

Letter of 5 October 2015 from the State Secretary for Finance, Eric Wiebes, to the House of Representatives presenting an assessment of the outcome of the BEPS Project and the outlook for the Dutch tax climate for businesses

On 5 October 2015 the final action reports of the Base Erosion and Profit Shifting Project ('BEPS reports'), which the OECD drew up at the request of the G20, were published in Paris.

In this letter I will review the BEPS process, present the government's assessment of the proposals and look ahead to the follow-up. Some of the proposed measures are already suitable for implementation in national legislation, while others are better suited to joint implementation. This could be done on an EU level (the Netherlands will hold the EU Presidency in the first half of 2016), but also on a broader level.

I will also discuss how possible measures might impact the Dutch tax climate for international businesses and outline the government's vision on the future of the Dutch tax climate.

1. The BEPS Project process

1.1 Background

The fight against tax avoidance by means of base erosion and profit shifting has never received as much attention as it is getting today. There is a reason for this. Falling tax revenues and reports about tax avoidance are putting pressure on countries' tax rules. These rules date from another era. They are mainly aimed at nationally operating companies and are not sufficiently harmonised. They therefore make it possible for multinational companies to avoid taxes. The rapid rise of globalisation and the changes in business models have increased that risk. New rules will allow a better response to the new circumstances and will be fairer and more robust. In this regard, global agreements are important for governments, individuals and businesses alike. They guarantee fair competition and prevent countries from taking uncoordinated, unilateral action. In view of the major public interest at stake and the desire for global, coordinated agreements, the G20 embraced the OECD's ambitious BEPS Action Plan in September 2013. The outcomes of that Action Plan have now been presented.

1.2. The involvement of developing countries

The BEPS Project is also of major importance for the fight against tax avoidance in developing countries. The involvement of a large number of countries, including both developed and developing nations, makes the project unique. Over 80 non-OECD countries were consulted during the project. Consultations were held with developing countries in 2014. Following this phase, and partly at the insistence of and with the support of the Netherlands, 14 developing countries and several regional bodies representing developing countries took part in the OECD's Committee on Fiscal Affairs (CFA) and various BEPS working groups. As a result, developing countries were more closely involved in BEPS Project discussions and decision-making this year and were able to take part on the same footing as OECD countries. Although the interests of developing countries and developed countries in protecting the tax base often do not differ, developing countries' close involvement in the BEPS Project enabled them to leave their mark on the outcomes. Alongside their involvement in decision-making, they were also given technical support during the project. In consultation with developing countries, the OECD is drafting manuals on the main BEPS outcomes, to ensure that developing countries can actually implement them.

Measures against base erosion through internal royalty and interest flows, treaty abuse and the lack of relevant information on taxpayers are particularly important for developing countries. The BEPS Project has put forward proposals for far-reaching countermeasures. It is of course up to these countries themselves to implement the measures, but the Netherlands is already well on the way to improving tax treaties with them by including anti-abuse provisions.

In the framework of the Addis Tax Initiative launched at the Financing for Development Conference in Addis Ababa, in which the Netherlands played a leading role, a group of 18 donors agreed to double funding for technical assistance no later than 2020.¹ Technical assistance is aimed at creating an effective tax system, partly through implementation of the new standards, and also at strengthening national and local tax authorities. The Netherlands is actively contributing to projects such as the OECD Tax and Development Programme and the Tax Inspectors without Borders initiative. In addition, bilateral activities are being carried out in several countries and the Netherlands is taking part in various multilateral

¹ Letter of 3 September 2015 from the Minister for Foreign Trade and Development Cooperation, Parliamentary Papers, House of Representatives, 2014/15, 32605, no. 171.

programmes. Technical assistance will be needed for several more years, and the Netherlands will maintain its active commitment in this area. See earlier letters sent to you by the Minister for Foreign Trade and Development Cooperation and myself.²

There have been minor changes to the state of play outlined in my letter of 2 June 2015 regarding the renegotiation of tax treaties with 23 developing countries. For an overview, see annexe 2 to this letter.

