choose from, the Netherlands is positioning itself as a favorable jurisdiction for setting up international investment funds.



Which types of vehicles are available?

2

Various types of legal forms are available in the Netherlands for structuring an international investment portfolio. The main distinction to be made is between corporate entities and noncorporate entities.

2.1 Corporate entities

2.1.1 Limited liability company (BV or NV)

Dutch company law recognizes two types of limited liability companies, the 'naamloze vennootschap' ('NV', the Dutch equivalent of a public limited liability company) and the '*besloten vennootschap met beperkte aansprakelijkheid*' ('BV', the Dutch equivalent of a private limited liability company). Both the NV and the BV are incorporated by execution of a notarial deed.

The BV and the NV are similar in basic characteristics, in the sense that they both have legal personality and a capital divided into shares. The most important distinctions are that:

- ▶ the NV may have bearer shares whereas the BV can only issue registered shares; and
- ▶ the BV's articles of association must contain restrictions on the transfer of shares, which is not compulsory for the NV.

The NV is the entity used for companies the shares of which are to be listed on Euronext in Amsterdam. Unless there is a specific reason to incorporate an NV (e.g., in order to qualify as an ICVC, see 2.1.2), the BV form is usually chosen at the outset. A BV can easily be transformed into an NV, and vice versa.

There is no preference from a Dutch tax perspective for choosing between a BV or an NV. Both types of companies are treated exactly the same for Dutch tax purposes. Depending on the other jurisdictions that are involved in a particular investment structure, there may be a difference from a foreign tax perspective. For example, the Dutch NV - unlike the BV - is regarded as a 'per se corporation' for US tax purposes, which means that it cannot be treated as a flow-through vehicle from a US tax perspective.

Recently, the Dutch government proposed new legislation regarding the BV. The new legislation will provide for simplification and increased flexibility. For example, the minimum capital requirement will be abolished, contributions in kind will no longer require an auditor's statement and the types of share classes that a BV can issue will be expanded. In future it will be possible for a



BV to issue both voting and nonvoting shares, shares that are denominated in a foreign currency, and shares that carry no entitlement to dividends.

2.1.2 Investment company with variable capital (ICVC)

The ICVC is essentially a special subtype of the NV which is specifically geared towards investment companies, in Dutch: the *'beleggingsmaatschappij met veranderlijk kapitaal'*. The main benefit of an ICVC is that it is exempt from certain rules concerning the capital of the corporation. These exemptions relate to the power of the management board to decide on the issuance of new shares, the pre-emptive rights of shareholders, the repurchase of shares and the redemption of shares.

It is possible for an ICVC to act as an umbrella investment fund holding various subfunds each with their own investment strategy by issuing various classes of shares, each representing interests in a distinct portfolio of investments.

Since September 2005, it is no longer required for the shares in the company to be listed on a stock exchange. Instead, the manager of the ICVC must possess a license from the Dutch supervisor (AFM) for the offering of shares in the ICVC. Therefore, this vehicle is not only available for listed funds (as was historically the case), but can now also be used by, for example, nonlisted hedge funds.

2.1.3 Cooperative (Coop)

The Coop is an association established by notarial deed with legal personality. Although the Coop is a legal entity, it shares some characteristics with partnerships, in the sense that there are no minimum capital requirements for a Coop and its capital may be expressed in a different currency than the euro. In many cases, the funds provided by a member to the Coop are entered in a member account in the name of the member similar to a partnership. Under the law, the members each have one vote, but the articles may confer the right to cast more than one vote on certain members. In general, the number of voting rights does not have to correspond with the amount of capital provided by the member.

A Coop may, by its articles, exclude or limit to a maximum, any liability of its members or former members to contribute to a deficit. Most Coops select a system of excluded or limited liability. In case of a system of limited liability, it is also possible to create different classes of members who are each liable to a different extent (or not at all).

When compared to a BV or NV, it is clear that the Coop provides for more flexibility in arranging the rights and obligations of the investors/participants. Also from a Dutch tax perspective, the Coop has an important advantage over a BV or NV: all distributions to investors can be made exempt from Dutch withholding tax, irrespective of the investor's country of residence. This particular feature also distinguishes the Coop from investment vehicles in other countries, that typically require

a complex hybrid financial instrument in order to repatriate cash to the investors without incurring tax.

In order to preserve the dividend withholding tax exemption, the Dutch tax authorities require the membership interests in the Coop not to be freely transferable. It is therefore currently not possible to list a Coop on the stock exchange without jeopardizing this tax benefit. Also because of this transferability restriction imposed by the Dutch tax authorities, the Coop itself usually does not constitute the actual fund vehicle. Instead, the fund is formed as a limited partnership and the Coop is used as the central holding company below the fund. The fund vehicle on top of the Coop can have any form and can be resident in any country, for example a Cayman limited partnership, a Guernsey limited partnership, a Luxembourg FCP, a Dubai investment company, et cetera. It is because of these exceptional features that the Dutch Coop has grown to become the preferred vehicle for structuring international private equity investments over the last few years.

