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6th Annual International Tax Developments Seminar

The next wave

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During the 6th Annual International Tax Developments seminar "The next wave", several Loyens & Loeff tax experts as well as officials from the Dutch Tax Authorities updated the audience on the latest international tax developments. The tax world has been increasingly changing since July 2013, with a steady flow of OECD, EU and unilateral initiatives to tighten the rules. Predictability and control on the tax front are amongst the businesses' challenges of today. Ingo Heijnen from Hill+Knowlton Strategies reflected on what the current world expects from businesses' corporate behaviour.

Opening

Margriet Lukkien

The new fiscal unity regime could entail a major overhaul of the existing fiscal unity rules.

Margriet addressed three important developments on the Dutch horizon relating to the substance requirements, the participation exemption and the fiscal unity. She also touched upon the recently installed Dutch Committee on taxation of multinationals.

As of 2021, relevant substance requirements for specific intra-group financing and licensing companies will be introduced. If needed, there is still enough time to improve substance to comply with these requirements. It is not yet known if the same requirements will also apply to holding companies at some point in time.

In February 2018, the Dutch government announced that it would examine whether stricter requirements for access to the participation exemption should be considered. Such requirements are aimed at businesses which only have holding companies without substance in the Netherlands. We understand from the Dutch Ministry of Finance's agenda that we can expect further news in March 2020.

The Ministry of Finance is exploring alternatives for the existing fiscal unity rules. A consultation procedure started in June 2019, asking input on 4 possible directions. This is a follow-up on the so-called "repair measures" introduced as of 2018, with the aim of bringing its fiscal unity regime in line with the Court of Justice of the EU's judgment in the Groupe Steria case. The Dutch Ministry of Finance is expected to publish a letter in March 2020 setting out the main features of a new regime. Such a new regime could entail a major overhaul of the existing fiscal unity rules.

On top of all of this, the recently installed Dutch Committee on taxation of multinationals will investigate and advise on measures to achieve a fairer taxation of the profits of multinationals by broadening the Dutch corporate income tax base. A challenging balancing act, as at the same time it has been acknowledged that the Netherlands should remain attractive for corporate headquarters. It is still unclear when a report will be published, and more importantly, what kind of proposals it will contain.

The new ruling policy (1 July 2019)

Judith Jansen and Robert Bastiaens (Dutch Tax authorities / *"College Internationale Fiscale Zaken"*)

A ruling can only be concluded if there is sufficient economic nexus with the Netherlands.

Judith Jansen and Robert Bastiaens elaborated on the differences which the new ruling policy as of 1 July 2019 contains compared to the old ruling policy, such as the different definition of "certainty in advance", who will assess ruling requests and the publication of anonymized summaries of all international ruling requests.

A ruling can only be concluded if there is sufficient economic nexus with the Netherlands. They touched upon what this involves. They also paid attention to the impossibility to conclude a ruling (i) if the main or decisive motive of the taxpayer is to save Dutch or foreign taxes, and (ii) on the tax consequences of direct transactions with entities in certain low-tax (i.e., blacklisted) jurisdictions.

Transfer pricing and state aid experiences

Rogier Sterk

Businesses need to protect themselves anyway by way of proper documentation.

Since 2009, the number of pages of OECD Transfer Pricing publications has more than doubled. All these publications are relevant as they provide insight into the interpretation of rules and regulations. However, it should be kept in mind that these OECD publications do not constitute law themselves.

For transfer pricing purposes, the following three elements are important: (i) the transaction, (ii) an appropriate transfer pricing method, and (iii) the price. Many transfer pricing related aspects are based on the interpretation of the facts, rules and regulations and the OECD publications. This is one of the reasons why we see a growing number of disputes with tax authorities. The main topics of their audits leading to discussions are:

- Qualification of activities as “routine” (TNMM) or “non-routine” (“valuable and unique”) (profit split method);
- Financial transactions with the emphasis on discussions regarding the characteristics of the transaction, leverage and options realistically available (including re-payment);
- Allocation of business losses;
- On-charging of head office expenses and other expenses; and
- Treatment of carried interests in the private equity sector.

Trends we see in these audits include:

- Involvement of European and other countries (Multilateral Audits);
- Also investigations into transactions with normally taxed entities (so not only transactions with “low-taxed entities”); and
- Rapid assessment of transfer pricing documentation as inadequate.

As to the state aid cases, for businesses, either being investigated by the European Commission or finding themselves in one or more similar situations, this leads to uncertainty concerning their tax position (including but not limited to the effective tax rate) and lengthy discussions with auditors on the tax position in their financial statements.