1.3. The result

The BEPS result comprises the conclusions on the 15 BEPS actions and builds on the interim reports from 2014.³ In annexe 1 to this letter, I discuss all the actions and provide a more detailed government assessment of them. The reports are available at: <http://www.oecd.org/tax/aggressive/beps-2015-final-reports.htm>.

The conclusions on the 15 actions take various forms, each with its own level of consensus, and they are not all equally binding on the countries concerned.

The least far-reaching conclusions are those providing guidance based on best practices; the idea is that they should provide a common basis for any measures that countries eventually introduce. Such guidance has been drawn up for the taxation of controlled foreign companies (CFCs) and for the requirement that taxpayers disclose their aggressive tax planning arrangements in advance.

Slightly more far-reaching are agreements on a common approach to tax planning arrangements. The countries concerned agree that something needs to be done, and a common approach is intended to ensure that national rules are harmonised. This includes agreements on combating hybrid mismatches and on limiting excessive interest deductions.

² Letter of 19 September 2014, Parliamentary Papers, House of Representatives, 2014/15, 34 000 XVII, no. 4, and letter of 18 June 2015, Parliamentary Papers, House of Representatives, 2014/15, 25087, no. 104.

³ I informed your House about these reports by letter of 16 September 2014, Parliamentary Papers, House of Representatives, 2014/15, 25087, no. 77.

The most far-reaching conclusions are those taking the form of a minimum standard. Countries have committed themselves to these standards. Minimum standards have been drawn up for:

- countering harmful tax practices by
 - modifying patent boxes;
 - exchanging information on rulings;
- preventing treaty abuse;
- implementing country-by-country reporting;
- improving dispute resolution.

Improved agreements have been made in the framework of the OECD Transfer Pricing Guidelines for intra-group transactions.

In addition to the minimum standard agreed for preventing treaty abuse, the criteria for defining a permanent establishment in the OECD Model Convention will be amended.

The report also contains conclusions in two areas that will not immediately lead to legislative measures in the countries concerned: special attention for the digital economy, and measuring the extent of BEPS and the effects of the measures.

Action 15 is about implementation. Now that there is more clarity on the measures to be taken, an ad hoc BEPS working group will start considering the scope for developing a multilateral instrument that includes several BEPS agreements.

1.4. Follow-up

When presenting the BEPS Action Plan, the OECD issued an explanatory statement. It emphasises that the measures constitute a coherent whole and underlines the importance of the next steps: implementation, monitoring implementation and continuing to involve as many countries as possible, including developing countries. The OECD rightly assumes that the experiences of the Global Forum on Transparency and Exchange of Information for Tax Purposes can be used to secure worldwide support and involvement. The passages on implementation express the difficulty of finding a balance between national sovereignty and shared responsibility. The government, too, recognises the importance of both aspects and will seek to strike the right balance during its follow-up action. A similar consideration applies to the development of a monitoring process. On the one hand, the agreements have little point if countries do not hold one another to account on the matter of timely implementation.

On the other hand, such a process can threaten national sovereignty, especially if it becomes too political. No concrete agreements have yet been made on monitoring.

2. Government assessment

The BEPS reports present standards and solutions for tackling tax avoidance in an impressive number of areas. The government believes that combating international tax avoidance and abuse is socially desirable and that measures are unavoidable. At the same time, we must ensure that fair competition and employment in the Netherlands are safeguarded. Effective new standards can therefore be adopted only on the basis of international consensus. In this case this approach has been successful, as the BEPS result shows.

The new standards are aligned with the principles which underpin the Dutch system. Our system has always taken account of companies that operate internationally, and ensures that national and multinational companies are treated equally. The participation exemption, the absence of withholding tax on interest and royalties, our extensive treaty network and providing certainty in advance are therefore not in themselves up for discussion. The proposed measures also clearly illustrate that the Netherlands is playing a pioneering role when it comes to exchanging information and including anti-abuse provisions in treaties.

Inevitably, it will also have to amend certain national rules so that, for example, its tax system is better aligned with those of other countries. This may meet with resistance, but resistance alone will place us in an unsustainable, isolated position, and this could unnecessarily damage the Netherlands' reputation. That is why we must participate, in a considered manner, in coordinated and binding international changes.

