# Netherlands

## Transfer Pricing

Authors
Harmen van Dam

Partner, head Transfer Pricing Team

Taco Wiertsema

Senior associate, member Transfer Pricing Team

Loyens & Loeff, the Netherlands

Latest Information:

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## 0. Documentation

### 0.1. Laws, decrees and other references

Article 8b of the Corporate Income Tax Act 1969.

Article 8c of the Corporate Income Tax Act 1969.

Article 29b to article 29h of the Corporate Income Tax Act 1969.

*See* section 2.3. for decrees issued in relation to transfer pricing.

### 0.2. Case law

Supreme Court, 3 April 1957, BNB 1957/165.

Supreme Court, 23 April 1958, BNB 1958/179.

Supreme Court, 12 February 1964, BNB 1964/95.

Supreme Court, 27 March 1968, BNB 1968/112.

Supreme Court, 25 June 1969, BNB 2010/93.

Supreme Court, 1 July 1969, BNB 1969/217.

Supreme Court, 23 January 1973, BNB 1986/100.

Supreme Court, 31 May 1978, BNB 1978/252.

Amsterdam Court of Appeal, 15 June 1978, BNB 1979/188.

The Hague Court of Appeal, 22 January 1982, BNB 1983/109.

The Hague Court of Appeal, 10 May 1984, BNB 1986/8.

Supreme Court, 21 September 1994, BNB 1995/15.

Supreme Court, 28 March 1990, BNB 1990/194.

Leeuwarden Court of Appeal, 19 September 1997, VN 1998/30.17.

Supreme Court, 17 August 1998, BNB 1998/385.

Supreme Court, 11 October 2000, BNB 2001/142.

Supreme Court, 28 February 2001, BNB 2001/199.

Supreme Court, 23 January 2004, BNB 2004/214.

Supreme Court, 23 April 2004, VN/2004/27.17.

Supreme Court, 25 November 2005, BNB 2007/117.

Amsterdam Court of Appeal, 11 February 2009, Case 04/04338.

Den Bosch Court of Appeal, 19 May 2011, BA 2011/19.7.

The Hague Lower Court, 11 July 2011, AWB 08/9105 VPB.

Breda Lower Court, 21 December 2011, VN 2012/32.2.1.

Supreme Court, 4 January 2013, V-N 2011/57.15.

Supreme Court, 1 March 2013, BNB 2013/109.

Zeeland-West Brabant Lower Court, 17 January 2014, AWD 11/3717.

## 0.3. Bibliography

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M.A. de Lange, P.W.H. Lankhorst & R. Hafkenscheid, *(Non-)Recognition of Transactions between Associated Enterprises: On Behaving in a Commercially Rational Manner, Decision-Making Traps and* BEPS, 22 Intl. Transfer Pricing J. 2 (2015), Journals IBFD.

M.A. de Lange, P.W.H. Lankhorst & R. Hafkenscheid, *Het negeren van transacties tussen gelieerde partijen*, Weekblad Fiscaal Recht, 7078 (12 February 2015).

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W.P.J. Schramade & P.A.M. Pijnenburg, *Fiscale Encyclopedie De Vakstudie Vennootschapsbelasting 1969 (article 8b)* (Kluwer 2015).

M. van den Berg, *The Enlarged Scope of Dutch Substance Requirements*, Tax Notes International (2014).

J.T. van Egdom, *Verrekenprijzen: de verdeling van de winst van een multinational* (Kluwer 2014).

L.F. van Kalmthout, *Verrekenprijzen*, in *Over de grenzen van de vennootschapsbelasting*, essays issued to Prof. Mr D. Juch (Kluwer 2002).

E.A. Visser, *Verrekenprijzen; een drieluik*, Fiscale Monografieën (2005).

### 0.4. Abbreviations and terms

| | | |
|---|---|---|
| APA | : | Advance pricing agreement |
| ATR | : | Advance tax ruling |
| CIT | : | Corporate income tax |
| CITA | : | Corporate Income Tax Act 1969 |
| CCA | : | Cost contribution agreement |
| CGTP | : | Coordination group transfer pricing |
| CPL | : | Cash pool leader |
| CUP | : | Method Comparable uncontrolled price method |
| DTA | : | Dutch tax authorities |
| GAAP | : | Generally accepted accounting principles |
| GTA | : | General Tax Act |
| IFRS | : | International Financial Reporting Standard |
| ITA | : | Dutch Income Tax Act 2001 |
| JTPF | : | EU Joint Transfer Pricing Forum |
| MAP | : | Mutual agreement procedure |
| MNE | : | Multinational enterprise |
| NPI | : | Net profit indicator |
| OECD Commentary | : | Commentary to the OECD Model Tax Convention on Income and Capital |
| OECD Guidelines | : | OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations |
| OECD Model | : | OECD Model Tax Convention on Income and on Capital |
| OECD Report | : | Report on the attribution of profits to permanent establishments |
| PE | : | Permanent establishment |
| State Secretary | : | Dutch State Secretary for Finance |
| TNMM | : | Transactional net margin method |

## 1. Corporate Tax System in Brief

*See* Corporate Taxation - Country Surveys section 1.

# 2. Allocation of Income

## 2.1. Systems applied

Effective from 1 January 2002, the CITA contains a specific provision (article 8b) in which the arm's length principle is laid down. The explanatory memorandum to the legislation[1] (the Explanatory Memorandum) indicates that with the introduction of article 8b, the Dutch government aimed at codifying the arm's length principle of article 9 of the OECD Model into the CITA. The Explanatory Memorandum further sets out that an improved correlation between international transfer pricing practice, the OECD Commentary and the OECD Guidelines was ensured with the article. In addition, documentation requirements were introduced in article 8b.

General principles of Dutch tax law also ensure that profits derived from a business are determined on the basis of the arm's length principle. Article 3.8 of the ITA and article 10 of the CITA allow both the courts and the DTA to adjust taxable income reported to the extent that such income (or the lack thereof) does not result from the business but instead from the relationship between a company and its shareholder. It is noted in this respect that Dutch tax law may not only require for such an adjustment to increase the taxable income; it may also require for a reduction of taxable income.

Article 3.8 of the ITA defines profits as the total benefits derived from a business, under whatever name and in whatever form. Article 10 of the CITA provides that direct and indirect distributions of profits may not be deducted in determining a company's taxable profits. At various times the State Secretary has indicated, on the basis of article 3.8 of the ITA and article 10 of the CITA, that the DTA accept the principles set out in the OECD Guidelines.[2]

Article 3.8 of the ITA and article 10 of the CITA provide the basis for adjusting taxable income reported to the extent such income is influenced by a shareholder relationship. Adjustments are made based on a disguised distribution to the shareholder or an informal capital contribution to the company. In case law,[3] profit distributions have been defined as "a shift of capital from the company to the shareholder as a result whereof money or other valuables, covered by profit potential, are distracted from the capital of the company for the benefit of the shareholder."

In its judgment dated 31 May 1978,[4] the Supreme Court applied the principle of article 3.8 of the ITA in relation to a corporate entity. In that case a Dutch company was granted the benefit of an interest-free loan by its Swedish shareholder. This benefit was not considered to constitute a business profit for the Dutch company but is instead a contribution to its capital by the Swedish shareholder. If the shareholder in this case had been a Dutch company, the profits of the Dutch company would have been increased with a deemed interest receipt determined on the basis of the market interest rate for loans concluded under comparable conditions. In this way, the non-arm's length aspects resulting from the shareholder relationship are eliminated from transactions between the related entities.

A distinction has been made by the Supreme Court between the situation in which the shareholder making the informal capital contribution is an entrepreneur whose profits are subject to tax and the situation in which the shareholder is not acting as an entrepreneur. In its judgments dated 8 July 1986,[5]

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1. *MvT*, *Kamerstukken* II 2001/02, 28 034, no. 3, pp. 7-8 and 19-23.
2. This was most explicitly confirmed by the Decree of 30 March 2001 (IFZ2001/295M), as amended by Decree of 21 August 2004 (IFZ2004/680M) and replaced by the Decree of 14 November 2013 (IFZ 2013/184M).
3. Supreme Court judgments dated 17 Mar. 1954 (BNB 1954/130) and 30 Dec. 1953 (BNB 1954/61).
4. Supreme Court judgment dated 31 May 1978 (BNB 1978/252).
5. Supreme Court judgments dated 8 July1986 (BNB 1986/295 and BNB 1986/296).

the Supreme Court ruled that an individual shareholder allowed its company a benefit by not charging certain costs that would have been chargeable under arm's length conditions. On the basis of the Swedish shareholder decision, such benefit should be eliminated from the company's profits since it was not a profit derived from the business. However, since any deemed charge could not be included in the taxable income of the individual shareholder (since the shareholder was not an entrepreneur and could only be taxed on income actually received), the Supreme Court ruled that the company should remain taxable on the benefit received. The Court did not want to create a leak in those cases where the benefit could not be taxed at the level of the shareholder. The elimination of the benefit at the level of the company depended on the ability to tax the benefit at the level of the shareholder.

In line with consistent case law, a deemed dividend can only be taken into account in case of so-called "double awareness", where both (i) the company intends to benefit its shareholder and (ii) the shareholder is aware of that intention.

Some authors, however, are of the opinion that the single awareness of the company is already sufficient.[6] The Supreme Court[7] also seems to suggest that no awareness by the benefiting shareholder is required. In later case law, the Supreme Court decided that the existence of a disguised distribution was clearly conditional on awareness by both the company and the shareholder.[8] The Court, however, interpreted the awareness requirement of the shareholder slightly more objectively by introducing that awareness is deemed to exist if the shareholder should have reasonably been aware.