2.2 Noncorporate entities

2.2.1 Limited partnership (CV)

A '*commanditaire vennootschap*' or CV is the Dutch equivalent of a limited partnership, i.e., a contractual arrangement between one or more general partners and one or more limited partners jointly to undertake activities with a view to profit. The general partner of the CV is charged with the management of the CV. The general partner is unlimitedly liable for all actions carried out on behalf of the CV, while the limited partners' liability is limited to their equity investment provided that they do not in any way take part in the management or representation of the partnership vis-à-vis third parties.

In the context of investment funds, the general partner is typically the management company of the fund, while the investors participate as limited partners. There is no requirement for an investment limited partnership to be open to the public.

A CV can be structured as either a transparent or a nontransparent ('opaque') entity for Dutch tax purposes. A tax transparent CV is not subject to corporate tax in the Netherlands and distributions to its partners are not subject to Dutch withholding tax. In addition, provided that the CV is either managed and controlled outside of the Netherlands or provided that the funds' investment strategy does not exceed regular asset management, any Dutch tax liability for foreign investors can be avoided as well. The Dutch tax authorities are generally willing to confirm this by way of an Advance Tax Ruling.

In order to guarantee the Dutch tax transparency of a CV, prior written consent of all partners with respect to the admission or substitution of a limited partner is required. In this respect, consent is deemed to have been given if no participant has refused his consent as regards admission or substitution within four weeks after having been asked in writing.

A CV does not have legal personality under Dutch law. Although it can sue and be sued and contract in its own name, it cannot hold property in its own name. A legislative proposal aimed at enabling Partnerships to elect to have legal personality, was recently cancelled by the Dutch legislator.

2.2.2 Fund for joint account (FGR)

The FGR (in Dutch: '*fonds voor gemene rekening*') is even more flexible than the CV as no mandatory rules apply. It is simply a contractual arrangement between a fund manager, a fund custodian and the investors. An FGR most closely resembles a unit trust as known in common law jurisdictions, although it is neither a body corporate nor a trust and has no legal personality of its own. Instead, the fund custodian holds legal title to the investments on behalf of the FGR's investors.

Similar to a CV, an FGR can be structured as either a transparent or a nontransparent entity for Dutch tax purposes. Tax transparency is typically achieved by providing for prior written consent of all partners with respect to the admission or substitution of an investor. However, unlike a CV, it is also possible for an

FGR to be treated as a transparent vehicle from a Dutch tax perspective if the units may only be issued and redeemed by the fund ('open-ended investment fund'). In that case, prior consent of the other investors is not required.



What kind of tax regime applies?

3

3.1 General tax aspects

Unlike other popular fund jurisdictions, the Netherlands does not levy any stamp duties or other taxes upon capital contributions in an investment vehicle. In addition, no annual subscription tax or net worth tax is levied in the Netherlands. Finally, outbound interest payments are generally not subject to Dutch withholding tax.

With respect to the corporate tax treatment and dividend withholding tax treatment of a Dutch investment fund, three different tax regimes are available:

- ▶ the regular regime;
- ▶ the Fiscal Investment Institution ('FII') regime;
- ▶ the Exempt Investment Institution ('EII') regime.

Whether a particular investment vehicle is eligible for either FII or EII status depends on its legal form and its tax status (transparent or nontransparent). The various possibilities are summarized in the table below.

Type	Legal form	Tax status	Tax regime available
Corporate	BV		Regular/FII
	NV/ICVC		Regular/FII/EII
	Coop		Regular
Noncorporate	CV	Transparent Opaque	n/a Regular
	FGR	Transparent Opaque	n/a Regular/FII/EII

The following paragraphs contain a description of these three tax regimes in more detail.

3.2 Regular tax regime

3.2.1 Corporate tax

By default, all nontransparent entities resident in the Netherlands are subject to Dutch corporate income tax at a rate of 25% (20% for the first EUR 200.000) on all income and gains. It is possible for a Dutch resident entity to calculate its taxable profits on the basis of another currency than the euro, provided that it also prepares its financial accounts in that other currency (see paragraph 5).

Despite the relatively high tax rate of 25%, a nontransparent entity such as a BV without special tax status can still present a tax-efficient vehicle for certain equity investments. This is because of the so-called 'participation exemption'. The Dutch participation exemption provides for an exemption from corporate income tax of any profit derived from a qualifying equity investment in another company, whether domestic or foreign. The profits concerned may be capital gains realized upon sale of the shares (including foreign currency exchange results), or any form of (deemed) distribution of profits by the company. On the other hand, any loss incurred on the shareholding in the other company is generally nondeductible, except if it is liquidated. A Dutch entity can benefit from the participation exemption if it holds at least 5% of the nominal paid-up capital of another company and that other company meets one of the following conditions:

- ▶ The participation is not held as a (deemed) portfolio investment ('motive test'). This motive test should be met if the participation is not merely be held with the

purpose to generate a return that can be expected from normal asset management.