Where the actual budgetary revenue generated by BEPS goes hand-in-hand with an unintended deterioration in the Dutch tax climate for businesses, the government intends, where possible, to use that revenue for specific measures to ensure that the tax climate remains as attractive as possible. In this regard, it will take account of the BEPS revenue target: €202 million in 2017, falling to €43 million on a structural basis from 2024. This target serves to balance the government's budgeted revenue for 2017 and beyond. Without prejudice to the above, the government will honour the undertaking it gave in its letter of 1

December 2014:⁴ any funds released by limiting the innovation box will be used to preserve an attractive tax climate for innovative businesses in the Netherlands.

In my letter of 2 June 2015,⁵ I roughly classified BEPS topics and international tax issues according to the risk of abuse and the risk of unnecessary harm to the real economy. I will do this again below. The measures are arranged vertically according to the extent to which they contribute to preventing abuse. Incidentally, this is not always easy to determine. For instance, exchanging information on rulings is placed at the bottom because rulings by the Dutch Tax Administration will always be in line with the law, policy and case law. At the same time, the exchange of information is important for ensuring that the same facts are known in both countries concerned. The measures are arranged horizontally according to the extent to which there is a risk of non-targeted measures harming the real economy. First and foremost, this refers to distortions caused by double taxation. The government recognises that greater transparency will increase the administrative burden and implementation costs, which may be experienced as a hindrance. This, too, will be taken into consideration when implementing the measures.

The first box in the figure lists the areas where the government wants to amend Dutch legislation or its aims in treaty negotiations in the light of the BEPS Project. I assume that the other BEPS Project partners will make similar efforts. The second box lists the issues requiring further discussion internationally. My strong preference is to do this multilaterally and to draw up binding European rules, for instance. The third box lists the areas where the government will continue to promote and strengthen current Dutch policy.

⁴ Parliamentary Papers, House of Representatives, 2014/15, 25 087, no. 80.

⁵ Parliamentary Papers, House of Representatives 2014/15, 25087, no. 102.