Benefits conferred by one company to another company having a common shareholder will be traced through the shareholder. Such benefits will be treated as deemed dividend distributions to the common shareholder followed by capital contributions to the benefiting company. If the common shareholder is a Dutch resident shareholder, the dividend income may be included in its taxable income, depending on the tax position of the shareholder.

Dutch case law mainly focuses on correcting the non-arm's length transactions between a company and its shareholders. However, it is acknowledged that a shareholder does not always act in its capacity of shareholder. He may also act in another capacity, e.g. as a creditor. If a shareholder waives the right to interest on a loan granted to its subsidiary as a result of the negative equity position of the subsidiary, it may be questioned whether the waiver took place in the capacity of shareholder or creditor. If the financial situation of the subsidiary/debtor is such that a non-related creditor would also have waived its right to interest, the shareholder may be considered to have acted as creditor rather than shareholder. As such, the waiver could be considered arm's length.[9]

Formulary apportionment is not applied in the Netherlands.

## 2.2. Legal basis of arm's length principle

The codification of the arm's length principle, as included in article 8b of the CITA, is worded as follows:[10]

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6. E.g. *see* E. Aardema, *De directeur-groot aandeelhouder met zijn B.V. en de fiscus* pp. 14-16 (Kluwer 1988).
7. Supreme Court judgment dated 28 May 1969 (BNB 1969/164).
8. E.g. reference is made to Supreme Court judgments dated 7 Jan. 1970 (BNB 1970/62), 4 May 1983 (BNB 1983/233) and 15 May 1985 (BNB 1985/271).
9. E.g. *see* Lower Court Amsterdam, 14 Mar. 2001 (no. 99/2387), where, as a result of the shareholder acting in its capacity as creditor, the debtor could not deduct an imputed interest expense.
10. Unofficial translation.

(i) In case:

a) an entity, directly or indirectly, participates in the management or supervision, or the capital, of another entity; and

b) the conditions (transfer prices) agreed or imposed of the transactions between these entities differ from conditions that would have applied in the market between independent parties, the entity's profit is determined as if "arm's length" conditions applied.

(ii) The first paragraph applies similarly to an individual who, directly or indirectly, participates in the management or supervision, or the capital, of the one and the other entity.

(iii) The entities mentioned in the first and second paragraph must include information in their records

a) which shows in which manner the transfer prices that are referred to in the first paragraph have been established; and

b) from which it can be deduced that, in the market, the transfer prices established would have been agreed to between independent entities.

The article has two effects. It allows for the adjustment of conditions (contractual terms) of related-party transactions for purposes of determining Dutch CIT and it requires taxpayers to maintain transfer pricing documentation. *See* section 13.2. for further guidance on article 8b of the CITA.

## 2.3. Regulations and circulars

The following decrees have been issued with respect to transfer pricing:

- Decree of 25 April 1985 (BNB 1985/196). This decree was replaced by the decree of 30 March 2001 (IFZ 2001/295M).
- Decree of 30 March 2001 (IFZ 2001/295M). This decree was replaced by the decree of 14 November 2013 (IFZ 2013/184M).
- Decree of 21 August 2004 (IFZ 2004/680M). This decree contained supplements to the above-mentioned decree. It was also replaced by the decree of 14 November 2013 (IFZ 2013/184M).
- Decree of 29 September 2008 (IFZ 2008/248M). This decree deals with the practical application of the MAPs initiated under double tax treaties and the EU Arbitration Convention (90/436/EEC).
- Decree of 27 January 2011 (IFZ 2010/457M). The decree deals with the attribution of profits to PEs and applies the guidance included in the OECD Report on the Attribution of Profits to Permanent Establishments dated 22 July 2010.
- Decree of 14 November 2013 (IFZ 2013/184M) (the 2013 Decree). The 2013 Decree replaced the decrees of 30 March 2001 and 21 August 2004. This decree intends to clarify the application in Dutch tax law of the guidance included in the OECD Guidelines on the arm's length principle. In the 2013 Decree, the State Secretary also expresses his view that the OECD Guidelines have direct effect in Dutch tax law.

- Decree of 3 June 2014 (DGB 2014/3098). This decree deals with the procedure of obtaining certainty in advance in the form of an APA with the Dutch tax authorities as regards the arm's length nature of intercompany transactions.
- Decree of 3 June 2014 (DGB 2014/3101). This decree deals with the procedure for obtaining certainty in advance as regards the Dutch tax consequences of financial service companies (FSCs) (*see* section 17.3.1.).
- Decree of 3 June 2014 (DGB 2014/3102). This decree contains a Q&A in relation to the decree on FSCs as well as the decree of 3 June 2014 on obtaining certainty in advance the form of an ATR (DGB 2014/3099).

As regards the legal effect of the decrees, and specifically the 2013 Decree, the following is noted. In its introduction, the 2013 Decree notes that it is intends to provide a further interpretation of the arm's length principle which is codified in Dutch tax law in article 8b of the CITA (i.e. specifically in respect of items of the OECD Guidelines that allow room for (member countries') own (different) interpretations or items which are unclear). It clarifies that the 2013 Decree sets out the policy and merely contains the view of the State Secretary as regards the application in Dutch tax law of the arm's length principle and the OECD Guidelines. In the 2013 Decree, the State Secretary also expresses his view that the OECD Guidelines have direct effect in Dutch tax law.[11]

However, from a Dutch formal tax law point of view, a policy decree can be considered an opinion of the State Secretary. Consequently, it has a legal status which differs from formal legislation. Unlike formal legislation, by which both the DTA and the taxpayer are legally bound, a policy decree only binds the DTA. In this respect, the Supreme Court clarified in its judgment dated 28 March 1990[12] that a taxpayer may rely on a policy decree (i.e. on the basis of the principle of good faith) and that Dutch courts (including the Supreme Court) are allowed to render a verdict on the application of a policy decree.

As regards the 2013 Decree, if it serves their interest, Dutch taxpayers may rely on the view of the State Secretary application in Dutch tax law of the arm's length principle and the OECD Guidelines. However, Dutch taxpayers are not required under law to apply the principles laid down in the 2013 Decree if these do not suit them.

## 2.4. Scope of legislation

Prior to the introduction of article 8b of the CITA (i.e. the codification of the arm's length principle in Dutch tax law), no definition existed of the term "related party". However, it was generally considered that a correction could only be made where a benefit was conferred by a company to its shareholder. In this respect, article 10 of the CITA expressly provides that direct and indirect distributions of profits are not deductible for purposes of determining a company's taxable profit. Furthermore, the ability to impose corrections was assumed to be limited to shareholder relationships. Additionally, transactions benefiting close relatives of a shareholder were covered.[13]

Neither statutory law nor case law provides clear standards for companies to be considered "related". Two Supreme Court judgments[14] gave rise to confusion with respect to the question whether corrections

11. Various authors disagree with the view of the State Secretary that the OECD Guidelines have direct effect in Dutch tax law. Reference is made most notably to E.A. Visser, *Verrekenprijzen; een drieluik*, Fiscale Monografieën (2005), p. 26 and L.F. van Kalmthout, *Verrekenprijzen*, in *Over de grenzen van de vennootschapsbelasting*, essays issued to Prof. Mr D. Juch, (Kluwer 2002), p. 99.
12. Supreme Court judgment dated 28 Mar. 1990 (BNB 1990/194).
13. Supreme Court judgment dated 27 Mar. 1968 (BNB 1968/112).
14. Supreme Court judgments dated 21 Sept. 1994 (BNB 1995/15 and BNB 1995/16).

should be limited to shareholder relationships. In these cases, certain expenses were disallowed for corporate income tax purposes, although the tax authorities could not show that beneficiaries of the expenses were related somehow to the company paying the expenses.

After the introduction of article 8b of the CITA, a transfer price correction may be made provided that an entity, directly or indirectly, participates in the management, supervision or capital of another corporate entity. The second paragraph of this article extends this concept to situations where the same person participates, directly or indirectly, in the management, supervision or capital of two corporate entities dealing with each other. The applicability of article 8b of the CITA extends to transactions between companies, partnerships, trusts, etc. (i.e. "entities"); however, the article does not cover individuals. Furthermore, under article 18 of the CITA, the guidance of article 8b of the CITA equally applies to non-resident corporate taxpayers that have taxable income arising from a business in the Netherlands (i.e. a Dutch PE). It is, however, questionable whether dealings between a PE and its head office are covered by the new text considering that the wording refers to "another entity" and taking into account that such "dealings" only exist within a single legal entity.[15] *See* section 10.1. for further guidance on the Dutch policy as regards the attribution of profits to (foreign) PEs.

Article 8b of the CITA clarified that the scope of the term "related party" extends to situations where parties are deemed related as a result of influence exercised through (common) management or supervision. The article requires that entities be related at the moment a transaction is entered into. Consequently, article 8b also applies where entities are currently no longer related, but were at the time of entering into the transaction.