- ▶ The participation is considered a 'qualifying portfolio investment', meaning that (i) the participation is subject to a profit tax resulting in taxation that is reasonable according to Dutch standards ('subject to tax test') and/ or (ii) the aggregated assets of the participation consist for more than 50% of non-portfolio assets or of portfolio investment assets of which the proceeds are taxed at a reasonable tax rate according to Dutch standards ('asset test').

For purposes of the asset test, real estate assets are deemed to be non-portfolio assets.

For private equity funds, venture capital funds, leveraged buy-out funds or real estate funds, a Dutch corporate entity (or opaque, noncorporate entity) can be a very attractive investment vehicle. Due to the participation exemption, all income and gains from the target investments can be collected tax-free in the hands of the Dutch entity.

In case the shareholding drops below the 5% threshold, for whatever reason, the participation exemption continues to be applicable to the remaining shares for three additional years, provided that the minimum 5% stake had been held for at least 12 months. This rule is particularly useful for private equity funds that gradually dispose of an investment instead of through a block sale.

Finally, it is important to realize that the Dutch participation exemption does not require a minimum holding period. Consequently, a capital gain realized upon a sale of a qualifying

participation after, say, seven months will still be exempt from Dutch corporate tax.

3.2.2 Dividend withholding tax

Profit distributions by regular taxable Dutch resident entities are subject to dividend withholding tax at a maximum rate of 15%. However, there are various instances where a reduced withholding tax applies. For example, distributions made by a Coop to its shareholders are completely exempt from dividend withholding tax (see paragraph 2.1.3).

In addition, a 0% withholding tax rate applies in situations where the shareholder is:

- ▶ a taxable entity resident in an EU Member State, Norway, or Iceland holding an interest of at least 5% in the Dutch investment vehicle;
- ▶ an entity that is resident of a country with a tax treaty with the Netherlands that provides for a 0% rate, such as the United States, Japan, Switzerland, Malaysia, Mexico, Singapore, the United Arab Emirates, Barbados, Bahrain, Oman, or Qatar. In this case, a minimum ownership is required (usually 10% or 25%), depending on the specific tax treaty applicable;
- ▶ a tax-exempt qualifying pension fund or non-profit organization that is resident in an EU Member State (by way of a refund mechanism);
- ▶ a US qualifying pension fund or non-profit organization.

3.3 Fiscal Investment Institution (FII)¹

3.3.1 Tax benefits

An investment entity with FII status is subject to Dutch corporate tax at a rate of 0%. But even though no tax is actually payable by the FII, it is considered liable to comprehensive taxation and subject to the tax laws of the Netherlands. Consequently, most countries are willing to grant treaty benefits to a Dutch entity with FII status. This is a very important advantage over the EII regime (see paragraph 3.4) and some tax-exempt investment vehicles in other jurisdictions.

Profit distributions by the FII are subject to 15% Dutch dividend withholding tax but this rate only applies effectively to current income (dividends, interest, rental income). All capital gains realized by the FII can be distributed tax-free to foreign investors. Moreover, the 15% withholding tax rate on current income can be reduced under a tax treaty, sometimes to 0% (e.g., in the case of US pension funds).

EU tax-exempt shareholders (e.g., pension funds and charitable organizations) are eligible for a full refund of Dutch dividend withholding tax. Finally, relief for incurred Dutch and foreign withholding taxes can be provided under certain circumstances by effectively reducing the Dutch dividend tax liability on profit distributions by an FII to its shareholders.

¹ In Dutch: 'fiscale beleggingsinstelling', often abbreviated as 'FBI'.





3.3.2 Requirements

An investment vehicle should meet some conditions in order to be eligible for the FII regime. Some of these conditions depend on the regulatory status of the FII and are discussed in paragraph 3.3.3.

The following requirements should always be satisfied, irrespective of the regulatory status of the FII:

(i) The FII must have a specific legal form:

- ▶ domestic: a BV, NV, or FGR; or
- ▶ foreign: a comparable entity incorporated or formed under the laws of an EU Member State, a tax treaty country with a nondiscrimination clause, the BES Islands, Aruba, Curaçao, or Sint Maarten.

(ii) The FII must exclusively be engaged in portfolio investment activities, i.e., it may not (partly) carry on an active trade or business. Traditional mutual funds should have no problem meeting this test, but private equity funds and opportunistic real estate funds typically do not qualify as their investment style exceeds passive asset management. It is possible to obtain prior clearance from the Dutch tax authorities on this matter. A real estate fund with FII status is allowed to engage in property development for its own investment portfolio, provided that the development activities are carried out in a separate taxable subsidiary. Improvements to existing properties do not qualify as development activities provided that the capital expenditure is less than 30% of the fair value of the property prior to the improvements.