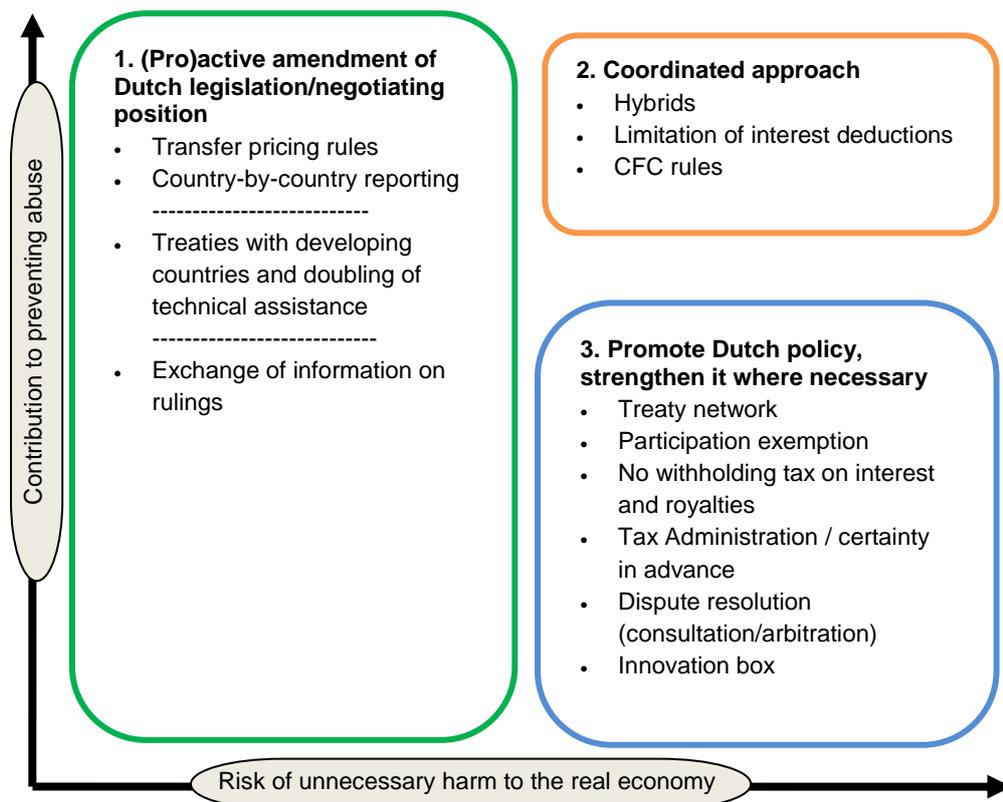


Figure 1: International tax issues and BEPS topics classified according to their contribution to preventing abuse and the risk of unnecessary harm to the real economy.

2.1. (Pro)active amendment of Dutch legislation/treaties

The government sees transparency and automatic exchange of tax information as a key weapon against tax avoidance. This is because transparency and exchange of tax information enable other countries to apply their own tax rules more effectively. The BEPS reports contain a minimum standard for the mandatory spontaneous exchange of information on rulings (action 5). The Netherlands aims to play a leading role in this regard. The Tax Administration will already start exchanging information on rulings on the basis of this OECD standard in 2016. On 14 July 2015 the Netherlands and Germany signed an agreement to begin the spontaneous exchange of information on rulings as soon as possible.⁶ The Netherlands also supports the European Commission's initiative on the automatic exchange

⁶ Order of the State Secretary for Finance of 14 July 2015, Government Gazette 2015, 21781.

of information on rulings. However, steps must be taken to ensure that the implementation costs remain proportionate to the expected benefits.

As regards transparency, the BEPS reports also contain a minimum standard for country-by-country reporting (action 13). In this regard, the government has already presented legislation to parliament, which should enter into force on 1 January 2016. This legislation will, among other things, require companies to notify tax authorities annually of the countries in which they declare their profits and how much tax they pay in which country.

The BEPS Project has also resulted in changes to the OECD rules on transfer pricing. In practice, these changes will barely affect how the Tax Administration applies the OECD's transfer pricing rules, as Dutch policy is already almost completely in line with the new rules.⁷ The Netherlands has clearly explained and promoted its policy convincingly. I am happy that other countries will now apply these rules as well.

Under action 6, a minimum standard has been agreed to prevent treaty abuse, and action 7 has led to new criteria for defining a permanent establishment. These new criteria will be incorporated into the next update of the OECD Model Convention.

The government will adopt the minimum standards for preventing treaty abuse (action 6) right away. This ties in with the Netherlands' commitment to include anti-abuse provisions in recent treaties. The government will also seek adoption of the recommendation on permanent establishments (action 7) in its negotiations on tax treaties.

2.2. Possible changes by means of a coordinated approach

In box 2 (coordinated approach) in the above figure, I indicate measures which I firmly believe should be fleshed out at multilateral or EU level. On a number of points important to the Netherlands, BEPS action plans fall short of providing minimum standards. These include action 2 on hybrid mismatch arrangements, action 3 on CFC rules and action 4 on limiting interest deductions. The Netherlands recognises the need to implement actions in these areas. It is therefore important, in the government's view, to formulate binding European rules on these issues at EU level. Legislating unilaterally on these relatively 'non-committal'

⁷ See the most recent transfer pricing order: order of 14 November 2013, IFZ 2013-184M, Government Gazette 2013, 32854.

BEPS outcomes would not be effective. Nor would it be conducive to a level playing field in the EU and beyond.

The European Commission ('the Commission') also takes the view that a number of BEPS issues are suited, in the absence of sufficient agreement at global level, to being further developed by the EU, either in the context of the common consolidated corporate tax base (CCCTB) or otherwise. The Communication 'A Fair and Efficient Corporate Tax System in the European Union: 5 Key Areas for Action' ('the EU action plan'), presented on 17 June 2015, addresses broadly the same subjects. The scope for further developing these subjects in a directive will be explored in the coming months. The Netherlands will continue to press for binding EU legislation during its EU Presidency in the first half of 2016.

