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Dutch Supreme Court renders judgment in long-running proceedings on acquisition loans and fraus legis

On September 5, 2025, the Dutch Supreme Court again ruled in the so-called 'Spectacles case' (*'Brillenzaak'*, concerning the takeover of a company in the optical industry), a long-running procedure on tax interest deduction on an acquisition debt. This case has now been brought before the Supreme Court for the second time. So far, the outcome of the proceedings was that the loan granted had to be regarded as an abuse of law – fraus legis – as a result of which the interest expenses could not be deducted. In this judgment, the Supreme Court confirms this conclusion and upholds the earlier judgment of the Amsterdam Court of Appeals. The judgment is also important because it provides a further piece of the puzzle regarding the relationship between the application of Section 10a CITA 1969 and fraus legis.

Background: interest deduction on acquisition loan?

This case concerned a private equity investor that had taken over the shares in the Dutch company in 2011 through an acquisition holding, a Dutch legal entity. The acquisition holding had financed this acquisition partly with a loan it had taken out from its Luxembourg shareholder. The Luxembourg shareholder had in turn financed this by issuing Preferred Equity Certificates ('PECs') to its shareholders – including the private equity fund. The issue under discussion was whether the acquisition holding could deduct interest expenses on the shareholder loan from its taxable profit. Because the acquisition holding had entered into a fiscal unity with the acquired company, these interest expenses would in fact reduce the corporate income tax burden of the acquired group. This case has now been decided by the Supreme Court for the second time.

No interest deduction limitation under anti-base erosion rules

In the earlier phase of the proceedings, the central question was whether the interest deduction should be refused on the basis of the anti-base erosion rules, Section 10a CITA 1969. It was established that, since the loan had been obtained from the Luxembourg 100% shareholder, and had been used for the acquisition of the 'Target company', the loan fell within the scope of the anti-base erosion rules. The question then was whether the financing was business motivated, in particular whether there was a *non-business motivated diversion* of the funds within the group. In the case of a third-party acquisition, as was the case here, this is an essential requirement according to previous case law in order for the interest deduction to be refused under Section 10a CITA 1969.

The Supreme Court had clarified this at an earlier stage of the proceedings there was no such 'diversion' in this case. The Luxembourg shareholder had not obtained the financing of the PECs from *related entities*; each shareholder to whom the PECs had been issued, held a shareholding interest that remained below the threshold to qualify as 'related'. The shareholders were therefore not part of the same 'group' as the acquisition holding, further to which the financing was not 'diverted within the group'. This meant that the financing could be assumed to be business motivated according to the Supreme Court – unless the tax inspector could demonstrate otherwise.

The case was referred back to the Amsterdam Court of Appeals, which also established that there was no such non-business motivated diversion, and therefore the loan could be regarded as business motivated for the purposes of Section 10a CITA 1969.

Although the parties had not lodged an appeal in cassation on this point, the Supreme Court explicitly confirmed that the judgment of the Court of Appeal on this point was correct.

The shareholder loans are considered abuse of law

The anti-base erosion rules are originally a codification and an extension of case law of the Supreme Court, in which certain (financing) structures were classified as fraus legis by the Supreme Court in the 1990s. Prior case law did show that in addition to Section 10a CITA 1969, fraus legis can also be invoked to refuse the interest deduction, but questions remained about the relationship between the statutory rules and fraus legis. For example, the question was whether a loan that had successfully passed the business motivation test of Section 10a(3)(a) CITA 1969 could still be regarded as fraus legis.

Although the Supreme Court initially seemed to suggest in its judgment of March 3, 2023 that this could not be the case, the Supreme Court nuanced this in a later judgment of March 22, 2024 by stating that fraus legis was only excluded if the loan was obtained from an entity that fulfils a 'pivotal financial function' within the group. But how exactly these two judgments relate to each other became the subject of much debate in the tax literature.

In line with the latter judgment of the Supreme Court, the inspector had successfully argued in the proceedings in the Spectacles case that there was an abuse of law, fraus legis. In the view of the Court of Appeals, the intended interest deduction for tax purposes was the decisive reason for the taxpayer to set up the financing and acquisition structure in this specific way; the loan served no other purpose. The interest deduction would therefore be contrary to the spirit and intent of CITA as a whole. In addition, no pivotal financial function was recognized in this structure.

At the Supreme Court, the taxpayer challenged this judgment of fraus legis by the Court of Appeals, arguing that the loan had already passed the test of Section 10a and should therefore not be regarded as fraus legis, in line with the judgment of March 3, 2023. In this second round of appeal of the Spectacles case, the Supreme Court now confirms the line set out in the judgment of March 22, 2024: a loan for which 10a rebuttal evidence – i.e. business motivation – has been successfully provided, can still yield fraus legis. An exception only applies for loans that are provided by an entity with a *pivotal financial function*: if the loan is granted from such a pivotal financial function and passes the test of Section 10a CITA 1969, then fraus legis would be excluded. The loan has to be granted on the basis of the pivotal financial function in the group, and the entity must not function as a conduit company in relation to the loan.

Comments by KPMG Meijburg & Co

Interest deduction in acquisition structures has now frequently been the subject of cases at the Dutch Supreme Court. Some cases, such as the one at hand, have also been brought before the Supreme Court more than once. At the moment, another case (the 'Coffee case'; *'Koffiezaak'*) is ongoing with a similar fact pattern as the Spectacles case, concerning an acquisition loan. Just like in the Spectacles case, the Supreme Court is expected to deliver his second judgment in that case too. In the Coffee case, the taxpayer – on similar grounds as in the present case – takes the position that fraus legis should not apply. So far, in that case, the AG has concluded that the interest deduction – insofar as it relates to the acquisition – can indeed be regarded as fraus legis (ECLI:NL:PHR:2024:182).

The most important conclusion that can be deduced from the judgment at hand, is that loans that fall within the scope of Section 10a CITA 1969 but are regarded as business motivated can nevertheless constitute fraus legis. The Supreme Court reaffirms in line with the judgment of March 22, 2024, that fraus legis is only excluded if the business motivated nature of the loans follows from pivotal financial function. Nevertheless, the Supreme Court also ruled on March 3, 2023 that even a loan originating from a financial pivot can still be non-business motivated if the financial pivot only acts as a 'conduit' with respect to that loan. The Advocate General discussed this exception of acting as a conduit in more detail earlier this year in an opinion on another case (March 28, 2025, ECLI:NL:PHR:2025:386), which case is currently pending at the Supreme Court.

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