(iii) The FII must distribute its 'distributable' profits annually within eight months after the end of its tax year. The distributable profits only include current income (dividends, interest, rental income). Unrealized gains on securities and realized gains on all other investments do not have to be distributed but can be added to a so-called 'reinvestment reserve'.

(iv) A maximum debt leverage is allowed equal to the sum of 20% of non-real estate assets and 60% of real estate investments (determined on the basis of tax book values). For purposes of these debt leverage restrictions, interests in related companies the assets of which consist for at least 90% of real estate, are regarded as real estate investments.

(v) Dutch resident entities cannot own, together or alone, an interest of 25% or more in the FII through non-Dutch resident entities.

(vi) The FII must distribute its dividends equally to all its shareholders (except in the case of umbrella funds, which may have various classes of shares).

3.3.3 Additional requirements

In addition to the general requirements listed in paragraph 3.3.2, there are some specific conditions regarding the types of investors who may invest in an FII. However, these conditions differ depending on the regulatory status of the FII. The conditions are generally less strict for regulated FIIs than for nonregulated FIIs.

Regulated FII

The category of 'regulated FIIs' for purposes of this rule includes the following funds:

- ▶ funds that are listed on a stock exchange;
- ▶ funds (or their manager) holding a license under the Dutch Financial Supervision Act;
- ▶ foreign UCITS with a European passport.

The shareholder restrictions that apply to regulated FIIs are the following:

- ▶ There cannot be a single corporate (either taxable or tax transparent) shareholder who holds 45% or more of the shares/units issued by the FII (also taking into account any shares/units held by affiliates), with the exception of another regulated FII.
- ▶ No single individual must own an interest of 25% or more in the FII.

Finally, certain restrictions apply for executive and supervisory board members of a regulated FII in order to preserve the FII's independence vis-à-vis its shareholders.

Most importantly, an FII board member cannot also be a board member of a shareholder who holds an interest of 25% or more.

Nonregulated FII

The following shareholder restrictions apply to FIIs that cannot qualify as a regulated FII:

- ▶ The shares/units issued by the FII should be owned for at least 75% by private individuals, tax-exempt entities, and/or regulated FIIs.
- ▶ No private individual may together with his/her partner own an interest of 5% or more.

The restrictions imposed on regulated FIIs with respect to board independence do not apply to nonregulated FIIs.

3.4 Exempt Investment Institution (EII)²

In order to present domestic and foreign asset managers with another alternative for structuring an investment fund, the Netherlands has introduced the EII tax regime. This regime provides for a complete exemption from corporate income tax and dividend withholding tax, very similar to the well-known Luxembourg SICAV. Unlike the FII regime, the EII regime does not involve any minimum distribution requirements. Furthermore, no restrictions apply with regard to the types of shareholders and gearing ratios. On the other hand, contrary to the FII, the EII is not eligible for tax treaty benefits.

The main conditions for a particular fund to qualify for EII status are the following:

(i) The EII must have a specific legal form:

- ▶ domestic: an NV or FGR; or
- ▶ foreign: a comparable entity incorporated or formed under the laws of an EU Member State, a tax treaty country with a nondiscrimination clause, the BES Islands, Aruba, Curaçao, or Sint Maarten.

(ii) The EII must have at least two shareholders or unit holders.

(iii) The EII must have an open-end character, meaning that the shares/units are, at the request of holders, repurchased or redeemed out of the fund's assets.

(iv) The EII must pursue risk diversification. This condition aims to exclude corporate enterprises utilizing an EII subsidiary in support of their regular business operations. Investment funds therefore generally satisfy this test.

(v) The investments must exclusively consist of financial instruments and/or bank deposits.

The term financial instruments includes not only equities, bonds, money market instruments, options and futures, but also cash settled derivative contracts regarding commodities, climate variables, emission licenses, inflation rates or other economic statistics. The EII regime is therefore not open to direct investments in real estate. Moreover, it is not allowed for an EII to invest in Dutch real estate through a partnership that is transparent for tax purposes.

² In Dutch: 'vrijgestelde beleggingsinstelling', or 'VBI'.





Dutch regulatory aspects of investment vehicles

4

Four categories should be distinguished when discussing the regulatory aspects of funds: (i) Undertakings in Collective Investments in Transferrable Securities (“UCITS”), (ii) funds from jurisdiction with adequate supervision, (iii) non-UCITS retail funds, and (iv) exempt funds.

UCITS

The European UCITS IV Directive of 2009 was transposed into the Dutch Financial Supervision Act on 22 July 2011. The UCITS IV regime enables Dutch funds fulfilling the UCITS IV requirements to obtain a European passport, authorising the marketing of such funds in other member states. Non-Dutch UCITS funds have to notify the competent financial regulator in their home member state prior to marketing their participation rights in the Netherlands. The only material action to be taken if foreign UCITS funds are marketed in the Netherlands, is the translation of the funds’ Key Investor Information Documents (“KIID”) into Dutch.