It is, however, stated in the Explanatory Memorandum[16] that in order for article 8b of the CITA to be applicable, the shareholder, supervisor and/or manager should have sufficient authority to influence the determination of transfer prices between the parties involved. Whether this is the case should be determined on a case-by-case basis. If a taxpayer is of the opinion that there is not sufficient authority to influence the determination of the transfer prices, the taxpayer may request for certainty in advance from the DTA. In accordance with article 9 of the OECD Model, the concept of related entities has not been further defined or qualified for purposes of article 8b CITA (i.e. the legislature specifically decided not to include a quantification in order to prevent manipulation). The article does not provide for a *de minimis* exemption concerning the extent of the relation between the entities. The Explanatory Memorandum further sets out that a common member of the supervisory boards would generally not trigger the application of article 8b of the CITA. According to the State Secretary, a taxpayer only has a limited duty to inquire whether another party to a transaction is related. If the relation is not presented or confirmed by the taxpayer, the tax inspector needs to demonstrate that the parties are in fact related. In first instance, the burden of proof rests with the DTA.

A judgment of the Den Bosch Court of Appeal concerned a Dutch company making marketing payments to its 20% shareholder.[17] Although the case concerned a minority shareholder, the view of the tax inspector that the documentation requirements of article 8b(3) of the CITA as regards related-party transactions were not complied with has not been disputed.

15. Concluding that these transactions are not covered under article 8b of the CITA would not impact the determination of the PE's profit but would avoid triggering documentation requirements. However, the legislator seems to have had the intention to bring dealings between a PE and its head office within the scope of article 8b.
16. *MvT*, *Kamerstukken* II 2001/02, 28 034, no. 3, pp. 7-8 and 19-23.
17. Den Bosch Court of Appeal judgment dated 19 May 2011 (09/00465).

## 2.5. Concepts of associated enterprises and control

*See* section 2.4.

## 2.6. Status and impact of OECD Guidelines and UN Transfer Pricing Manual

*See* section 5.3.

# 3. Comparability Analysis

## 3.1. Comparability factors

The Netherlands applies the guidance of the OECD Guidelines on comparability factors. These factors include (i) the characteristics of the property or services transferred, (ii) the functions performed by the parties (taking into account assets used and risks assumed), (iii) the contractual terms, (iv) the economic circumstances of the parties and (v) the business strategies pursued by the parties.

## 3.2. Internal comparables

The DTA allow the use of both internal and external comparables. There is no guidance with respect to internal comparables.

## 3.3. External comparables

In the Netherlands, external comparables are typically identified on the basis of publicly available company data (*see* section 3.5.).

## 3.4. Foreign comparables and secret comparables

The DTA generally allow benchmarking analyses to be based on pan-European database information. This is the result of the fact that due to the limited size of the economy the Netherlands lacks sufficient related-party transactions and the general idea that for most products the EU market is ‘harmonized’. In practice, the DTA may require taxpayers to account for incremental risk on certain transaction due to the location of the beneficiary through the use of, for example, country risk premiums.

*See* section 14.6. for guidance on the use by the DTA of secret comparables.

## 3.5. Databases

Commercial databases generally applied in the Netherlands and accepted by the DTA include Bureau van Dijk’s Amadeus and Orbis Databases, Bloomberg, Moody’s RiskCalc and LossCalc as well as Thomson Reuters LPC's DealScan. As regards transactional net margin method (TNMM) transfer pricing reports, the DTA in practice require the use of 3-year data. In the 2013 Decree, the DTA indicate that in order to prevent hindsight, only data of the respective year and previous years can be used. In practice, due to the fact that data is generally obtained from commercial accounts filed at the various European chambers of commerce, the most recent data will generally be at least 2 years old.

## 3.6. Comparability adjustments

In accordance with the OECD Guidelines comparability adjustments are applied in practice in the Netherlands. These adjustments are primarily made to account for differences in capital, functions, assets and risks. In addition, working capital adjustments are also made in practice; however, the DTA seem reluctant to accept such adjustments in the scope of APA requests.

### 3.7. Arm's length range and statistical tools

In the 2013 Decree, the State Secretary acknowledges that since transfer pricing is not an exact science, a range of prices, rather than one single price, is generally determined. Statistical tools, such as the interquartile range, may be applied to increase the reliability of the comparable data. Subsequently, the State Secretary indicates that a point within the (interquartile) range should be selected that is consistent with the relevant facts and circumstances of the specific case. If the price applied falls outside of the range, the OECD Guidelines[18] note that the adjustment can take place up to the point within the range that corresponds as close as possible with the facts and circumstances of the respective intra-group transaction. If such point cannot be determined (based on the specific facts and circumstances), the State Secretary takes the position that the transfer prices should be adjusted to the median (i.e. the middle point of a range of observations).

The State Secretary further indicates that, if and to the extent the price applied already falls within the range, an adjustment can only take place if the taxpayer substantiates the reasons therefore and if this adjusted price is contractually agreed upon and paid.

### 3.8. Timing issues in comparability

Reference is made to the guidance included in the OECD Guidelines.

## 4. Transfer Pricing Methods

### 4.1. Description of methods available

The State Secretary indicates in the 2013 Decree that, in line with paragraph 4.9 of the OECD Guidelines, the DTA will conduct a transfer pricing audit from the perspective of the method applied by the taxpayer at the time of the transaction. Consequently, Dutch taxpayers have a certain degree of freedom as regards their choice for any of the five methods described in the OECD Guidelines, provided that the method applied leads to arm's length results for the specific transaction. The OECD Guidelines provide three traditional transaction methods:

- the comparable uncontrolled price method (CUP method);
- the resale price method; and
- the cost-plus method,

and two transactional profit methods:

- the transactional profit split method (the PSM); and
- the transactional net margin method (i.e. the TNMM).[19]

The DTA confirm that a taxpayer is not required to apply a so-called "best method rule" for the selection of the transfer pricing method (i.e. where a taxpayer is required to (i) assess all methods available and (ii) substantiate that the method applied provides for the best result given the circumstances). The DTA only expect a taxpayer to take into account the reliability of the method applied in relation to the facts and circumstances of the situation and to substantiate its choice.

18. OECD Guidelines, para. 3.62.
19. Numerical examples on the transfer pricing methods can be found in the decree dated 30 Mar. 2001 (IFZ2001/295M, replaced by the 2013 Decree).

## 4.2. Hierarchy of a method

We experience a tendency with the DTA to explicitly prefer the CUP method and most notably the PSM over the other (one-sided) transfer pricing methods (i.e. the resale price method, cost-plus method and the TNMM).

## 4.3. Selection of a method

*See* section 4.1.

## 4.4. Comparable uncontrolled price method

In the Netherlands, the CUP method is commonly applied for the transfer pricing of intra-group loans. The arm's length interest rate on an intercompany loan can be determined by reference to the market rate for loans with comparable conditions. In this respect, relevant factors can be debtor/credit rating, maturity, denomination, subordination, etc.

The Leeuwarden Court of Appeal[20] ruled that under certain circumstances reference can be made to an individual investor, rather than a financial institution, for the determination of an arm's length interest rate on an intercompany loan.

The Supreme Court[21] further ruled that in determining the taxable profit of the creditor and debtor, the interest rate on a "tainted loan" (i.e. a related-party loan of which the interest rate is not in accordance with the arm's length principle) is set at the rate that the debtor would have paid if it had attracted the loan from an independent third party under guarantee of the actual creditor. In the 2013 Decree, the State Secretary assumes, unless the taxpayer can substantiate the contrary, the existence of a "tainted loan" if such loan is granted to a related debtor with a credit rating lower than BBB-.

## 4.5. Resale price method

No current guidance exists for the resale price method in the Netherlands. In practice, the resale price method is hardly ever applied because the data used to compile public databases does not generally provide for a consistent classification of cost items among either cost of goods sold or operating expenses. As such, gross profit levels of comparable companies may not be very reliable. For this purpose, the DTA generally require taxpayers in the scope of an APA to apply a remuneration based on operating profit or EBIT such as the TNMM with "total cost" as net profit indicator (NPI) or TNMM with "revenue" as NPI. In practice, these systems are sometimes referred to as "net cost-plus" and "net resale minus" respectively.

The DTA take the view that a sales-based remuneration system (i.e. resale price method or TNMM with a NPI based on revenue) is the most appropriate method for remunerating distribution activities.

## 4.6. Cost-plus method

Due to the fact that transfer pricing methods are in practice generally based on EBIT, the cost-plus method (i.e. a gross profit method) is often incorrectly referred to when in fact the TNMM with "total cost" as NPI (the "net cost-plus") is applied. *See* section 4.7. for further guidance on the application of the TNMM.

20. Leeuwarden Court of Appeal judgment dated 19 Sept. 1997 (VN 1998/30.17).
21. Supreme Court judgment dated 25 Nov. 2011 (BNB 2012/37).

In the 2013 Decree, the State Secretary included guidance as regards the use of budgeted and actual costs as well as the use of pass-through costs. These items are further discussed below.

**Budgeted versus actual costs**

The 2013 Decree indicated that prices are generally determined in advance on the basis of budgeted costs. As regards price adjustments (i.e. when actual costs differ from the budget), the 2013 Decree indicates that the acceptability adjustments for tax purposes depends on the cause of the difference. If, for example, given differences between budgets and actuals are caused by inefficiencies, the 2013 Decree indicates that a price adjustment would not be accepted in third-party situations. The 2013 Decree assumes in this respect that as the party supplying the services is able to influence the costs relating to the services, it will also need to bear the increased costs resulting from inefficiencies. As regards the use of budgets for transfer pricing purposes, the 2013 Decree indicates that these would need to be determined on the basis of proper economic fundamentals.

