Introductory statement Prof. Dr. Jan van de Streek (Professor of Tax Law, University Leiden) | 'Case studies in Member States national tax policies – The Netherlands: implemented national tax reforms and the combat against aggressive tax schemes' | Monday, 28 March 2022

Dear Members of the European Parliament, Dear Chairman of the FISC Subcommittee,

I would like to thank you for inviting me to this public hearing to share my thoughts on the impact of the Dutch national tax reforms in recent years on aggressive tax schemes. I also take the opportunity to give my views on what the Netherlands could do more. In this introductory statement, I will touch upon five recommendations (short list). It goes without saying that many more recommendations can be made.[1]

I. Recent Dutch national tax reforms on aggressive tax schemes

The Netherlands has a long history of facilitating aggressive tax planning by multinational companies. While the Dutch Ministers of Finance in the periods 2012-2017 and 2017-2021 have admitted the existence of this history (under pressure of scandals, media exposure and parliamentary debates), they have explained it as a 'by-product' of a national tax policy aimed at attracting companies and employment. Only in the last period (2017-2021) a major policy shift has taken place. During this period the Netherlands has taken a number of measures that go 'beyond' the implementation of the minimum standards of the OECD/BEPS-project, the amendments of the European directive on administrative cooperation (DAC) and the European anti-tax avoidance directives (ATAD1&2). I would like to briefly highlight three of them:

1. **Introduction of a withholding tax of (currently) 25.8% on outbound interest and royalty payments as from 2021**. This withholding tax applies to payments made to related entities located in (a) jurisdictions listed on the EU blacklist of tax havens and (b) jurisdictions with a nominal tax rate below 9%.
2. **Stopping transfer pricing mismatches leading to nowhere-income as from 2022.** The Netherlands abandoned its long-standing practice of allowing a so-called *unilateral downward adjustment* of taxable profits from commercial profits. This measure responds to a long-standing wish of the European Code of Conduct Group (Business Taxation) dating back to 1999.
3. **Limiting interest deductions to 20% of the earnings before interest, tax, depreciation and amortization (ebitda) as from 2022.**

How can this measures be categorized? The measures show that the Netherlands is moving towards a tax inspector who checks whether the entire profit of a multinational is taxed (**world tax inspector**). This is also reflected in the **Dutch ruling policy changed midway 2019** under which a multinational company cannot longer obtain a tax ruling if the transactions are aimed at avoiding non-Dutch taxes. In my opinion this is all groundbreaking. The Netherlands, as a small country, recently cares about the integrity of the taxation of multinational corporations worldwide.

[1] For example regarding (i) the weak spots of the Dutch dividend withholding tax, (ii) the lack of an anti-fragmentation approach with respect to the € 1 million threshold of the earnings stripping rule, (iii) the lack of combatting abuse of the Dutch participation exemption and (iv) the toothless Dutch CFC-rules.

The budgetary revenue of the first two measures is close to zero (because multinational companies will restructure) and the measures are expected to reduce the tax competitiveness of the Netherlands. So the question arises as to the reasons for this major policy change. I can see two reasons:

1. **Reputational risks**. The Netherlands is increasingly confronted politically by other countries, including the EU, with its non-cooperative tax policies from the past. At the end of the day, these reputational risks also harm the attractiveness of the Netherlands as a place for doing business.
2. **Morality risks**. The phenomenon of the Netherlands as a tax haven for multinational companies eventually has a harmful effect on the tax morale of Dutch citizens and small and medium sized businesses.

To counter both risks, I believe the Netherlands has been willing to say goodbye to two cornerstones of its tax system (i.e. no withholding tax and unilateral downward transfer pricing adjustments).

The third measure - the earnings stripping rule to a maximum of 20% of ebitda - has a (high) budgetary revenue and is also driven by the desire to achieve the ultimate goal of the Dutch corporate tax system, which is to tax the return on Dutch equity of multinational companies. In this context, it is relevant that the additional revenue is **<u>not</u>** used by the Dutch legislator to reduce the corporate tax rate. Instead, **the standard corporate income tax rate** has been **increased from 25% to 25.8%** as from 2022. This has been a major break in trend which has ended the downward fall of the corporate income tax rate over the last decades.