The manager of a UCITS fund requires a separate license. Subject to the completion of notification requirements towards the home member state’s financial regulator, this license may be used as a European passport for the management of UCITS funds domiciled in other member states.

Adequate supervision funds

Managers of investment funds that are established in a jurisdiction that has been designated by the Dutch Minister of Finance as having adequate supervision, do not require licensing in the Netherlands. Instead, they need to complete a notification procedure towards the Dutch Authority for the Financial Markets.

The Dutch Authority for the Financial Markets (“AFM”) will rely solely on supervision carried out by the foreign supervisor.

At present, the following countries have been designated by the Dutch Minister of Finance as having adequate supervision:

- ▶ United States (if the fund is SEC-registered);
- ▶ Luxembourg;
- ▶ Ireland;
- ▶ United Kingdom;
- ▶ France;
- ▶ Guernsey (for Class A and Class B open-end funds and closed-end funds);
- ▶ Jersey;
- ▶ Malta.

This unique regime option has proven to be a very popular route for fund managers who wish to establish a fund in a tax neutral jurisdiction and access a European market in a quick and cost-efficient way by raising capital through a listing on Euronext Amsterdam. In addition, Eurolist by Euronext in Amsterdam is a regulated market as referred to in the EU Markets in Financial Instruments Directive (unlike, for example, the Alternative Investment Market in the UK, that only has exchange-regulated status).

Notwithstanding the exception as described above, adequate supervision funds are still subject to some requirements in the Netherlands with respect to the content of their prospectus, investor reporting, advertising and annual accounts.

Retail funds

Managers of foreign non-UCITS funds which are marketed to the Dutch retail public and are not established in a jurisdiction with adequate supervision require a full Dutch license. This involves the issuance of a prospectus, the issuance of a Key Investor Information Document, capital requirements, screening of directors and organizational requirements. However, if such non-Dutch funds are only marketed to investors in the Netherlands, on the basis of one of the exemptions described below, these licensing requirements do not apply.

Exempt funds

Dutch law provides exemptions on the license requirements for investment funds which satisfy one or more of the following conditions:

- ▶ The fund only markets to 'qualified investors' (i.e., inter alia entities which have a license or are otherwise regulated to be active on the financial markets, large corporate entities, governmental bodies, international and supranational organisations, certain other institutional investors and certain high net worth individuals).
- ▶ The fund is marketed to a maximum of 99 non-qualified investors.
- ▶ The shares or units of the fund have a minimum denomination of € 50,000 or can only be acquired against a minimum consideration of € 50,000. Please note that these threshold amounts will each be increased to € 100,000 as of 1 January 2012, pursuant to an amendment of the Dutch Financial Supervision Act.

Both Dutch funds and non-Dutch funds which are marketed to investors in the Netherlands can rely on the above exemptions. If units or shares are offered on the basis of such an exemption, specific selling restrictions and standardised mandatory warnings (the so called "Wild West Warning") may be required. When applicable these have to be inserted in the fund documentation, prospectuses and marketing materials.

The voluntary supervision regime

Certain institutional investors are limited to investing in regulated funds pursuant to their investment restrictions. From a commercial point of view it may therefore be useful for fund managers to be subject to some level of (governmental) supervision. As described above fund managers do not require a license from the AFM, and are therefore not subject to

its supervision, if the units or shares in their funds are offered exclusively to qualified investors. Pursuant to an amendment to the Dutch Financial Supervision Act, such managers may opt in to voluntary supervision by the AFM. As a consequence the manager obtains a written declaration from the AFM that it is subject to its supervision. The manager is consequentially required to comply with a regulatory light regime. This light regime includes, amongst others, minimum requirements on own capital, liquidity, reliability and experience of the management and the organisation of the business.

The AIFM Directive

The European Alternative Investment Fund Managers Directive requires attention as this will materially reshape the legal framework applicable to the managers of all non-UCITS funds domiciled or marketed in Europe. The directive has entered into force on 21 July 2011 and has to be transposed into Dutch law no later than 22 July 2013. The directive regulates the managers of non-UCITS funds, including hedge funds, private equity funds and real estate funds, if the assets managed by such manager exceed a threshold amount (i.e. €100 M or € 500 M depending on the situation). The directive contains requirements on the general organisation of business, rules of conduct, remuneration, risk management, liquidity management, use of leverage, reporting requirements and the mandatory depositary.



