The post-BEPS advantages of the Netherlands

Roelof Gerritsen and Ivo Kuipers, both partners at Atlas Tax Lawyers in the Netherlands, look at why the country will remain a prime location for multinationals and foreign investors as governments worldwide transition towards more harmonised tax rules in line with the OECD's BEPS Project.

As we have all witnessed, a lot has happened since 2012, when Atlas Tax Lawyers wrote an article for International Tax review, which highlighted the advantages of a Dutch holding company.

The major changes have come from the OECD and the EU, which have been working hard to increase tax transparency and combat aggressive tax planning.

Today, the tax community is facing major changes at a pace that has not been seen in decades. This makes it a good time for a review, an overview of recent developments and a further outlook. Will the Netherlands remain attractive in the post-BEPS era, and are the advantages still relevant today?

Gateway to Europe

What has not changed over the past couple of years is the Netherlands' top position in the various rankings for the investment climate and doing business, such as the Global Competitiveness Report of the World Economic Forum. Foreign multinationals still choose the Netherlands as a hub for the European market and for its location when choosing a regional headquarters. The Netherlands has clearly maintained its position as a gateway to Europe. As well as having a beneficial tax system, its key success factors are its international business climate, a strong financial sector, its strategic location within Europe, a superior infrastructure, a highly esteemed education system, a multilingual workforce, its quality of life and a pro-business government. These non-tax aspects will become ever more important as the national tax systems across Europe increasingly begin to resemble each other. This will be because of EU initiatives, such as the Anti-Tax Avoidance Directive (ATAD) and the common consolidated corporate tax base (CCCTB) that aim to reduce the discrepancies, but also due to competition between countries.

It is widely expected that the Netherlands will continue to be a prime location for multinational companies and foreign investors. Not only because of the non-tax aspects, but also because of tax features as the business friendly corporate income tax system, attractive innovation and R&D incentives, extensive treaty network, and cooperative tax authorities.

OECD and EU initiatives: The Dutch perspective

The main reason for the OECD's BEPS Action Plan was the growing frustration that the tax rules, at the time, did not reflect the economic reality of globalisation, the growing international trade networks, and the rise of the digital economy. The rules, once designed to avoid double taxation, led to base erosion and evasive tax planning that made use of international mismatches and artificial structures without economic substance.

The main principles of international taxation no longer resulted in a rational allocation of profits. Today, where the income generating assets are located is not the only relevant factor anymore. More important is the question about where people are working who add value to the company and control the risks.

The Netherlands has a proven track record of successfully attracting multinational companies and foreign investors

The view of the Dutch government is clear: we need measures to combat aggressive tax planning and we are prepared to be at the forefront of the discussions and the implementation, but with due regard of a level playing field and the investment climate in the Netherlands.

The Netherlands was among the first countries to implement country-by-country reporting (CbCR) and the common reporting standard (CRS). In addition, under the Dutch presidency, EU member states agreed on the ATAD in June 2016. As a result, many discrepancies between national tax systems will disappear.

With such an open economy, keeping a good investment climate is important for the Netherlands, especially for the economic growth and creation of new jobs. According to Statistics Netherlands (known as CBS in Dutch), multinationals account for 80% of the international trade of goods and 40% of all jobs in the Netherlands.

It is understood that the competition in Europe is severe, especially from countries like the UK, Ireland, Belgium and Switzerland that are announcing measures to attract foreign investors. Despite numerous benefits, the state aid allegations from the European Commission may discourage foreign multinationals from choosing an EU country. This may be beneficial to the UK (after Brexit) and Switzerland.

Economic substance will be key

One of the effects of the recent developments is that the number of mere conduit companies without economic substance will reduce significantly, also in the Netherlands. As a result of the General Anti-Avoidance Rules (GAAR) of the EU and BEPS Action 6 (preventing the granting of treaty benefits in in appropriate circumstances), source countries will be less prepared to apply reduced tax treaty rates.

The policy of the Netherlands is rather straightforward, however. When submitting a corporate income tax return, Dutch conduit companies that have invoked a tax treaty should indicate whether they fulfil the list of minimum substance requirements. If this is not the case, the Dutch Ministry of Finance will actively notify the treaty partner that the Dutch company has indicated that not all substance requirements were met in a particular year. It is then up to the source country to decide if and how this information is used. The Dutch Ministry of Finance believes it is not up to them to deny treaty benefits.

In our view, the fiscal policy in the Netherlands should focus on companies with substance. Companies with less substance should be encouraged to become companies with real economic activities

to become "BEPS proof". This is not only good for the business, but will also create jobs and is good for the economy.