**Pass-through costs**

The 2013 Decree notes that these costs do not need to be included in the cost base. Such costs include costs that are initially paid by the contracting party providing the service but that are generally charged separately to the client. Pass-through costs include legal fees, court registry fees and service costs. In general, such costs should be charged separately to the client. Although these costs are related to the services provided, they do not require a separate remuneration alongside the reimbursement. Whether or not costs should be considered as pass-through should depend on the willingness of third parties to accept a recharge of these costs without a markup (in this respect, the 2013 Decree refers to paragraph 2.93 of the OECD Guidelines).

According to the 2013 Decree, when performing a transfer pricing analysis, the appropriate remuneration needs to be determined without taking into account subsidies, fiscal incentives and partially deductible expenses and that subsequently these subsidies, fiscal incentives and partially deductible expenses should be taken into account. Subsidies should generally not be deducted from the cost base when applying a cost-based remuneration.

## 4.7. Transactional net margin method

According to the 2013 Decree, the TNMM with “total cost” as NPI should be applied if so-called “routine services” are provided; however, the 2013 Decree does not indicate what constitutes “routine services”. One may take the view that whether or not an activity is considered “routine” should not have any relevance as regards its transfer pricing treatment. Instead, on the basis of economic theory (i.e. the study of processes by which scarce resources are allocated to satisfy unlimited wants) scarcity, rather than the character, of an activity (routine or not) should be taken into account for transfer pricing purposes because it reflects market prices for an activity.[22]

As regards manufacturing activities, a TNMM with “total cost” as NPI is generally accepted as the method to determine the arm’s length remuneration for contract manufacturing. Due to the absence of, or limited, risks the contract manufacturer should generally not be allocated a profit in excess of a

22. M.A. de Lange, P.W.H. Lankhorst & R. Hafkenscheid, *(Non-)Recognition of Transactions between Associated Enterprises: On Behaving in a Commercially Rational Manner, Decision-Making Traps and BEPS*, 22 Intl. Transfer Pricing J. 2 (2015).

fixed percentage of the production costs. This was confirmed by the The Hague Court of Appeal on 13 June 1984.[23]

As regards centralized purchasing activities (CPA), the State Secretary indicated in the 2013 Decree that such companies generally perform "routine" activities and incur limited risks (price and/or stock-related risks). The State Secretary further indicates that independent purchasing agents also generally perform routine or auxiliary functions. They are generally remunerated on the basis of a percentage of the purchased goods and that – in practice – it is difficult to obtain reliable comparables. For that reason, the DTA will test the arm's length character of a remuneration for a CPA entity on the basis of a cost-based remuneration. The value of the purchased goods should not be included in the cost basis due to the routine character of the functions performed.

The Supreme Court[24] confirmed the judgment of the Arnhem Lower Court[25] that the remuneration of procurement activities should generally be determined on the basis of the cost-plus method (i.e. the TNMM with total cost as NPI). This case law relates to situations wherein (i) goods were acquired by a procurement company and (most) were sold on to a related Dutch company and (ii) the procurement company acted as a facilitator, where goods were transferred directly by the independent suppliers to a Dutch company. The courts based their decision for the application of the cost-plus method mainly on the fact that the procurement companies performed limited functions and incurred limited risks.

### 4.8. Profit split method

No case law or guidance is available in the Netherlands on the application of the PSM. Reference is made to the OECD Guidelines. In practice, we observe a tendency for tax administrations (including the DTA) to have an explicit preference for the CUP method and the PSMs over the other (one-sided) transfer pricing methods (i.e. the cost-plus method, the resale price method and the TNMM).

### 4.9. Other methods

No case law or guidance is available in the Netherlands on the application of other methods. It is noted, however, that other methods would be acceptable provided that they lead to arm's length results.

### 4.10. Combined use of methods

The State Secretary indicates in the 2013 Decree that certain situations may allow for the use of a combination of transfer pricing methods. The taxpayer, however, is not obliged to apply multiple methods; he does need to substantiate his choice for applying multiple methods. The State Secretary does not provide for examples of transactions in which the use of multiple methods would be accepted.

## 5. Intangibles

### 5.1. Definition and classification of intangible property

Dutch tax law does not provide for a definition of intangibles nor does it refer for such definition to other sources of Dutch law or regulations. In addition, in the Netherlands, whether an intangible is legally protected only impacts the value that can be attributed to the intangible.

23. The Hague Court of Appeal judgment dated 13 June 1984 (BNB 1986/13).
24. Supreme Court judgment dated 23 Apr. 2004 (VN 2004/27.17).
25. Arnhem Lower Court judgment dated 24 Apr. 2003 (VN 2003/29.3.2).

## 5.2. Legislative or administrative guidance on intangibles

*See* section 5.3.

## 5.3. Ownership of intangible property

As a main rule under Dutch tax law, the actual legal arrangements existing between parties will need to be taken into account as the starting point for determining a company's taxable profit. Consequently, the holder of the legal title to an asset should in principle also be considered the owner for tax purposes.[26]

However, in the 2013 Decree, the State Secretary takes the view that the legal owner of an intangible asset will only be entitled to a limited remuneration from such asset if he does not have the necessary functionality to manage the intangible asset and is therefore incapable of incurring the risk on such asset.[27] The views expressed by the DTA in the 2013 Decree are in line with the views included in the OECD's Action Plans 8, 9 and 10 on Base Erosion and Profit Shifting ("Assure that transfer pricing outcomes are in line with value creation"; the BEPS Actions).[28] Although the DTA have published their view in the 2013 Decree, in our experience they have already applied these views in practice for several years. In that respect, the views of the DTA in respect of transfer pricing are not expected to materially change due to the publications of the OECD in its BEPS Actions on transfer pricing.

In relation to the above it is worthwhile noting that there is scant Dutch case law in which transactions between related entities are recharacterized. Furthermore, the Supreme Court has no such decisions on paragraph 1.65 of the OECD Guidelines. One may take the view on the basis of current case law that the Supreme Court will not easily allow for transactions to be recharacterized or ignored, and only so in case of abuse. Reference is made to the "paper trader" case[29] mentioned in section 6.1.

## 5.4. Transfer pricing methods

Dutch courts are generally willing to accept the transfer prices based on acceptable independent comparables if the taxpayer succeeds in identifying one. An example of such independent comparable was accepted in the judgment of The Hague Court of Appeal.[30] The case concerned a Dutch movie rental company (i.e. renting out movies to third parties). The US parent company granting the movie rights to the Dutch company required a compensation from the Dutch company equal to 79% of its rental income. After taking into account losses available to be set off against its income, the Dutch company would only have realized positive income if the arm's length charge payable to the parent company for the movie rights had been lower than 66%. The court ruled that by referring to margins payable by independent movie rental companies, the company had sufficiently demonstrated that the US company would at least have charged 66% of the rental income when dealing with a third party.

## 5.5. Comparability factors

*See* the OECD Guidelines as regards comparability factors.

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26. Supreme Court judgment dated 3 Nov. 1954 (BNB 1954/356). However, on the basis of Supreme Court judgment of 8 May 1985 (BNB 1986/75), the legal owner will only not be considered the owner for tax purposes if the entire beneficial interest with the asset lies with another party pursuant to a legal relationship between the owner of the asset and that other party (i.e. the economical owner should have the entire upside potential as well as the downside risk on the asset).
27. *See* para. 8 of the 2013 Decree.
28. Actions 8, 9 and 10 include the development of transfer pricing rules (i) that will prevent inappropriate returns from accruing to an entity solely because it has contractually assumed risks or has provided capital, (ii) that will clarify the circumstances in which transactions can be recharacterized; and (iii) for transfers of hard-to-value intangibles.
29. Supreme Court dated 4 Jan. 2013 (no. 11/00762).
30. The Hague Court of Appeal judgment dated 10 May 1984 (BNB 1986/8).

## 5.6. Valuation methods

In practice, the discounted cash flow method is often applied in the Netherlands for the valuation of intangible assets; however, other methods are generally acceptable provided that they result in arm's length prices.

## 5.7. Sale, licensing and other means of transfer or use of intangibles

Under Dutch tax law, profit realized on the sale or licensing of intangibles by a Dutch taxpayer to a foreign or domestic party will be fully subject to tax in the Netherlands (and in the reverse situation the corresponding charges will be tax deductible, either directly or through amortization of the acquisition price). As regards the Dutch transfer pricing consequences of transactions involving intangibles, the State Secretary takes the view in the 2013 Decree that a transfer of (tangible or) intangible assets to a related entity cannot be considered at arm's length if that related entity does not add value to such assets due the absence of appropriate functionality and, therefore, the ability to control the risks in relation to the assets. In the view of the State Secretary, a transfer of such assets will only take place if both parties aim at increasing the overall profitability and if both parties are capable of controlling the risks in relation thereto.

In the view of the State Secretary, an increase in overall (net) profitability resulting from a transferee residing in a low-taxed jurisdiction does not lead to a different conclusion, since in such case the transferee will be fully dependent on the knowledge and skills of the transferor. The State Secretary refers to the example included in paragraph 9.190 of the OECD Guidelines, which relates to the transfer of intellectual property rights to a "shell" company.

Although the State Secretary seems to assume that a transfer of such assets can only be considered at arm's length if the transferee itself disposes of qualified personnel that has the required expertise to control the associated risks, in practice, transfers of intangibles between third parties are often observed where such parties do not have relevant expertise themselves, but obtain this expertise from the group and/or third parties.