Even more is happening in the multilateral arena, as indicated in section 1.3 above. In the coming months countries will be working within the OECD on a multilateral instrument: a treaty that, at a stroke, will implement the treaty-related BEPS outcomes in as many existing treaties as possible. The Netherlands is playing an active part in this effort.

2.3. Promoting Dutch policy

In box 3, 'Promote Dutch policy, strengthen it where necessary', I list the main strengths of the Dutch tax system. While these strengths entail a – limited – risk of abuse, unfocused and disproportionate countermeasures could have major consequences for the Dutch tax climate for businesses. The Netherlands has promoted these features of its tax system during discussions within the OECD and the EU, and will continue to do so in the future. The government considers the main strong points of our tax system to be our extensive treaty network, the participation exemption, absence of withholding tax on interest and royalties, our efficient Tax Administration and our efficient dispute resolution procedures. These elements help to create a transparent, clear and attractive tax climate for international businesses. Where the BEPS reports touch on these advantages, the government is prepared to make them more robust to prevent abuses. As I said in section 1, the government will henceforth incorporate the results of actions 6 (treaty abuse) and 7 (permanent establishments) in Dutch treaty policy.

The Netherlands already meets the minimum standard for dispute resolution (action 14). From the outset the Netherlands has called for improvements to dispute resolution procedures and it will continue, within the OECD and the EU, to urge other countries to meet those requirements so that Dutch businesses wishing to invest abroad are not unnecessarily

burdened by stricter measures. This endeavour is consistent with the transparent and approachable stance taken by the Dutch Tax Administration.

The BEPS report on action 5 gives a minimum standard for the design of patent boxes like the Dutch innovation box. The government sees the innovation box as an important tool to promote successful innovative activities and high-value employment in the Netherlands. However, concerns have been expressed internationally that preferential regimes can lead to tax avoidance. In 2014 the United Kingdom and Germany reached a compromise, which enjoyed widespread backing, on the requirements that patent boxes should meet. Its main focus was on strictly limiting incentives to 'patent or patent-like' innovations. The government took the view that this compromise was too restrictive to permit tax incentives for innovation that were sufficiently broad in scope. This entailed the risk that SMEs, for whom patent applications are often not a viable proposition, would miss out. Moreover, there are some industries, like software, in which patents are rare, but which do produce genuine innovations. In consultation with the House, the government has sought to have the compromise broadened, so that SMEs do not miss out. The business community has echoed this call for broader eligibility criteria for innovations. I note that the OECD outcomes meet the Netherlands' wishes in this respect. Not only patents, but also software innovations and plant breeders' rights would qualify for tax benefits under the innovation box. In addition, SMEs would continue to qualify for the innovation box on the basis of a declaration under the Research and Development (Incentives) Act. I would be pleased to discuss the practical implications with the House.

3. Outlook

3.1. The Dutch tax climate for businesses

The Dutch tax system has a long-standing international focus. Foreign markets are vitally important for businesses from a small country with an open economy, like the Netherlands. To achieve similar economy of scale as multinationals in larger countries, it is especially important for Dutch companies to do business across borders. This international focus is reflected in our tax system, e.g. in the participation exemption and the absence of withholding tax on interest and royalties. This enables Dutch businesses based in the Netherlands to compete fairly with businesses based in other countries and vice versa. The international focus of the tax climate also finds expression in the almost 100 tax treaties that the Netherlands has signed. These treaties avoid double taxation and so provide companies operating internationally with legal certainty, which is of great practical importance to both

individuals and businesses. Businesses also benefit from the efficiency of the Dutch Tax Administration. It is consistent, approachable, transparent and focused on finding solutions within the parameters laid down in legislation, policy and case law. This includes giving businesses certainty in advance on proposed juridical acts.

The Netherlands has also built up good relations with many tax authorities in other countries. This is especially true of mutual agreement procedures. The Netherlands has successfully concluded many of these procedures and is increasingly concluding bilateral advance pricing agreements (APAs) together with other countries. This prevents double taxation and provides certainty for businesses in both countries that are party to the agreement. The government wishes to maintain and to continue promoting these good relations and arrangements.