The burden of proof is crucial in transfer pricing cases. It follows from case law that substantiating a transfer pricing correction is not an easy task for the tax authorities. What businesses can do depends on the level of certainty (i.e. risk appetite) they are aiming for. Businesses need to protect themselves anyway by way of proper documentation, not only standard transfer pricing documentation, but also other documentation documenting decisions and realistically available options. Another option for businesses is to discuss issues with the tax authorities in advance. In a worst case scenario, litigation is the only option left.

The future of holding and finance structures following the Danish cases

Linda Brosens

It is imperative that businesses monitor their cash flows if third countries are involved.

In six Danish cases, the Court of Justice of the European Union (CJEU) was asked amongst others to rule on the constituent elements of abuse and the meaning of the term “beneficial ownership”. These cases had in common that intermediary holding companies were used between entities established in third countries and Danish operational companies in order to obtain an exemption from Danish withholding tax on either interest or dividend payments.

With respect to abuse, the CJEU first observes that proof of abusive practices requires that a structure is artificially created with the essential aim to benefit from the EU tax

Directives and doing so contravenes the purpose of these Directives. Although the CJEU cannot assess the facts in the case at hand, it gave various indications that could lead to the conclusion that abuse is present, including the following:

- All or almost all of the income is, very soon after its receipt, passed on to an entity that cannot benefit from an EU tax Directive;
- Absence of economic activity, which should not only be established with reference to infrastructure and staff, but also with reference to for example the low amount of expenses incurred; and
- Inability to have economic use of the income received.

With respect to beneficial ownership, the CJEU concludes as follows:

- The concept of beneficial ownership laid down in the EU Interest and Royalty Directive should be interpreted as the entity which benefits economically from the interest received and, accordingly, has the power to freely determine how to use that income. According to the CJEU, the OECD Model Tax Convention and successive commentaries are relevant when interpreting beneficial ownership in the EU Interest and Royalty Directive; and
- In respect of the EU Parent-Subsidiary Directive, which does not contain an explicit beneficial ownership requirement, the dividend withholding tax exemption provided for in the Directive can be refused if the beneficial owner of the distributed dividend is a tax resident of a third state. Such refusal is not subject to the presence of fraud or abuse.

At present, it is uncertain how tax authorities in EU Member States will apply the outcome of the Danish cases in practice. The following questions can for example be raised:

- How will the tax authorities apply the indications of abuse to holding and financing structures?
- How many indications need to be present before one may conclude that abuse is present?
- What are the tax consequences if abuse is invoked?
- Will tax authorities interpret beneficial ownership economically, even in tax treaty situations?
- When is a recipient considered to benefit economically from the income?
- Will tax authorities read a separate beneficial ownership requirement in the EU Parent-Subsidiary Directive, even in the absence of abuse?

In order to ensure that holding and finance structures are acceptable from a tax perspective, it is recommended to continuously document the business reasons for the structure and to create sufficient substance supporting these business reasons. This may not be sufficient though. Following the Danish cases, it has also become imperative that the cash flows are closely monitored if third countries are involved.

Businesses might therefore want to re-asses their structure. If such reassessment reveals that a structure contains some weaknesses, businesses can already start to create a defense file for the past and may want to improve or even reconsider their structure going forward.

Withholding tax – From abolishment to stricter anti-abuse measures

Jeroen Janssen

Businesses may consider restructuring to optimise their tax position before implementation of several expected legislative proposals.

As of 1 January 2016, a General Anti Abuse Rule (GAAR) has been implemented in the EU Parent-Subsidiary Directive. Following the implementation of the GAAR, changes on the withholding tax front have come up in quick succession. The latest developments, include - amongst others - (i) the failed attempt of the Dutch government to abolish Dutch dividend withholding tax, (ii) case law of the CJEU and the impact on the Dutch substance requirements, and (iii) the implementation of the conditional withholding tax (CWHT) on interest and royalty payments as of 1 January 2021.

Following EU case law, the Dutch policy-based substance requirements for foreign intermediate holding companies can no longer constitute a so-called ”safe harbour” for Dutch dividend withholding tax and non-resident corporate income tax purposes. As a result, these substance requirements are only relevant for the “burden of proof” towards the Dutch tax authorities as of 1 January 2020. In this respect, the recent ruling of the Dutch Supreme

Court of 10 January 2020 is relevant. According to this ruling, a corporate structure could be regarded as abusive if a foreign shareholding in a Dutch BV qualifies as a portfolio investment at the moment of the dividend distribution (irrespective of the fact that it could qualify as an entrepreneurial activity shortly before the dividend distribution and the funds distributed originated from the entrepreneurial period).

As of 1 January 2021, Dutch CWHT on interest and royalty payments will be imposed on payments to:

- Low-tax or EU blacklisted jurisdictions;
- Entities interposed with the main purpose, or one of the main purposes, of avoiding the CWHT; and
- Hybrid entities.