## 5.8. Embedded intangibles and package deals

Under Dutch tax law, the components of package deal (usually the provision of a service together with a transfer of an intangible) are not treated differently (i.e. both are either taxable or tax deductible). That may explain the lack guidance in the Netherlands as regards embedded intangibles and package deals. In addition, the Netherlands does not provide for withholding tax on royalties and services, so also from a withholding tax point of view the interest would be limited.

## 5.9. Round-tripping

*See* section 5.11.

## 5.10. Assignment of employees

The DTA have not issued guidelines in relation to the assignment of uniquely qualified and experienced employees to a foreign related entity (i.e. whether such would constitute a transfer intangible property). In line with the guidance provided in the OECD's BEPS Action 8 (Guidance on Transfer Pricing Aspects of Intangibles),[31] such workforce does not constitute an intangible. Instead, the existence of

31. Published on 16 Sept. 2014.

uniquely qualified and experienced employees may need to be taken into account in a transfer pricing comparability analysis.

As regards location savings, in line with the OECD Guidance on Transfer Pricing Aspects of Intangibles,[32] these may need to be considered comparability factors to be taken into account in a transfer pricing analysis.

In the 2013 Decree, the State Secretary mentioned that he considers the OECD Guidelines to have direct effect on Dutch tax law. Therefore, taxpayers may rely on the guidance included in the OECD Guidelines on location savings and workforce in cases where the DTA would argue that the transfer thereof would need to be considered a transfer of intangible assets.

## 5.11. Commensurate-with-income standard

Under certain circumstances, the DTA take the view that the transfer of intangibles against a fixed price is not in line with the arm's length principle if the value at the time of transfer is extremely uncertain and independent parties, in a comparable situation, would only have agreed upon a variable price. In the 2013 Decree, the State Secretary deems a price adjustment clause to be included in the agreement relating to the transfer by a Dutch company an intangible asset to a foreign related entity, where the latter subsequently grants a licence to the Dutch company (or a related Dutch company), of at least 50% of the intangible, unless the taxpayer shows that it is likely that (i) it has business reasons for the transaction and (ii) unrelated entities would have entered into a fixed price agreement as well.

On 17 August 1998, the Supreme Court[33] ruled on the arm's length pricing of know-how transfers. The case concerned a Dutch real estate development company which incorporated subsidiary companies for each new development project. Once the parent company obtained sufficient know-how on a possible project location, this know-how was transferred to a separate project company at no or a low consideration. Subsequently, the project company instructed the parent company to examine the feasibility of the project and later, if the project turned out to be feasible, the parent company was instructed to develop and realize the project for a consideration of 4%-6% of the total contract price. This way, the majority of the profits realized with the project was transferred to the project company. Due to the fact that independent parties do not generally transfer know-how and projects to another party at an early stage of development, no comparable uncontrolled transaction was identified. However, the courts held that the transactions could only be arm's length if the parent company would retain the majority of the profit potential. In good justice, the courts determined the project company's arm's length profit at 2% of the building sum and project costs (referring to the fact that such reimbursement would result in a reasonable return on the project company's equity).

In a case decided by the Supreme Court on 25 June 1969,[34] a taxpayer transferred patents and patent requests to a subsidiary in the Dutch Antilles for a price equal to the development costs. The Court of Appeal previously ruled that the results realized with the exploitation of the patents must be considered deemed capital contributions of the taxpayer into its subsidiary. The Supreme Court ruled that even if it is plausible that a taxpayer transfers intellectual property rights to a foreign group company to benefit from a lower effective tax rate, this does not mean that future royalties should be allocated to this taxpayer

32. *See* n. 31.
33. Supreme Court judgment dated 17 Aug. 1998 (BNB 1998/385).
34. Supreme Court judgment dated 25 June 1969 (In BNB 2010/93).

in the years that the royalties accrued. According to the Supreme Court, the transfer value has to be determined at the moment the intellectual property rights are transferred.

The Breda Lower Court[35] ruled in a case concerning an individual who developed a chain for use in cars. He sold his know-how to a Japanese firm. Two contracts were concluded. The first agreement was a "Patent License Agreement" between (an entity owned by) the taxpayer and the Japanese firm. Under this agreement, the Japanese company obtained the right and licence to use the patents to manufacture the product and to use and sell the product. The second agreement was a "Know-How License Agreement" concluded between the Japanese company and a Swiss trust. This agreement extended all necessary information on the product to the Japanese company. The trust was controlled by the taxpayer. In the year under review, the trust received EUR 1.5 million of royalty income from the Japanese company. The issue was whether the royalties paid by the Japanese company were taxable in the Netherlands as a "result from other activities" of the taxpayer. In the view of the Lower Court, the know-how relating to the royalty payments was provided by way of labour of the taxpayer and it is therefore likely that there was a source of income for the taxpayer. In the view of the court, the taxpayer did not transfer his know-how to the trust. The only task of the trust was to temporally administer the money belonging to the taxpayer. The EUR 1.5 million royalty income was therefore considered taxable income of the taxpayer.

# 6. Intra-Group Services

## 6.1. Sale and use (lease) of tangible property

This section only sets out relevant Dutch case law due to the absence of specific Dutch guidance relating to the sale and use of tangible assets.

On 1 July 1969, the Supreme Court ruled in a case where a Dutch subsidiary of a Swiss AG supplied goods to its parent at prices significantly lower than the prices used with independent purchasers.[36] The Swiss parent company acted as a sales company for the Benelux region. The Lower Court concluded that the intra-group transfer at lower prices was not at arm's length; it took into account a corrected transfer price. This led to an increased profit and a deemed dividend distribution by the Dutch company to its Swiss parent company for the difference between (i) the intra-group price and (ii) the third-party price. The Supreme Court, however, ruled that the Lower Court had not sufficiently analysed the position of third-party purchasers. Because the Swiss parent also acted as a sales company, its position could well deviate from that of independent purchasers. Before applying the CUP method for correcting transfer prices, courts need to determine the comparability of transactions, taking into account the functions and positions of the relevant parties. To determine the appropriate transfer price, the activities performed and risks undertaken by the group companies will always need to be taken into consideration.

In its judgment of 11 October 2000, the Supreme Court ruled in a case concerning a Dutch company which was part of a multinational group engaged in the business of producing and selling coated boards.[37] Until 1990, the Dutch company purchased the boards from a Swiss group company. The activities of the Dutch company consisted of adding a coating to the board and selling back part of the coated boards to the Swiss company at a price equal to the cost price (80% of which constituted the cost of uncoated boards) plus a profit margin of 1%. As of 1991, the activities of the Dutch company

35. Breda Lower Court judgment dated 21 Dec. 2011 (VN 2012/32.2.1).
36. Supreme Court judgment dated 1 July 1969 (BNB 1969/217).
37. Supreme Court judgment dated 11 Oct. 2000 (BNB 2001/142).

were limited to the coating of the boards for the risk and account of the Swiss company. The boards remained in the ownership of the Swiss company. The consideration paid by the Swiss company for these limited intra-group services consisted of the cost price of the coating process increased by a 2% profit margin. As a result of the changed pricing (due to its changed business), the profit margin realized by the Dutch company decreased by 60%. The Lower Court ruled that the reduced transfer price could not be justified. Consequently, the price for 1991 should be corrected in line with the profit margin realized by the Dutch company in previous years. The Supreme Court, however, ruled that the Lower Court's ruling lacked sufficient justification. The Supreme Court stated that intra-group transfer prices should, inter alia, be based on the activities performed and risks incurred by the relevant group companies. Because the Dutch company no longer owned the boards and no longer incurred inventory risks, the activities performed and risks incurred by the Dutch company had significantly changed. The Supreme Court ruled that these changes should have been taken into account by the Lower Court.

On 22 January 1982, The Hague Court of Appeal determined whether a transfer price was arm's length by reference to the margin earned by the foreign related company acting as a purchasing and selling agent.[38] In this case, a Dutch company (BV) incorporated a Netherland Antilles company (NV) to avoid trading restrictions that resulted from the fact that the US supplier of the group was no longer able to deliver goods to the European market due to restrictions included in a license agreement. NV purchased goods from the US supplier, for the risk and account of BV, without a brand and without a factory guarantee. NV transferred the goods to BV at the significantly higher price applicable to the European market for goods with a brand and a factory guarantee. The court ruled that BV could not be said to have acted under arm's length conditions. Third parties would never have granted NV a profit in excess of a commission on the purchased goods. Because NV did not hold any inventory and did not require any supplier's credit, the court determined the commission to be 7.5% of the purchase value.

In a case decided by the Amsterdam Court of Appeal, a foreign subsidiary acquired business assets (machinery) from its Dutch parent company and subsequently rented this machinery back to the Dutch parent company (sale and lease-back).[39] The following items were subject to discussion in the case: (i) the transfer price for the machinery; (ii) the amount of the lease rentals and (iii) whether or not a transfer of "profit potential" ("goodwill") would need to be identified. The court ruled that there was a clear link between the amount of the lease rentals and the transfer price for the machinery. The amount of the transfer price and lease rentals was subsequently determined on the basis of various factors (i.e. choice of comparable machinery, the method of calculating the rental fees, the risk premium, discount percentage, etc.). More importantly, the court did not identify a goodwill realization in this specific case. The court determined that prior to the transfer of the machinery, the Dutch parent company was not involved with renting out machinery and that no business assets to perform this activity were transferred to the foreign subsidiary to perform the rental activities. Furthermore, the court found it important that no employees were transferred from the Dutch parent company to the foreign subsidiary. The foreign subsidiary hired new employees that did not work for the group prior to the transfer of the business assets. On the basis of these facts and circumstances, the court ruled that there could not be a goodwill realization. The outcome of this court case is in our view consistent with the remarks that have been made in chapter IX of the OECD Guidelines in which it is specifically mentioned that the transfer of profit potential does not necessarily result in a goodwill realization.