Abolishing dividend withholding tax in corporate structures

When discussing the Netherlands' investment climate with multinationals and foreign investors, the Dutch domestic dividend withholding tax rate of 15% is a point of attention. In September 2016, the Ministry of Finance issued a long expected letter in which it proposed to abolish the withholding tax charged when dividends are distributed to corporate shareholders owning at least 5% and residing in tax treaty countries. So in essence, the exemption under the EU Parent-Subsidiary Directive is extended to all treaty countries. This is good news for investors from jurisdictions such as the US, Canada, China, India and Brazil and will further improve the investment climate of the Netherlands.

In the same letter the Ministry of Finance took the opportunity, as expected, to discourage the use of the cooperatives as a holding company. In the public debate, the use of cooperatives as a holding company to avoid a dividend withholding tax became somewhat controversial lately. The government proposed that holding cooperatives may become subject to dividend withholding tax, like a company with a capital divided into shares, such as a BV. Cooperatives used in active business structures remain exempt from dividend withholding tax. In order to prevent the facilitating the untaxed routing of dividends from the Netherlands to tax havens, there will be rules to combat the improper use. The changes are intended to become effective from January 1 2018.

In our view, the proposal is a good example of the Dutch government's intentions, on the one hand, to combat abusive structures and, on the other hand, to improve the investment climate for active business structures with sufficient economic substance.

Innovation box

The innovation box regulations in the Netherlands have been amended to align with the modified nexus approach n Action 5 of the OECD's BEPS Project. The regime allows companies to have profits derived from (qualifying) IP taxed at an effective 5% corporate income tax rate. The new Dutch innovation box regime distinguishes small and large taxpayers. To qualify for the innovation box regime, both categories of taxpayers must have so-called R&D-declarations for the development of IP. Additionally, large taxpayers need to have patents, software programs or pharmaceutical certifications to qualify for the new innovation box regime. In line with the previous Dutch innovation box regime, the new legislation contains guidance on how to deal with acquired IP. If a taxpayer continues R&D activities relating to acquired IP, the regime can only be applied insofar as these continued R&D-activities result in new IP.

A further outlook

The Netherlands has a proven track record of attracting multinationals and foreign investors. The Dutch government seems to acknowledge this as important for the Dutch economy. The tax laws should support the investment climate policy taking into account the open economy of the Netherlands.

The OECD's concept that profits should be taxed where the value is created and where risks are controlled, encourages the Netherlands to become that jurisdiction for multinationals, or at least the location where key functions will be performed.

Foreign companies with minimal substance should be encouraged to increase the level of activities in the Netherlands, from treasury to logistics and R&D. Given the wide spectrum of beneficial factors (both tax and non-tax), the Netherlands has a good chance that this approach turns out to be successful.

Not only do countries position themselves for the post-BEPS era, multinationals do as well. The fundamental changes may lead to uncertainty for multinationals, however. What will be the effect on their tax structure? The outlines for the announced measures are more or less clear, but the exact implementation of them is not, yet. And perhaps more than ever, reputation management plays an important factor. It can be expected that, contrary to the past when it was more fragmented, in a post-BEPS environment multinationals will likely seek to concentrate their assets, people and functions in one jurisdiction. Countries should create the necessary preconditions to facilitate this.

The Dutch government has announced that it will focus on the following key elements of its tax system: a fully-fledged participation exemption, the absence of withholding taxes on interest and royalty payments, R&D incentives, an extensive treaty network, and its ruling practice. In our view, the easy access to the Dutch tax authorities to discuss the tax consequences remains one of the most important features of the Netherlands.

These features are no longer unique for the Netherlands. The discrepancies between the national tax systems across the EU will disappear and it can be expected that the statutory tax rates will become more important. Competition will shift from the tax base to tax rates.

The Dutch statutory corporate income tax rate of 25% is relatively high. Not surprisingly, there is a strong lobby from the business community to lower this rate. To stay on the shortlists of foreign investors, the government announced plans in autumn 2016 to reduce the corporate income tax rate. It further clearly mentioned that the Netherlands should not become Europe's discounter. Since the Netherlands is facing general elections in March 2017, the question of what to do next will be for the new government to decide.

Apart from the upcoming general elections, the question is what the EU will bring in 2017. In particular the new ATAD proposals concerning the application of anti-hybrid measures towards third countries and the re-launch of the CCCTB.

The 28 finance ministers of the EU Economic and Financial Affairs Council (ECOFIN) did not reach an agreement on the new ATAD and the CCCTB during the last ECOFIN meeting in 2016. In line with the OECD, the standpoint of the Dutch government is that hybrid mismatches involving third countries should be neutralised in the country of residence of the recipient of the payment and not so much in the EU per se. Only if the third country refuses to change its legislation, the EU should deny a deduction of the payment.

Looking ahead

Despite fundamental changes, the Netherlands will keep its attractive investment climate, especially if the corporate income tax rate is reduced and the dividend withholding tax is abolished as anticipated. The tax system is business friendly, there is a good tax treaty network and the Netherlands is a prime location to build the necessary substance to develop new business activities.

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