In case of a payment, it should be assessed whether levying of CWHT is allowed under the applicable tax treaty. Businesses that envisage the payment of CWHT may consider restructuring to optimise their tax position before year end.

Several legislative proposals are expected. This new legislation should target certain loopholes in the Dutch Dividend Withholding Tax Act, and is expected to have an impact on: (i) cross-border migrations and cross-border mergers of Dutch companies, (ii) genuine Dutch operational cooperatives with shareholders located in tax havens, (iii) foreign investors investing in Dutch real estate via Dutch REITs, (iv) refund requests of Dutch dividend withholding tax by foreign investment funds, and (v) dividend stripping structures. Businesses may consider restructuring to optimise their tax position before implementation.

MLI: the New World

Charlotte Kiès

Businesses reorganise their groups in response to MLI uncertainties.

At this moment, 94 jurisdictions participate in the MLI, of which 42 have ratified and deposited their ratification instruments with the OECD. It is expected that the MLI will impact around 2,000 tax treaties.

Currently, many tax treaties qualify as 'Covered Tax Agreements' and are subject to the MLI. Many agreements are pending MLI ratification by a treaty partner or awaiting entry into effect. There are fifteen Dutch tax treaties which are fully in the scope of the MLI as of 1 January 2020. For a number of treaties the MLI is already partially effective, only for withholding taxes. The Netherlands, Luxembourg and Belgium deposited their ratification instruments in time for entry into effect for withholding taxes as of 1 January 2020. Only the Netherlands deposited its instrument in time for entry into effect for other taxes as of 1 January 2020. For example, this means that under the Netherlands-Luxembourg tax treaty the MLI will generally apply to other taxes as of 2021. This may give flexibility for restructurings prior to the full entry into effect of the MLI by the end of this year. This should be reviewed on a case-by-case basis. Switzerland has chosen a deferred entry into effect on the basis of separate notifications. Once the MLI is fully effective, companies must continue to monitor their positions as jurisdictions can make new notifications choosing for additional opt-ins which expand the MLI scope. Tax treaties currently not qualifying as Covered Tax Agreements may do so in the future or may be affected by bilateral negotiations to implement BEPS standards.

Based on the choices made by the Netherlands, the MAP-tiebreaker replaces the current corporate tiebreaker based on place of effective management in certain tax treaties. No tax treaty benefits are available until the treaty residence is settled in a Mutual Agreement Procedure. In December 2019, the Netherlands has issued a decree on the MAP-tiebreaker also including unilateral grandfathering rules for certain existing structures. Several MLI provisions targeting anti-avoidance of the qualification of a permanent establishment may furthermore affect current structures.

Applying to all tax treaty provisions, the Principal Purposes Test (PPT) will significantly increase uncertainty. The PPT requires a case-by-case review in which the source countries will play an important role. Although the examples in the OECD Commentary do not provide for safe harbours, genuine economic activities appear to be important. Businesses are responding by establishing and substantiating genuine economic presence through group restructurings. E.g. by centralising activities in one jurisdiction, integrating activities and functions of multiple Dutch entities into one, and relocating functions and assets within the group. Non-tax aspects, such as employment

law, corporate law and regulatory aspects, should also be taken into account.

Businesses are advised to:

- Be aware that the MLI has effect as of 2020;
- Check and re-check the impact of the MLI;
- Monitor positions of jurisdictions, gather and share experiences, and identify risks and exposures; and
- Take action to manage risks, optimise their position and make sure that they have a sustainable structure.

Digital taxation / BEPS 2.0 developments

Maarten de Wilde and Harmen van Dam

It is hard to say whether the businesses most likely targeted should act now.

Since the first part of the OECD's BEPS project there has been a shift in taxation, but public opinion is still that digital service businesses don't pay their fair share of taxes in their market jurisdictions. That's why the OECD has come forward with a proposal for a unified approach to reform profit allocation rules, Pillar 1, and a global minimum level of taxation, Pillar 2.

Where the measures in the first part of the OECD/BEPS project aimed at urging target businesses to align their functions with their business structure, Pillar 1 aims to shift the tax base from production countries to market jurisdictions. This pillar splits the profit allocation rules into Amount A, Amount B and Amount C. While the concepts of Amount B and Amount C are not new and mainly follow the principles of current TP rules, Amount A introduces a new taxing right within the international tax framework. A portion of a business's residual profit is allocated to the market jurisdiction, even in the absence of any physical presence within this market jurisdiction. The issue is: how large will Amount A be? If market countries are gaining taxing rights, production countries will have to give up these rights to mitigate double taxation.