The aforementioned characteristics make the Netherlands an attractive location for international businesses. It goes without saying that other factors, unrelated to tax, also play an important role. These include our excellent infrastructure and highly educated labour force. Many international companies have come to the Netherlands in recent years to set up (regional) head offices, offices, distribution centres, marketing and sales offices, R&D units, service centres or other subsidiaries. This has created many jobs. More than 15% of the Dutch labour force works for 'foreign' companies. Clearly this constitutes a very important contribution to the Dutch economy. I therefore believe it is crucial that the Netherlands remain an attractive location for the head offices of companies and - foreign and domestic - businesses performing real economic activities.

However, we need to remember the old adage 'If you stand still you go backwards.' If the Netherlands does not keep up with international trends for attracting businesses, it will get left behind. And if the Netherlands unilaterally implements a number of BEPS outcomes that increase the tax burden, the Netherlands could become less attractive than other countries in the future. Therefore, in order to safeguard employment in the future, I would like to explore, in consultation with the House and key stakeholders, how we can ensure that after the BEPS measures have been introduced the Netherlands remains attractive to head offices and other companies performing real economic activities. In cases where the introduction of BEPS measures gives rise to undesirable or unintended increases in the tax burden I will, taking into account the BEPS revenue target, seek to identify compensatory measures. This could mean lowering the headline rate of corporation tax, changing the corporation tax rate structure, a separate box within the corporate income tax regime, changes to dividend withholding tax, or a combination of these measures.

3.2. The EU and the Dutch Presidency

I have indicated that the best way of fleshing out various BEPS actions is by means of international coordination and binding agreements. Where global agreements are currently not feasible, it is natural to consider measures at EU level. On 6 July this year I sent you an assessment of the Commission's EU action plan of 17 June 2015. In that plan, the Commission sets out its vision on the future of corporate taxation in the EU. The Commission envisages a phased introduction of the CCCTB, starting with measures stemming largely from the BEPS actions, e.g. on hybrid mismatches, CFC rules, interest deduction limitations, and permanent establishments.

The Commission believes that the Council should reach agreement on these measures within 12 months and that this agreement should be made legally binding prior to the conclusion of an agreement on the revised CCCTB. Developing these measures further will be a key issue for the current Luxembourg and upcoming Dutch Presidencies.

I share the Commission's ambition to pursue these matters and draw up binding rules on them. This will guarantee a level playing field in the EU. Harmonisation may provide a solution in cases where differences between tax systems are exploited in an undesirable way. This should be the limit of harmonisation and there is no need to strive for consolidation. Strict and binding rules that apply only in the EU risk making the EU as a whole less attractive for investment. The EU would put itself at a disadvantage compared with the rest of the world. We must not lose sight of this risk, and I will make sure we keep it in mind during the Dutch Presidency.

4. Conclusion

The publication of the BEPS reports is a milestone in international tax law. Abuses and tax avoidance will be severely curtailed. Developing countries, too, will acquire new instruments to help them counter tax avoidance. These developments will have consequences for the Netherlands and the Dutch business community. There is certainly no need for the tax climate for businesses to suffer, provided measures are coordinated and implemented in all countries in the same way. In a number of areas, especially the exchange of information and the inclusion of anti-abuse provisions in treaties, the Netherlands will remain a leading player. We will continue to play an active role in fleshing out the other actions in a coordinated manner. Where measures have an unintended impact on innovative enterprises,

head offices and companies performing real economic activities and providing jobs, I will, taking into account the BEPS revenue target, take targeted compensatory measures to ensure the tax climate for businesses remains attractive.

By implementing the BEPS outcomes and simultaneously promoting the strengths of the Netherlands' tax system, I have every confidence that the government will succeed in finding the right balance: combating international tax avoidance and artificial structures, adopting a coherent policy towards developing countries, and ensuring the Netherlands remains an attractive location for national and international investments and companies.