38. The Hague Court of Appeal dated 22 Jan. 1982 (BNB 1983/109).
39. Amsterdam Court of Appeal dated 11 Febr. 2009 (no. 04/04338).

In a case decided by the Supreme Court, a Dutch company was involved with the purchasing and on-selling of paper.[40] The BV's sole director and shareholder (X) performed the purchasing and on-selling activities. In June 1994, a Swiss company was incorporated. The Swiss company was also involved with the purchasing and on-selling of paper. In the course of a tax audit, it was established that X also performed the purchasing and on-selling activities of the Swiss company in the Netherlands and that the Swiss-resident director of the Swiss company was solely involved with administrative/auxiliary activities of the Swiss company. For this reason, the Lower Courts ruled, and the Supreme Court later confirmed, that the Swiss company should be remunerated on the basis of the cost-plus method, whereby a markup of 15% was applied. Any residual profits of the Swiss company should be allocated to the Dutch company. It was further ruled that certain expenses could not be included in the cost base (i.e. factoring and insurance related expenses).

The contents of the court case seem to be in line with the practical approach of the DTA where they impose adjustments in relation to activities performed by foreign companies with limited substance based on transfer pricing principles. In our view, it is remarkable that the DTA did not take the position that the Swiss company operated through a PE in the Netherlands.

## 6.2. Services

### 6.2.1. Guidance on services

The transfer pricing decree dated 30 March 2001 (the 2001 Decree),[41] currently replaced with the 2013 Decree) replaced the Decree of 25 April 1985 (BNB 1985/196) on intra-group services of a supporting, preparatory and auxiliary nature. This decree indicated that, in principle, a remuneration for intra-group services will be considered arm's length if an appropriate markup was provided. The 2013 Decree stipulates that the transfer price for intra-group services can be determined on the basis of any of the transfer pricing methods included in the OECD Guidelines. In practice, a method based on costs incurred is often applied (i.e. in this respect, the cost-plus method or the TNMM with total cost as NPI are meant). In practice, such arm's length remuneration is often determined by using the cost-plus method, with a cost base including (estimated) direct and indirect costs. Overhead, financing costs and disbursements are generally excluded from the cost base.[42] According to the 2013 Decree, the cost-plus method can only be applied where so-called "routine" services are provided. It should be noted, however, that the 2013 Decree does not provide any authority to support such limitation.

As regards intra-group services, the Supreme Court[43] determined the profits of a Dutch company rendering such services on a cost-plus basis. In the case under review, the banker's association and two Dutch banks were the shareholders of a company that was active in the field of processing payments for its participants. The company was remunerated on the basis of the number of payments processed without a profit markup. In the case, the Supreme Court did not accept the argument of the taxpayer that arm's length pricing generally does not need to exceed a more than reasonable yield on the equity of the servicing company. In the view of the Supreme Court, every separate legal entity should strive for profitability and it was therefore not considered arm's length to refrain from imposing a markup for services rendered. A cost-plus with a mark-up of 5% was determined to be an arm's length price.

40. *See* n. 30.
41. Decree dated 30 Mar. 2001 (IFZ 2001/295M).
42. Reference is made to para. 6 of the 2001 Decree.
43. Supreme Court judgment dated 28 Nov. 1984 (BNB 1989/114).

The Amsterdam Court of Appeal ruled in a case concerning a Dutch company that incorporated a Swiss company in order to commence a foreign sales office.[44] Goods sold were directly transferred from the Dutch company to the local purchasers and invoiced to the Swiss company. Most of the activities were carried out by the shareholder and employees of the Dutch company. The Swiss company, however, had a rented office at its disposal and hired an administrative employee. Even though the existing cost allocation needed to be amended to ensure that the Dutch company would receive an arm's length consideration for the activities performed for the Swiss company, the tax inspector had not demonstrated that the sales activities of the Swiss company did not represent a real function. Consequently, not all of the profits realized by the Swiss company could be attributed to the Dutch company.

A Supreme Court case dated 23 April 2004 concerned a Belgian subsidiary of a Dutch company[45] that acted as central purchasing entity of the group. Rebates relating to its purchases were directly paid to the Belgian subsidiary. The Court of Appeal in Den Bosch was of the opinion that the profits were relatively high compared to the activities and costs of the Belgian subsidiary and that this was the result of the shareholder relation between the Dutch company and the Belgian subsidiary. Part of the profit was therefore allocated to the Dutch company (relating to the purchasing of goods for the Dutch company) based on a cost-plus remuneration of 5% for the Belgian subsidiary.

### 6.2.2. Definition of services

#### Group services

The 2013 Decree identifies intra-group services as an activity performed for a group entity which activity provides the respective group entity with increased economic or commercial value and for which activity the group member would generally be willing to pay. The costs associated with intra-group services need to be on-charged to the group companies that benefit from these services. Costs associated with shareholder activities do not need to be on-charged (i.e. these may be borne by the ultimate parent company). The 2013 Decree provides for a list of activities that in principle qualify as shareholder activities:

i. Activities relating to the legal structure of the company

    1.1. Compliance with the corporate legal requirements of the Civil Code

- Organization, preparation, and holding of shareholders' meetings.
- Activities with regard to the preparation, and approval of the annual accounts and the submission to the Chamber of Commerce.
- The activities of the Supervisory Board to the extent it concerns the statutory supervisory tasks.
- The activities of the works council.

    1.2. Tax compliance of the company itself

- Keeping accounts/records.
- Complying with the obligation to retain records.

44. Amsterdam Court of Appeal judgment dated 15 June 1978 (BNB 1979/188).
45. Supreme Court judgment dated 23 Apr. 2004 (VN 2004/27.17).

- Filing tax returns.
- Complying with the obligation to provide information.

ii. Activities relating to the issuance of shares of the company itself, or comparable securities, on the capital market and activities with regard to the application for and maintenance of the company's listing on a (foreign) stock exchange

- Meeting the admission requirements for a listing on a stock exchange.
- Activities which relate to the listing, for example, preparation of forms which are submitted to the U.S. SEC in connection with the listing, annual accounts, annual reports, etc.
- Membership in the associations and other bodies, which represent the stock exchanges.

iii. Activities relating to compliance with regulatory control of trading in securities

- The introduction and maintenance of the registration system based on the Securities Transactions (Supervision) Act 1995.
- Reporting of securities transactions by employees of the company subject to this legislation.

iv. Activities relating to the corporate governance of the company itself or of the group as a whole

- The implementation of corporate governance prescribed by law or regulations, including the inclusion of a paragraph in the annual report in this respect.
- Reporting on the environmental policy, social policy, and policy on corporate responsibility.

v. Activities relating to the reporting to stakeholder of the company itself or of the group as a whole

- Press conferences and other communications with shareholders and other stakeholders, such as financial analysts, but only to the extent the communication relates to the financial reporting, financial performance, and future expectations of the company itself or the group as a whole.

The above list is exactly the same as the list included in paragraph 1 of the 2004 Decree. However, the following was included in the 2013 Decree: "[T]he activities listed below are deemed to have been performed in the capacity of a shareholder and are therefore not classified as intra-group services *if and to the extent they add no economic or commercial value … and if and to the extent that part of the group would not normally be prepared to pay for them*."

The wording indicated in italics is new compared to the text of the 2004 Decree and it effectively eliminates the "safe harbour" that was provided for in the 2004 Decree. In other words, the fact that an activity is on the list no longer justifies the conclusion that these activities should be classified as shareholder activities, since apparently it also needs to be established that they add no economic or commercial value and that another part of the group would normally not be willing to pay for them.

**Auxiliary services**

Based on paragraph 7.37 of the OECD Guidelines for specific auxiliary services (services in the areas of bookkeeping, legal affairs, tax affairs and personnel affairs), the DTA allow the taxpayer to charge all relevant actual costs (without a markup) instead of determining an arm's length remuneration, unless the DTA can plausibly argue that (i) the activities involved are part of and add more than marginal value to the primary operating processes of the group or (ii) the relevant services are provided to non-affiliated parties on more than an incidental basis.

The actual relevant costs to be charged include the direct and indirect costs related to the relevant support services and the overhead costs. The relevant costs also include financing costs and extraordinary costs (such as severance costs, reorganization costs and non-monetary salary). The foregoing applies regardless of which legal entity within the group performs the support services. For example, the services could be rendered by a dedicated shared service centre. Notwithstanding the above, the DTA allow a taxpayer to pay a markup on service charges by foreign related service providers.

Upon request by the taxpayer, other group services may qualify for no markup, provided the taxpayer can plausibly argue that the activities (i) are not part of, or do not add more than marginal value to, the primary operating processes of the group and (ii) are not provided to third parties on more than an incidental basis. The tax authorities will decide whether to grant the request, keeping in mind the following elements:

- *What is the nature of the activities?*

  In general, the following activities are part of the primary operating processes: manufacturing, purchasing, sales, marketing, product development and research and development.

- *What is the relative scale of the activities within the group?*

  The relative scale of the activities is evaluated on the basis of the total scale of similar activities and activities which are a direct extension of the relevant activities performed within the group as a whole.