Reporting and audit requirements

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Entities which, pursuant to the Dutch Financial Supervision Act, are not subject to supervision by the Dutch Authority for the Financial Markets or the Dutch Central Bank and which do not have to comply with certain accounting standards given their legal status, are very flexible in preparing their financial reporting. For example, tax transparent FGRs can simply include in their prospectus the set of accounting standards they want to apply, whether it be IFRS, Dutch GAAP or US GAAP, or even a limited set of financial reporting standards suited to the needs of the investors. The timing of the reporting can be defined in the fund rules as well.

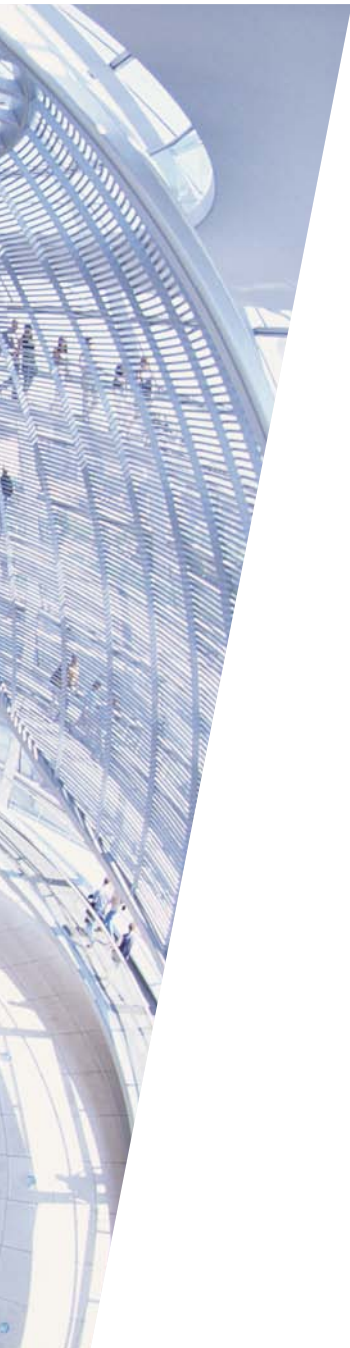
Legal entities such as the BV, NV and ICVC will have to comply with the requirements of the Dutch Civil Code and Dutch GAAP. As long as these entities are not under supervision, they are likely to have limited external reporting requirements under the Dutch Civil Code as they may qualify as 'small' entities. Once a certain size is reached, the reporting requirements are more significant. These entities are allowed to apply IFRS voluntarily.

In general, limited partnerships such as CVs do not have to comply with the requirements of the Dutch Civil Code, although some exceptions do exist. For entities under supervision (for example investment funds making public offerings of securities with a nominal value of less than € 50,000 per security (or € 100,000 as of 1 January 2012, pursuant to an amendment of the Dutch Financial Supervision Act), both semiannual and annual reporting is required. Reporting requirements include reporting on the nature of the investments, details of expenses and related-party transactions. Deadlines for the reporting are 4 months from year-end (and 2 months for the semiannual reporting). An audit of the annual financial statements is required.

Dutch GAAP contains a special rule that is currently not available under IFRS and that is particularly beneficial for private equity funds. Consolidation of subsidiaries is not required if these subsidiaries are held to be sold. This requires that at the acquisition date a clear exit strategy is available that evidences that the subsidiary is only held to be sold at a moment as defined under the exit strategy.

Under Dutch GAAP, the functional currency used for financial reporting is not necessarily the euro. The functional currency should be the currency that best reflects the economic reality of transactions, events and situations that are relevant for the entity. For funds with investments, equity and/or debt instruments in another currency, that currency might qualify as functional currency.





VAT and fund structuring

6

Value Added Tax

('VAT') is a significant consideration for fund structuring. The current standard Dutch VAT rate is 19%, which means that VAT can be a real and considerable cost for funds that are not in a position to recover VAT incurred. However, it is possible to mitigate the VAT cost, for example, by structuring a fund in such a way that the management services provided to it are exempt from VAT (see below 'management fees'). It is also possible, and often useful, to discuss the the fund structure with the Dutch tax authorities in advance to obtain their view regarding the VAT position. This can provide valuable insight regarding the possible VAT implications of the structure.

VAT position of the fund

Before considering mitigation of the VAT incurred, it is important to consider the VAT position of the fund itself. Prior to a decision of the European Court in 2004, it was common practice in the Netherlands not to treat investment funds as taxable persons for VAT purposes , i.e. with no VAT registration requirement but also no VAT recovery. However, following this decision, it became clear that, under certain circumstances, investment funds can qualify as taxable persons.

However, this does not necessarily mean that the fund should charge VAT in respect of its supplies, or that it can recover VAT incurred on costs. This depends on the specific activities of the fund. A fund with an investment portfolio in financial assets (e.g. securities), will generally be making VAT exempt supplies, which will usually restrict the recovery of the VAT it incurs. The VAT recovery position is important, as this can ultimately have an impact on the performance of the fund. It is important, therefore, to try to minimise the amount of VAT incurred.

