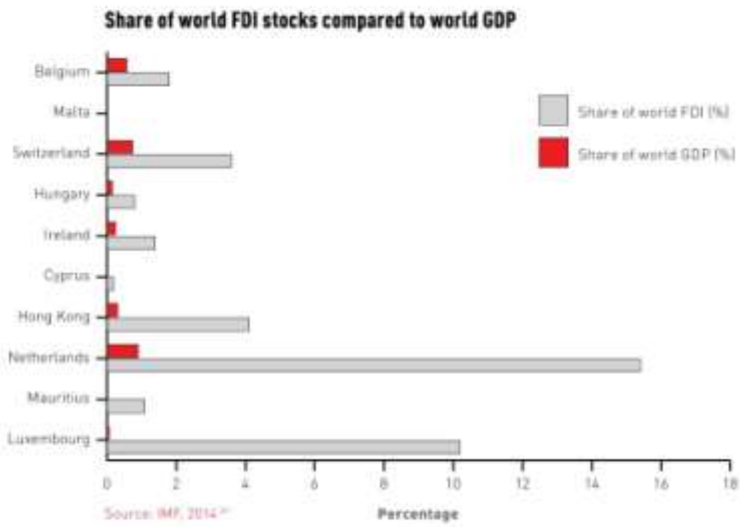
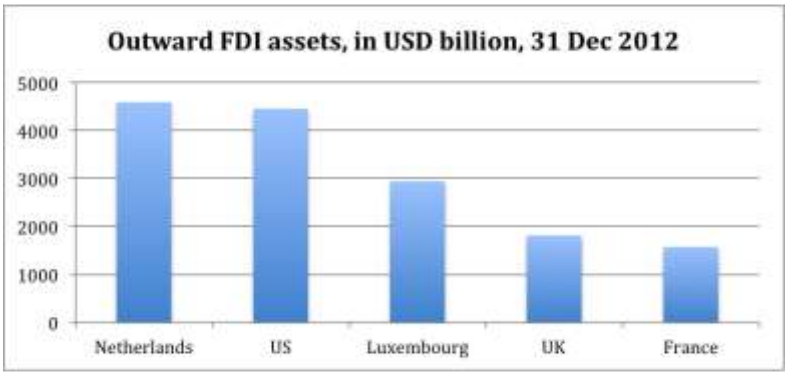
TAXE: Briefing on the Netherlands – 25-05-15

The Dutch model in graphs and key figures

The Netherlands is the world's most important source of FDI, surpassing Luxembourg and the US…





It is the preferred jurisdiction for US multinationals both on number **of subsidiaries and profits booked…**

Figure 1: Percent of Fortune 500 Companies with 2013 Subsidiaries in Twenty Top Tax Havens

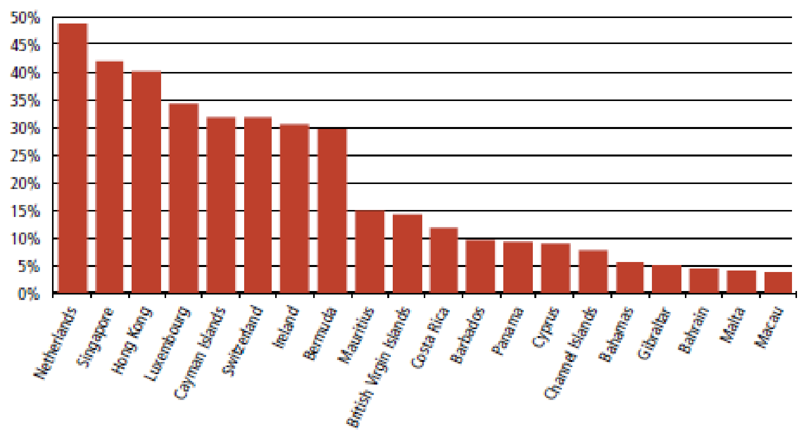
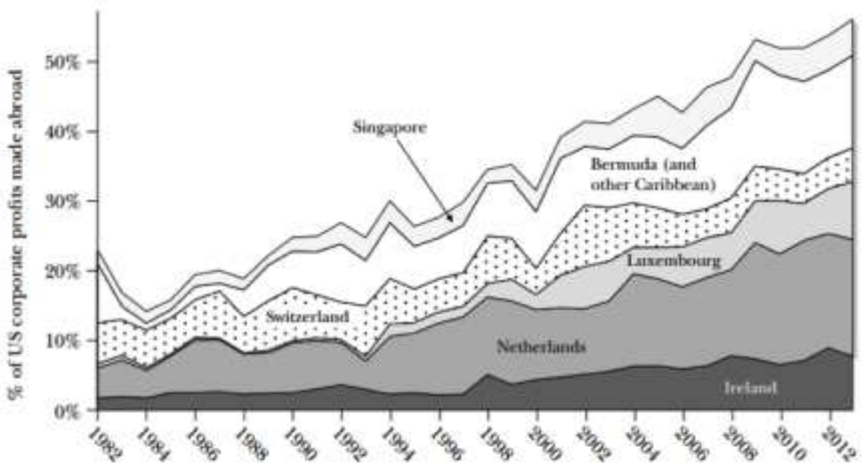