Pillar 2 aims to secure a minimum tax paid, thus undermining jurisdictional competition (the so-called "global anti-base erosion" or "GloBE" proposal). If a source country levies no or not enough tax, the resident country may levy tax to achieve this minimum level of tax (income inclusion rule). On the other hand in cases where the resident country levies no or not enough tax, the source country may levy tax up to the minimum level of tax (undertaxed payments rule).

How should MNEs prepare themselves? First, they have to determine whether they are a targeted business. Digital service businesses, such as internet and social media companies, are most definitely targeted businesses. They usually do not have any physical presence in their market jurisdictions and so manage to pay no or hardly any corporate income tax in these countries. Similarly, businesses having a minimal physical presence in the market jurisdictions will most likely be targeted. Businesses that do have more than a minimal physical presence in their market jurisdiction, through dealerships, for example, could be targeted but are less likely to be so. Businesses with a substantial physical presence in their market jurisdictions will most likely not be targeted. Despite the foregoing, it is uncertain to which businesses the new rules will apply at this stage, as it is difficult to separate the digital part of the economy from the rest of the economy. In principle, it could apply to any business unless specifically carved out.

It is hard to say whether the businesses most likely targeted should act now. If a reorganisation is in the pipeline anyway, it would certainly be a good time to take these new developments into account. MNEs may consider moving their business and actual functions to market jurisdictions and thus create a taxable base in these market jurisdictions, so that they secure single taxation rather than double taxation.

Mandatory Disclosure Directive – reporting starts soon

Carlijne Brinkers

Taxpayers should be aware that they might have to disclose information as intermediary.

Businesses today need to bear in mind that in 2018 the Mandatory Disclosure Directive (MDR Directive) of the European Union entered into force. This directive imposes an obligation on intermediaries, and in certain circumstances on taxpayers, to report to the tax

authorities of the EU Member States certain cross-border arrangements.

The Netherlands implemented the MDR Directive in its domestic legislation in December 2019. As of 1 July this year, Dutch intermediaries and taxpayers will have to report qualifying cross-border arrangements to the Dutch tax authorities within a time frame of 30 days. Due to its retroactive effect, all reportable cross-border arrangements of which the first step is implemented in the time frame between 25 June 2018 and 1 July this year must be reported no later than 31 August this year.

Taxpayers should be aware that they might, as an intermediary, have to disclose information on a reportable cross-border arrangement to the Dutch tax authorities. This is the case if an entity that forms part of a multinational group employs an in-house adviser (for instance, an in-house tax or legal department) which advises one or more affiliated group entities on a reportable cross-border arrangement, whereas the group entity that employs the in-house adviser is not involved in the arrangement itself. The entity that employs the in-house adviser is in principle considered the intermediary and not the individual in-house adviser.

The implementation of the MDR Directive will impact all taxpayers that operate within or across EU borders. In order to stay in control as much as possible of the information that will have to be disclosed, Carlijne recommended that businesses should:

- Monitor all arrangements implemented as of 25 June 2018 that involve EU jurisdictions and arrange for disclosure assessment by in-house advisers together with local advisers;
- Raise awareness within legal and business departments for typically disclosable transactions without an important tax component and request the involvement of the tax department;
- Maintain a central record of any potentially disclosable arrangements;
- Develop together with their advisers an internal procedure in order to collect all relevant information; and
- Maintain proof of filings made.

From corporate apologies to corporate behaviour: become part of the Force for Good!

Ingo Heijnen (Hill+Knowlton Strategies)

It's about building acceptance for business choices and policies.

For years, businesses expected the public to trust them to do the right thing for all stakeholders. But this trust has eroded. Too many scandals, too many apologies have induced the public, including politicians and regulators, to expect more. A clear change for companies can be identified, from apologising for mistakes and asking for trust, to explaining what their corporate behavior is going forward and letting their publics decide whether they accept this explanation. This means that businesses need to change the way they think: from assuming they have a license to operate to actively securing this license through their (permissible) behaviour.

This change is gathering pace and is happening everywhere. In 2019, the American Business Roundtable – a consultation platform of CEOs in the United States – declared the creation of stakeholder value rather than shareholder value the most important goal for companies. The focus of businesses moves from shareholder value to being part of the society at large. It's about building general acceptance for business choices and policies. Acceptance comes by demonstrating the behavior that the outside world wants to see, in terms of Environmental, Social and Governance (ESG) aspects. Long-term value is created by corporations that embed these themes in their strategy, practices and reporting. Corporate tax reporting and tax behaviour are part of it, or will become so very soon.

Nowadays the public demands transparency and disclosure. Hence, acceptable corporate behaviour should be a top priority. Businesses disclose information they never expected to disclose. An example is the recent disclosure by MNEs of their tax contribution to society. This is another step in a process that is changing the world of tax professionals.

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