II. What more the Netherlands can do to counter aggressive tax planning (short list)

1. Quick wins to combat Dutch paper box companies

I believe that two simple quick wins can make the Netherlands less attractive for letterbox companies to channel interest, royalties and dividends:

- **Removal of the safe-harbor** in Dutch tax law under which a letterbox company is deemed to have '**appropriate equity**' (€ 2 million[2]). Instead, any amount of sufficient equity should be determined on a case-by-case basis including a functional analysis. The lack of sufficient equity is currently one of the triggers for spontaneously exchanging information with Dutch tax treaty partners about Dutch paper box companies channeling interest and royalties**.**
- **Extension of spontaneous exchange of information** with Dutch tax treaty partners to **Dutch holding companies** distributing dividends.[3]

2. Tackling weak spots of the Dutch withholding tax on interest and royalty payments

The Dutch withholding tax on interest and payments has three major weaknesses that could be addressed:

[2] Or the lower amount of 50% of the outstanding loans or 50% of the royalties to be received annually.
[3] The organization of Dutch tax advisers (Nederlandse Orde van Belastingadviseurs (NOB)) is fiercely lobbying against this extension which gives me impression that it is a quite effective measure.

- **Extension** of the Dutch withholding tax to **all payments** to related entities in tax havens. Currently, the Dutch withholding tax on royalties can be easily circumvented by making the payment part of an intra-group service contract (embedded royalties).
- **Tackling abuse** whereby interest and royalty payments are made to a related entity in a tax haven via a related entity in a non-tax haven. Currently, in principle no abuse is assumed if the entity in the non-tax haven meets the substance requirements (office building + annual wage bill of at least € 100,000).
- **Reversing the removal of the United Arab Emirates and Saudi Arabia from the Dutch list of tax havens** as of 2022. These two countries have been removed by the Dutch Ministry of Finance from the Dutch list of tax havens without any parliamentary debate. The Zakat (property tax) has been incorrectly labeled by the Ministry of Finance as a profit tax with a statutory rate of at least 9%.

3. Increasing the transparency of the Dutch tax ruling practice

According to guidance of the Code of Conduct Group (Business Taxation) the Dutch tax authorities publish anonymous summaries of tax rulings on a regular basis.[4] These rulings include patent box rulings, advance tax rulings (ATR's), advance pricing agreements (APA's) and other rulings with an international character. The summaries are, however, (too) high-level and should be improved in the following ways:

- **More facts and circumstances**.
- **More details on the tax outcome**. Currently, only ranges of the percentage of profits attributed to the Dutch patent box regime are disclosed (for example 45%-60%). With respect to APAs, only the lowest quartile and the highest quartile of a benchmarking study are currently disclosed.

Currently, the published summaries have little added value in the context of transparency. Moreover, these summaries lack potential to restore public trust in the Dutch corporate income tax system.

It is recommended that the summaries also include **agreements** made by multinational companies and the Dutch tax authorities under the **cooperative compliance program (COCO)**. Finally, it is recommended that the Dutch tax authorities produce updated guidance of its ruling practice with, for example, **a summary of experiences or a Q&A**.

4. Abolishment of the Dutch patent box regime

I recommend the **abolishment of the Dutch patent box regime**. According to economic studies, the Dutch patent box regime, like all other patent box regimes, is **<u>not</u> effective in stimulating innovation**:

- A patent box regime only rewards already successful innovations, which are often already protected by a patent.
- For start-up companies, a patent box regime results a competitive <u>dis</u>advantage.

[4] https://www.belastingdienst.nl/wps/wcm/connect/bldcontentnl/standaard_functies/prive/contact/rechten_en_plichten_bij_de_belastingdienst/ruling/ruling.

The Dutch patent box provides for a reduced tax rate of 9% instead of the standard corporate income rate of 25.8%. The tax expenditure for the Dutch innovation box is about **€ 1.5 billion** a year, of which a large part goes to **only a few multinational companies**. A specific problem is that it is **not clear how to determine which part of the profit is attributable to R&D activities**. In 99% of the cases companies conclude a ruling with the Dutch Tax Authorities.

5. Regulation of Dutch tax advisors

The **Dutch Association of Tax Advisers** (Nederlandse Orde van Belastingadviseurs (NOB)) has a long tradition of involvement in aggressive tax planning. This organization seems to have a harder time saying goodbye to these practices than the Dutch government. The organization suffers from a lack of self-reflection, which can be illustrated by three recent examples:

- The ongoing lobbying against all measures that prevent base erosion and profit shifting. For example, the organization repeatedly called for a **Dutch veto in the EU** against the anti-tax avoidance directives (ATAD).
- The organization **struggles to establish a good tax governance code** that expects tax advisors to take into account the spirit of the law and societal views on aggressive tax planning.
- The organization is **reluctant to cooperate with tax authorities** under the Dutch cooperative compliance program (horizontal monitoring). So far, the organization has not been able to conclude a covenant with the Dutch tax authorities.

It is recommended to investigate whether Dutch tax lawyers can be regulated. Without regulation, there seems little chance of a culture change. For example, the organization's executive director recently called the FISC committee chair without any hesitation "a lunatic who should be locked up in prison."

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