Management fees

A significant part of a fund's costs may consist of management fees. It is therefore important to establish whether or not such fees are exempt from VAT. European VAT legislation provides for a VAT exemption for the management of special investment funds. This means that no VAT is incurred by such funds on management fees. The implementation of this exemption in Dutch legislation is broad and basically only requires the fund to constitute a 'collectivity'. This requirement is already satisfied if capital has been raised by several (more than one) legal entities or private individuals. The application of this exemption has been challenged in the European Court, which has raised more questions regarding its scope, i.e. it's potential wider application to other types of funds. Indeed, questions are being put to the European Court to

determine if the exemption should apply to the management of pension funds. Discretionary individual asset management is currently regarded as VAT taxable. However, the German Court has referred questions to the European Court asking if the exemption should also apply to individual asset management. Since there are various possibilities for achieving a collectivity of assets (e.g., by pooling arrangements) in the Netherlands, it is possible to secure a VAT exemption for management services. The definition of management has also been questioned by the European Court that decided that the following services fall within the scope of the management exemption:

- ▶ investment management;
- ▶ administration:
 - (a) legal and fund management accounting services;
 - (c) valuation and pricing (including tax returns);
 - (d) regulatory compliance monitoring;
 - (e) maintenance of unit holder register;
 - (f) distribution of income;
 - (g) unit issues and redemptions;
 - (h) contract settlements (including certificate dispatch);
 - (i) record keeping;
- ▶ marketing.

The exemption can apply to services performed by a third-party manager in respect of the administrative management of the funds but only if they form a distinct whole and are specific to, and essential for the management of those funds. A (sub) manager who performs the above services (a)-(i) for a manager/collective investment fund can therefore, in principle, benefit from the exemption.





Which type of investment vehicle should I use?

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In this section we look at various asset classes and fund types to see which vehicle is most appropriate for a particular type of fund. Please note that the overview below is only of an indicative nature and that the optimal choice will depend on a variety of other criteria and requires a careful analysis of the actual situation of an individual fund.

7.1 Retail mutual funds

For mutual funds that are marketed to the public and that invest in listed securities, the Dutch ICVC or nontransparent FGR with either FII or EII status would normally be the logical choice. If tax treaty protection is required (such as with many equity investments), the FII regime is more beneficial than the EII regime as the FII is usually entitled to reduced withholding tax rates (or a compensation from the Dutch tax authorities).

7.2 Money market funds

The same considerations apply here as for regular retail funds. As many money market funds typically do not suffer withholding taxes on the income from their investments, a Dutch ICVC or nontransparent FGR with EII status is normally the right choice.

7.3 Hedge funds

The FII regime may not always be appropriate for hedge funds in view of the maximum gearing of only 20%. The new EII regime, however, presents an interesting opportunity for hedge funds, as it is not subject to any leverage restrictions. The EII is completely exempt from tax. Contrary to similar entities in other countries, a company with EII status is not subject to any license or other regulatory requirements provided the EII adheres to the regular exemptions (e.g., the basis of the minimum nominal value of the units or shares, see paragraph 4). Furthermore, there are no requirements to involve Dutch service providers or otherwise incur costs in the Netherlands.

7.4 Private equity funds

Private equity funds are characterized by the active involvement with regard to the investments, a high risk profile and high expected returns. This means that both the FII and the EII regimes are normally not available for such funds. Instead, the most tax-efficient solution here would be to use a Coop for holding the various investments, provided that the equity stake in the underlying target companies is at least 5%. In that case, all income and gains derived from these investments should normally not be subject to Dutch tax pursuant to the participation exemption. In the event that the shareholding drops below the 5% threshold, for whatever reason, the participation exemption continues to be applicable to the remaining shares for three additional years, provided that the minimum 5% stake had been held for at least 12 months. This rule is particularly useful for private equity funds that gradually dispose of an investment instead of through a block sale. The fund vehicle itself would be a CV or a foreign limited partnership (e.g., Guernsey, Bermuda, Cayman) formed on top of the Coop.

7.5 Fund of funds

A fund of funds is normally best off using an ICVC or FGR with EII status, as this gives maximum flexibility (similar to hedge funds).

7.6 Real estate funds

The appropriate type of vehicle for real estate investments mainly depends on the fund's investment style and the location of the assets.

Core funds have the broadest selection to choose from. They have the possibility to use an entity with EII or FII status, but they can also opt for a regular BV without any special tax regime and rely on the Dutch participation exemption for avoiding any tax leakage. The ultimate choice will depend on whether tax treaty protection is required. Value added and opportunistic funds, on the other hand, are usually not eligible for EII or FII status. They should therefore use a BV or Coop for holding the local property companies and ensure that the participation exemption is applicable.

In case the fund also invests in real estate assets situated in the Netherlands, the EII regime is not available. The FII regime would then typically provide for the most tax-efficient solution, especially for EU and US pension funds.