Figure 2
The Share of Tax Havens in US Corporate Profits Made Abroad



Source: Author's computations using balance of payments data. See online Appendix.
Notes: This figure charts the share of income on US direct investment abroad made in the main tax havens. In 2013, total income on US direct investment abroad was about $500 billion. Seventeen percent came from the Netherlands, 8 percent from Luxembourg, etc.

Key figures:

- 76 out of FTSE100 companies have subsidiaries in the Netherlands[i]
- 82 out of the 100 US MNC with the most cash offshore are present in Netherlands.[ii]
- The scale of foreign companies in the Netherlands economy is highly significant, accounting for 55 percent of GDP as compared to only 22 percent in Belgium and 20 percent in Germany. [iii]
- The high number of major multinational companies based in the Netherlands obscures that there is an extreme concentration of funds among only a handful of multinational companies. According to the Commission, around 2/3 of the Netherland's income account can be attributed to only 10 Multinational Companies. [iv] For example, Google alone in 2013 routed through approximately USD 10 bn. through the Netherlands.[v]
- Netherlands is home to approximately 125,000 foundations ("Stichting") of a particular notorious type that obscures the beneficial owner[vi]
- Netherlands is also home to some 23,000 letterbox companies

What is the Dutch model?

The reason for the high concentration of multinational corporations in Netherlands is to be found in the tax treatment available for them. The day after LuxLeaks broke the Dutch Court of Audit released a report on the Dutch tax system which pointed out that the Dutch tax climate for multinational corporations *"does not deviate from other comparable European countries like the United Kingdom, Switzerland and Luxembourg"*.[vii]

The Commission nicely summarises the main features of what makes the Netherland's attractive from a tax perspective in these four factors [my highlights}:

> "The fiscal attractiveness of the Netherlands results from several factors. One of these is the so-called ***'participation exemption'*** that exempts business profits (dividends as well as capital gains) from subsidiary companies abroad from corporate income tax levied in the Netherlands. A second reason is the large Dutch Double Taxation Treaty (DTT) network that substantially reduces withholding taxes on dividends, interests and royalty payments between Treaty countries and the Netherlands. A third reason is the "advance tax ruling" system whereby, contrary to many other countries, the Netherlands offer the possibility to discuss tax positions in advance with the Dutch tax authorities. These discussions can be formalized in agreements binding both the taxpayer and the tax authorities. Fourth, there is a special regime for group financing companies offering very low tax rates on interest received from loans to subsidiaries, while interest payments can be deducted at the tax rate abroad."[viii]

To that can be added a fifth factor which is the favourable treatment of R&D expenditures through the Netherland's patent box regime. Combined these are the broad features of the Dutch model.

Notice that in some very important ways the Netherland's is different from some other traditional tax havens. Its corporate income tax rate is not particularly attractive which is why multinational companies often combine subsidiaries in the Netherlands with subsidiaries in low-tax jurisdictions such as Bermuda. Also its offshore financial sector is relatively modest, accounting for less than 1 percent of the global market for offshore services.[ix] Lastly and related to the small offshore financial sector, the Netherlands has a relatively "clean" image and is largely compliant with most international standards on money-laundering and transparency.[x]

The relatively "clean" image of the Netherlands is however somewhat an illusion.