- *What is the added value of the activities?*

  An evaluation will be performed whether these activities added more than a marginal value to the primary operating process of the group.

## 6.2.3. Benefit test

It is noted in this respect that the benefit test included in the 2013 Decree differs slightly from the benefit test included in paragraph 7.6 of the OECD Guidelines.

The benefit test included in the 2013 Decree reads as follows: "'Under the arm's length principle, an activity is considered an intra-group service if such service (i) provides the respective group entity with an increased economic or commercial value and (ii) the group member would generally be willing to pay for the activity."[46]

46. *See* the 2013 Decree, para. 6.2.

The benefit test of the OECD Guidelines is worded as follows: "Under the arm's length principle, the question whether an intra-group service has been rendered when an activity is performed for one or more group members by another group member should depend on whether the activity provides a respective group member with economic or commercial value to enhance its commercial position. This can be determined by considering whether an independent enterprise in comparable circumstances would have been willing to pay for the activity if performed for it by an independent enterprise or would have performed the activity in-house for itself. If the activity is not one for which the independent enterprise would have been willing to pay or perform for itself, the activity ordinarily should not be considered as an intra-group service under the arm's length principle."[47]

The benefit test included in the 2013 Decree provides for a double test (i.e. not only does the taxpayer need to substantiate that the services provide it with an increased economic or commercial value, it also needs to substantiate that it would have been willing to pay for such service). Under the benefit test included in the OECD Guidelines, a taxpayer only needs to substantiate that it would have paid for the service itself or that it would have performed the service in-house for itself (i.e. if so, the activity is considered to provide the taxpayer with economic or commercial value to enhance its commercial position). Consequently, the definition of the benefit test in the 2013 Decree seems more restrictive. In addition, the benefit test included in the 2013 Decree does not allow the taxpayer the opportunity, in a situation in which it would not be willing to pay for a service, to substantiate that it would nevertheless have performed the service in-house for itself. Under the 2013 Decree, such activity would not constitute an intra-group service whereas it would under the definition included in the OECD Guidelines.

### 6.2.4. Scope of shareholder expenses

*See* section 6.2.2.

### 6.2.5. Methods applied

In the 2013 Decree, the State Secretary indicated that the DTA have a preference for the direct charge method. However, he also noticed that in case practice issues render the direct charge method inapplicable, the DTA will consider accepting the indirect charge method acceptable as well.[48] In any case, the outcome of the method applied needs be reliable and the results it provides need to be in line with the arm's length principle. The 2013 Decree furthermore provides examples of allocation keys for the use of the indirect method, such as turnover, number of employees or employee expenses. An allocation key based on profit is not considered to likely lead to arm's length results.

### 6.2.6. Cost basis

In paragraph 6.3 of the 2013 Decree the State Secretary states that, in practice, an arm's length remuneration for intra-group services is often determined on the basis of a markup plus (budgeted) direct and indirect costs relating to the services. The markup needs to be determined such that it can cover overhead expenses and an adequate profit.

### 6.2.7. Profit element

*See* section 6.2.6.

47. OECD Guidelines, para. 7.6.
48. In our experience, the direct charge method is hardly ever applied in practice.

### 6.2.8. Documentation

On the basis of article 8b(3) of the CITA, Dutch taxpayers need to include information in their administration (i) which shows in which manner transfer prices have been established and (ii) from which it can be deduced that prices applied would also have been agreed upon between independent entities. Consequently, both the provider and the recipient of the services need to comply with these documentation requirements.

### 6.2.9. Common audit issues

In their audit process, the DTA will need to ensure that the system for intra-group services is applied consistently among all entities of the group and that it can be verified. In practice, Dutch taxpayers may facilitate a tax audit process if they allow the DTA to efficiently check the following items in their transfer pricing documentation:

- qualification of costs for Dutch tax purposes (i.e. deductible intra-group services versus non-deductible head office expenses);
- calculation of the costs allocated to the Netherlands (specifying the Dutch taxpayers' data on which the allocation keys are based) and total costs incurred with all intra-group services;
- reconciliation of intra-group service costs with amounts included in annual accounts; and
- confirmation that the system is applied consistently among all group entities.

### 6.2.10. Tiered services

For Dutch tax purposes, tiered services are not treated differently from other services. The lower tier charges are commonly treated as "disbursements" which do not trigger a profit markup.

### 6.2.11. Non-chargeable services

Other than costs relating to shareholder activities, which do not need to be on-charged, these are deductible for the entity performing the services (*see* section 6.2.2.). Dutch tax law does not include specific restrictions relating to the chargeability of intra-group services.

# 7. Cost Contribution Arrangements

## 7.1. Definition

Dutch tax law does not provide for a specific definition of a cost contribution arrangement (CCA) (or cost-sharing arrangement). In the 2013 Decree, the State Secretary refers to chapter VIII of the OECD Guidelines for CCAs. No case law on CCAs is available in the Netherlands.

## 7.2. Types allowed

The concept of concluding CCAs to centralize certain activities and costs that may benefit all contributing group companies, such as research and development costs or costs of central management, is generally accepted.

## 7.3. Benefit test and criteria

In the 2013 Decree, the State Secretary indicates that benefits derived from a CCA need to be in line with the arm's length principle (i.e. that such benefits may not substantially differ from the benefits that parties would have received outside the scope of a CCA). On the basis of the arm's length principle, the benefit from a CCA needs to be determined on the basis of the functions performed (and the assets used and risks assumed).

While referring to chapter VIII of the OECD Guidelines, the State Secretary indicates that the OECD Guidelines prescribe that the relative contribution of a participant to a CCA should be aligned with the relative share of that participant in the anticipated benefits thereof. He states that the relative contribution of the participant and the relative share in the anticipated benefits should be determined at fair market value. If, however, the average relative value contributed by the various participants to a CCA is more or less the same, one may, under the arm's length principle, use the cost price of the contributions to determine whether each participant's share of the overall expected benefits is in line with each participant's share of the contribution.

The State Secretary further acknowledges that certain countries may not accept the charge of a markup. If such countries, on the other hand, allow a fee to be charged for the capital used for the relevant activities, effectively the same result may be achieved. In such case, the DTA may, in light of the acceptability of charges in certain countries, allow for the use of a particular method, provided such method is in accordance with the OECD Guidelines.

**Example of the 2013 Decree**[49]

Group Company A is engaged in the development, production and sale of consumer products. Group Company B has a staff of two persons with financial and administrative backgrounds. Group Company A carried out initial research into the development of a new product. The market prospects for the product for continent A and continent B are good, but additional research needs to be carried out before the product is ready for production and sale. The expected total value of the development result for continents A and B is expected to be equal. Group companies A and B decide to enter into a CCA under the following conditions:

- Contribution by Company A of the initial development results and development capacity. The total costs in this respect are EUR 5 million. The total value in the open market is EUR 10 million.
- Company B pays Company A EUR 5 million and 50% of the costs to the extent that they exceed the projected costs of EUR 5 million.
- Companies A and B respectively become the economic owners of the development result in so far as this relates to continent A and continent B respectively.
- Company A becomes the legal owner.

In addition to the contract it appears that Company A takes care of the overall management of the project (including the supervision and decisions to be taken).

Conclusion: The functions of Company A encompass the whole R&D activity (ranging from the decisions regarding the nature of the research to be carried out, up to the implementation itself). In doing so, Company A manages the R&D activities completely independently. The contractual provisions stipulate that 50% of the risks associated with this R&D activity will be borne by Company B (Company B pays EUR 5 million and 50% of the costs in so far as they exceed the projected costs and becomes the economic owner of the right developed). However, Company B does not have the required functional

**49. This example is included as "Example O" in the 2013 Decree.**

expertise to manage the risk it incurs associated with the R&D activity. In fact, all of the risk is managed by Company A so that all of the risk needs to be allocated to Company A. The compensation to be received by Company A must be in line with the functions it performs and the risks associated with these functions. Under the agreement with Company B, Company A is incorrectly only remunerated for its development activities in so far as they do not relate to the management and the risk allocated to it. The conditions of the contract entered into between Companies A and B are therefore not at arm's length.

## 7.4. Participants

According to the 2013 Decree,[50] for Dutch tax purposes, an entity will only be considered a participant to a CCA if, in exchange for its contributions under the CCA, it is entitled to part of the rights developed under the CCA, which rights need to be susceptible to being exploited or used by the participant. If, for example, a participant to a CCA only contributes the means of financing of the development under the CCA, under the view expressed in the 2013 Decree, it will not be considered a party to a CCA and will consequently not be considered the owner of rights developed under the CCA.

## 7.5. Conditions to the agreement

Dutch tax law does not impose requirements on CCAs in order to be considered valid.

## 7.6. Amount of contribution and profit element

*See* section 7.3. for guidance on profit elements included in CCA contributions. As regards contributions in kind, these need to be valued at fair market value (i.e. with reference to what a third party would pay for the contribution under comparable circumstances). As regards balancing payments, the DTA would want to ensure that a party making such payments is actually involved in the CCA and that it is not merely financing activities performed by the other participants.

## 7.7. Buy-in and buyout

Dutch tax law does not provide for guidance on buy-in or buyout payments. These payments should be determined on the basis of the relative contribution of the entrant of the CCA in the total anticipated benefits.

## 7.8. Arm’s length adjustments

In the 2013 Decree, the State Secretary indicated that in practice it will be difficult to exactly determine the fair market value of both the contributions of the participants to a CCA and the benefits associated with such CCA. When assessing CCAs, the DTA therefore need to acknowledge that transfer pricing is not an exact science. Nevertheless, the DTA may request taxpayers to substantiate that independent parties under comparable circumstances would also enter into such agreements.