7.7 Asset pooling funds

Asset pooling allows institutional investors, including pension funds, from several countries to pool their investment assets into a single vehicle, thereby realizing a number of fundamental cost and efficiency benefits. The FGR is an excellent choice as a vehicle for pooling international (pension) assets. The FGR, if properly structured, is treated as a flow-through entity for Dutch tax purposes, so that any favorable tax characteristics of the underlying income are retained at the level of the investors.

The Dutch government has committed itself to promote the FGR as the preferred vehicle for crossborder asset pooling. The Dutch Ministry of Finance is actively approaching foreign fiscal authorities in order to reach an agreement on the local tax treatment of the FGR. In this respect, the FGR is engaged in fierce competition with the Irish CCF and the Luxembourg FCP.

7.8 High-level comparison between the different types of investment vehicles and tax regimes

Tax regime Features	Regular	Transparent	FII	EII
1 Eligible entities	BV, NV, Coop, ICVC, opaque CV, opaque FGR	Transparent CV, transparent FGR	BV, NV, ICVC, opaque FGR	NV, ICVC, opaque FGR
2 Subject to CIT to CIT	25%, but full exemption for income and capital gains from qualifying equity investments	Not applicable	0%	Exempt
3 Subject to dividend WHT	15%, but reduced under tax treaty or domestic exemption (EU corporate entities and pension funds) Coop is exempt	Not applicable	15%, but reduced under tax treaty or domestic exemption	Exempt
4 Eligible for tax treaties	Yes	No	Yes	No
5 Transferability of interests	<ul style="list-style-type: none"> ▶ Some transfer restrictions for BVs ▶ Membership interests of the Coop may not be freely transferable 	Prior written consent of all investors regarding admission or substitution of an investor	Some transfer restrictions for BVs	
6 Distribution obligation	None	None	Distributable profits (excluding capital gains) must be distributed within 8 months after end of tax year	None
7 Shareholders requirements	None	None	Yes, see section 3.3.3	None
8 Subscription tax or capital duty	None	None	None	None



How Ernst & Young can help

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As a firm with a recognized global capability in the investment funds industry, Ernst & Young ensures a truly global service covering all aspects of our clients' businesses. Ernst & Young's global asset management business is supported by over 1,000 staff, including over 230 partners, senior managers and managers who spend virtually all of their time on investment management related clients. We serve over 700 investment advisors globally and audit over 13,000 pooled investment vehicles, including 4,000 investment partnerships and hedge funds. Our global asset management clients include many of the industry's leading public and private businesses.

Through our global network, we can provide expert advice and assistance to promoters proposing to establish an operation in the Netherlands.

Our expertise allows us to provide a wide range of services including:

- ▶ preliminary advice on a suitable structure for a fund to meet the needs of the promoter and target investors;
- ▶ arrangement of introductions and assistance in negotiations with third-party service providers, legal advisors, banks and regulatory authorities;
- ▶ provision of quality audit services;
- ▶ ongoing advice on taxation, accounting and regulatory matters and on general industry developments;
- ▶ specific tax advice on cross-border investments, emerging markets and securities lending; and
- ▶ our associated law firm Holland Van Gijzen can assist in drafting the constitutive documents of any type of Dutch fund.

We have an in-depth understanding of the structural and regulatory issues surrounding the set-up of investment funds in the Netherlands and have the practical experience as well as the capabilities of fund administrators and trustees/custodians.

This brochure and its future updates will be placed at www.ey.nl.

Contact information

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For additional information with respect to this publication, please contact any one of the following:

Taxation

Ton Daniels	+ 31 (0)88-407 12 53	ton.daniels@nl.ey.com
Silvain Niekel	+ 31 (0)88-407 14 37	silvain.niekel@nl.ey.com
John Borsboom	+ 31 (0)88-407 16 57	john.borsboom@nl.ey.com
Arjan van Oostrom	+ 31 (0)88-407 11 13	arjan.van.oostrom@nl.ey.com
Joost Hendrikx	+ 31 (0)88-407 10 42	joost.hendrikx@nl.ey.com

VAT

Lizzie Bijl	+ 31 (0)88-407 85 84	lizzie.bijl@nl.ey.com
Lionel van Rey	+ 31 (0)88-407 10 05	lionel.van.rey@nl.ey.com

Assurance/audit

Jeroen Preijde	+ 31 (0)88-407 16 79	jeroen.preijde@nl.ey.com
Remco Bleijs	+ 31 (0)88-407 39 35	remco.bleijs@nl.ey.com
Zaina Ahmed-Karim	+ 31 (0)88-407 10 51	zaina.karim@nl.ey.com

Legal/regulatory

Alexander Filius	+ 31 (0)88-407 04 12	alexander.filius@hollandlaw.nl
Juan Vervuurt	+ 31 (0)88-407 04 66	juan.vervuurt@hollandlaw.nl

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