First, there are its associated territories which have more traditional offshore activities and strict banking secrecy laws.[xi] For example, the Netherlands jurisdiction of Curacao has almost the same secrecy score as Switzerland in the Tax Justice Network's Financial Secrecy Index, while the Netherlands jurisdiction of Aruba has a score similar to Hong Kong.[xii] The importance of these jurisdictions in the offshore world is however relatively modest.

Second, the "clean" image is also challenged from Netherland's own domestic practices. The so-called "Stichting" type of foundation is a case in point. This type of foundation effectively obscures the beneficial owner of the foundation. According to the Wall Street Journal, stichtings are often used in Netherlands to move bank clients' assets of the official balance sheets, away from the scrutiny of tax administrations, but in the process building to the problem of shadow banking. The Wall Street Journal also reports that stichting's have been used to allow both Gadaffi and Russian oligarch's on sanction lists to operate covertly.[xiii]

Dutch letterbox companies

Perhaps the most central feature of the Netherland's model is its many letterbox companies. The most recent figures indicate that the Netherlands is home to some 23,000 letterbox of these companies that have little or no substance in the country. Around 12,000 of these are so-called Special Financial Institutions (SFIs) that are ideal for conduit financing functions (routing of investments), whereby royalties, interests and dividends can be made between subsidiaries within the same company group.[xiv] The tax treatment of these companies largely explains why the Netherlands is the world's largest source of FDI.

First, there is no withholding tax on interests and royalties in Netherlands.

Second, due to the so-called participation exemption dividends from foreign sources are also in effect tax-exempt despite an official 15 percent rate:

> The Dutch participation exemption on cross-border intra-firm dividend payments has been a major attractor of companies to the Netherlands. This exemption implies that when transnational companies repatriate affiliate income, or in other words, pay themselves dividends from abroad, the tax treatment of this income is not subject to domestic taxation19. This has made (and makes) the Netherlands very attractive as an investment base for regional expansion, with many firms setting up their European headquarters.[xv]

Third and related, from 2012 the Netherland's applies a territorial tax system which effectively implies that foreign profits are excluded from the tax base. This system is similar to what Gibraltar is now under investigation for in the current EC state aid case against the small island.

Fourth, the Netherlands allows for consolidation of global losses and gains within a multinational group and have flexible rules for the carry forward of losses, and even allows for losses to be carried back one year[1].[xvi]

Lastly, the many Dutch tax treaties and its access to EU directives ensure that the Netherlands retains a good portion of the taxing right in cross-border taxation with other jurisdictions and that the rates applied are low.

These favourable tax characteristics have led to a massive rise in financial flows through the Netherlands in recent years. According to the Dutch Court of Auditor royalties going through SFIs grew from €5.4 billion in 2003 to €18.5 billion in 2012, while those exiting the Netherlands grew from €4.4 billion to €13.3 billion. In roughly the same period, interest flows through Netherlands-based SFIs doubled. Dividend payments coming into SFIs also increased from €13.1 billion in 2004 to €72.7 billion in 2012, while outgoing dividend payments rose from €25.6 billion to €53.7 billion.[xvii]

The negative effect on other countries' tax bases of these flows are well document. In a recent report, it was found that the authorities in Greece had missed out on at least EUR 1.7 million of tax revenue from one company alone due to its subsidiaries in the Netherlands.[xviii]

Dutch tax rulings

Although statistics on it are very sketchy there is reason to believe that the Netherlands might surpass Luxembourg in terms of number of tax rulings. For example, the Commission's Joint Transfer Pricing Forum (JTPF) has monitored the use of one type of tax rulings in member states – the Advance Pricing Agreements – and found that while Luxembourg entered into 107 of these in 2013 the corresponding number for the Netherlands was 228.[xix] According to the Dutch Court of Auditor the tax office in the Netherlands approved

[1] Carry forward implies that losses in one year can be used to offset profits in subsequent years. So for example, if a company invests 1 bn. in 2011 and has a profit of 500 million in 2012 and 2013, it use the cost of its investment in 2011 to offset its profits in year 2012 and 2013 to make sure that its taxable profits is 0. Carry back of losses works in the same way, just for the accounts of the preceding financial year.

669 tax rulings in 2013.[xx] On average, 420 Advance Tax Rulings and 226 Advance Price Agreement have been issued annually in the period 2010-2014.[xxi]

In its investigation of the Netherlands tax ruling with Starbucks the Commission has noted that:

> The Netherlands seem to generally proceed with a thorough assessment based on comprehensive information required from the tax payer. The Commission therefore does not expect to encounter systematic irregularities in tax rulings.[xxii]

This is in contrast to its findings in some of its other investigations into tax rulings, for example in Ireland where it pointed out that seemed to be little or no real analysis determining the content of the ruling. However, the Commission is at the same time of the opinion that the ruling obtained by Starbucks in Netherlands does in fact constitute selective state aid.

Questions for officials in the Netherlands

- What is the economic rationale for not levying withholding taxes on interests and royalties in the Netherlands?
- Considering that Netherlands is home to tens of thousands of letterbox companies does the government of Netherlands intend to implement a fully public register of the beneficial owners of companies in its transposition of the fourth Anti-Money Laundering Directive? And would the so-called Stichting foundations be covered in the register?
- Considering the very high number of tax rulings granted in the Netherlands and the questions raised about these rulings through the Commission investigation does Netherland consider it useful to publish information from these tax rulings?
- Civil society based in the Netherlands has raised the recommendation to the TAXE committee ahead of our visit here that there should be a requirement for multinational companies operating in the Netherlands to report publicly on a country by country basis. Would the government of the Netherlands support such a requirement for public corporate disclosure?

---

[i] Christian Aid (2014): FTSEcrecy, http://www.christianaid.org.uk/pressoffice/pressreleases/may2014/new-research-reveals-a-black-hole-at-the-heart-of-londons-ftse100.aspx
[ii] Citizens for Tax Justice (2014): Offshore Shell Games
[iii] EC (2015): SWD(2015) 38 final, p.20
[iv] EC (2015): SWD(2015) 38 final, p.24
[v] http://www.customstoday.com.pk/google-shifts-e10b-in-royalties-to-tax-haven-of-bermuda-via-netherlands/
[vi] Wall Street Journal (2015): The rise of the Stichting – An obscure takeover defense, http://www.wsj.com/articles/the-rise-of-the-stichting-an-obscure-takeover-defense-1429716204
[vii] https://euobserver.com/news/126413
[viii] EC (2012): The Dutch current account balance and net international investment position, p.20
[ix] Tax Justice Network (2013): The Financial Secrecy Index - Netherlands
[x] OECD (2013): Global Forum on Transparency and Exchange of Information for Tax Purposes – Netherlands Phase I and II review, http://www.keepeek.com/Digital-Asset-Management/oecd/taxation/global-forum-on-transparency-and-exchange-of-information-for-tax-purposes-peer-reviews-netherlands-2013_9789264205840-en#page1
[xi] http://www.slideshare.net/Homealoneagain/bank-secrecy-in-the-netherlands-antilles-and-aruba
[xii] http://www.financialsecrecyindex.com/introduction/fsi-2013-results

[xiii] Wall Street Journal (2015): The rise of the Stichting – An obscure takeover defense, http://www.wsj.com/articles/the-rise-of-the-stichting-an-obscure-takeover-defense-1429716204
[xiv] SOMO (2013): Private Gain, Public Loss, p.9
[xv] EC (2012): The Dutch current account balance and net international investment position, Economic Papers No.465, p.17
[xvi] PwC (2014): Doing Business in the Netherlands, p.17
[xvii] https://euobserver.com/news/126413
[xviii] http://www.somo.nl/publications-en/Publication_4177?set_language=en
[xix] http://ec.europa.eu/taxation_customs/resources/documents/taxation/company_tax/transfer_pricing/forum/final_apa_statistics_2013_en.pdf
[xx] https://euobserver.com/news/126413
[xxi] TAXE (2015): Documentation for the visit to The Netherlands of the TAXE Committee
[xxii] http://europa.eu/rapid/press-release_IP-14-663_en.htm