More specifically, in the 2013 Decree the State Secretary refers to chapter VIII of the OECD Guidelines for guidance on the treatment of CCAs. Based on the examples included in the 2013 Decree, on the one hand, a participant’s share of the benefits form a CCA may be adjusted if, for example, that party does not have the required functional expertise to manage the risk it incurs associated with its contribution to the CCA (*see* the example included in section 7.3.). On the other hand, for Dutch tax purposes, a party to a CCA may not be considered entitled to the expected benefits of a CCA, whereas such party may still receive arm’s length payments for its contributions to the CCA.

50. In the guidance included in the 2013 Decree on CCAs (i.e. para. 7), specific reference is made to para. 8.10 of the OECD Guidelines.

### Example of the 2013 Decree[51]

Group company A, group company B and group company C are active in the production and sale of similar consumer products in continent A, continent B and continent C respectively. Group company A has an R&D centre. Group companies B and C employ several product experts who also have knowledge of product development, but they do not have their own R&D centre. Group company A carried out initial research into the development of a new product. The market prospects for the product for continents B and C are good, but major research has to be carried out before the product is ready for production and sale. The expected total value of the result of the development in continents B and C is expected to be equal. The product does not appear to be interesting for continent A.

Group companies A, B and C decide to enter into a CCA under the following conditions:

- Jointly and with equal contributions B and C formulate a research programme for the (continued) development of the product. In addition, they provide equal capacity to manage the project (strategic project planning and management, including supervision and decisions to be taken with regard to the project).
- Contribution by A: The results of the initial research. Costs incurred for the development: EUR 1 million. Value in the open market of the research result: EUR 2 million.
- Contribution by A: Development capacity (personnel + fixed assets): The R&D department of A elaborates on the project plan and submits the details to B and C. Subsequently, the R&D department of A undertakes the implementation of the research. In this connection the R&D department of A regularly renders account to B and C with regard to the course of events. The expected costs associated with this development capacity are EUR 1.8 million. The value in the open market of the development capacity if carried out under an assignment: EUR 2 million.
- Contribution by B and C: They each make a payment to A amounting to EUR 2 million as a compensation for the contribution by A. In addition, each will bear half of the additional costs paid to third parties (procurement of materials, hiring third parties) amounting to EUR 2 million.
- The participants each bear the costs of their own contribution.
- B and C acquire the legal and economic ownership of the development result for continent B and continent C respectively.

Conclusion: A is not a participant in the CCA because A itself cannot derive any benefit from the development result (*see* paragraph 8.10 of the OECD Guidelines). In fact, A sells the initial development result to B and C in combination with the performance of contract research activities for B and C. B and C can indeed both be considered as participants in the CCA because for their contribution (money and management) they acquire a part of the right being developed, which right they can moreover operate/use independently (*see* paragraph 8.10 of the OECD Guidelines). A provides development capacity and the initial development result with a value in the open market of EUR 4 million in total and as a compensation it receives an amount of money of EUR 4 million. Such a compensation is at arm's length. The contribution of both participants in the CCA (B and C) and the benefit to be expected (the right that they acquire) correspond with each other. Although the contract can therefore not be considered as a CCA for A, the compensation arising from this contract can be considered as at arm's length for all participants.

**51. This example is included as "Example N" in the 2013 Decree.**

# 8. Intra-Group Financing

## 8.1. Intercompany loans and deposits

### 8.1.1. Loan amount: Debt or equity

As a general rule under Dutch tax law, the Dutch civil law qualification of a financial instrument as a loan will also be taken into account for Dutch tax purposes. However, based on Supreme Court case law,[52] a loan may under certain circumstances be qualified as equity for Dutch tax purposes. Such equity qualification will take place in case of one of the following three situations:

- a "bottomless pit loan" (i.e. if, at the time of granting, the terms of the loan were such that the borrower could not (partially or fully) repay the loan);
- a "sham loan" (i.e. if the parties concluded a loan agreement, but in fact intended to provide equity); or
- a "participating loan" (i.e. if the terms of the loan are such that creditor's position approximates that of a shareholder). The following features are (cumulatively) decisive in respect of the qualification as a "participating loan": (i) interest on the loan depends (almost) entirely on the profit of the debtor; (ii) the loan is subordinated to other creditors and (iii) the loan does not provide for a maturity date (or a maturity of at least 50 years) and may only be called upon in case of bankruptcy, suspension of payment or liquidation.[53]

As a result of the above equity qualification for Dutch tax purposes, the interest is considered as non-deductible dividend which may become subject to Dutch dividend withholding tax (this may be reduced to zero under the EU Parent-Subsidiary Directive and the implementation thereof in Dutch tax law or under applicable double tax treaties). In addition, a write-off of such "loan" cannot be deducted for Dutch tax purposes.

Outside the scope of the above case law, taxpayers are in principle free as regards the extent to which they choose to finance their operations with debt.[54] Consequently, in case of debt, the return is taxable at the level of the creditor and in principle deductible at the level of the debtor (reference is made to the interest deduction limitations mentioned in section 8.1.2.1.). In case of equity, the return may be exempt for the investor under the participation exemption (article 13 of the CITA) and non-deductible for the investee.

In a case concerning a related-party loan,[55] a Dutch company (i.e. the taxpayer) transferred its investment portfolio to another newly incorporated Dutch company (BV) against an interest-bearing debt (i.e. full debt financing). Due to the negative equity of BV, the taxpayer decided to write off its loan receivable on BV. The tax inspector rejected the deduction of the write-off. In its judgment, the Supreme Court ruled the following:

- Outside the scope of the above case law,[56] a loan will not be recharacterized into equity for tax purposes. However, the taxpayer had assumed the debtor risk on the loan in its capacity of

52. Supreme Court judgment of 27 Jan. 1988 (BNB 1988/217).
53. Supreme Court judgments dated 11 Mar. 1998 (BNB 1998/208) and 25 Nov. 2005 (BNB 2006/82 and BNB 2006/83).
54. From 1 Jan. 2004 until 31 Dec. 2012, Dutch tax law contained a "thin capitalization" interest deduction limitation (i.e. art. 10d of the CITA was abolished as per 1 Jan. 2013 following the introduction of an interest deduction limitation for loans financing exempt participations).
55. Supreme Court judgment of 25 Nov. 2011 (BNB 2012/37).
56. *See* n. 45.

shareholder rather than creditor. The Supreme Court therefore rejected the write-off of the loan as a tax deductible item.

- In order to consider the loan as "non-business-like" (tainted) it should be determined whether the interest rate is at arm's length or can be adjusted to an arm's length rate (i.e. not being a profit participating rate), while maintaining the other conditions of the loan. If an arm's length interest rate cannot be determined, the loan as a whole is considered tainted.
- Whether or not a loan should qualify as "tainted" needs to be determined at the moment of granting the funds. However, during its term a loan may also become tainted as a result of actions of the creditor that are considered not arm's length.
- The arm's length interest rate on a tainted loan is set at the rate that the debtor would have paid if it had attracted the loan from an independent third party under a guarantee of the actual creditor (i.e. a deemed guarantee).
- While a write-off of the tainted loan is not a tax-deductible item at first, it may ultimately be deductible upon liquidation of the debtor pursuant to the Dutch participation exemption rules concerning liquidations."

On the basis of the above case law, one may arguably draw the following conclusions:

- The Supreme Court did not allow for the recharacterization of the loan into equity on the basis of article 1.65 of the OECD Guidelines.[57] Apparently, the Court is reluctant to apply recharacterization of transactions outside the scope of situations of apparent abusive.
- A company may decide to entirely debt finance its assets.
- According to the 2013 Decree, if a tainted loan is provided by a group company that has a credit rating which is worse than the credit rating of the debtor, the arm's length interest rate should be set at a risk-free interest rate as the "deemed guarantee" does not add any value.

### 8.1.2. Interest amount: Arm's length interest rate

#### 8.1.2.1. Interest charged

As regards the transfer pricing consequences of intra-group financing, according to the 2013 Decree it firstly needs to be considered whether comparable financial transactions between independent third parties can be identified. If and to the extent the conditions of an intra-group financial transaction deviate from the conditions under which a similar third-party financial transaction is executed, such conditions need to be adjusted. In the 2013 Decree, the State Secretary indicates that in first instance a price adjustment should be made (i.e. an adjustment to the interest rate). If no appropriate price adjustment can be made, it should be considered whether adjustments to the other conditions of the loan can be made (e.g. as regards guarantee arrangements) in order to render it arm's length. According to the Decree, in extreme cases, a loan may be ignored or recharacterized under paragraph 1.65 of the OECD Guidelines. As mentioned in section 8.1.1., it may be questioned on the basis of the tainted loan case law whether the Supreme Court will also follow such recharacterization.

In the 2013 Decree, the State Secretary takes the position that loans granted to group companies with below BBB- credit ratings (or ratings that become lower than BBB- due to the entering into the financial

57. In this respect, reference is made to M.A. de Lange, P.W.H. Lankhorst & R. Hafkenscheid, *Het negeren van transacties tussen gelieerde partijen*, Weekblad Fiscaal Recht, 7078 (12 Feb. 2015).

transaction) are presumed not arm's length. Consequently, in such cases, the taxpayer should prove that entering into the loan leads to an arm's length result for both the lender and the borrower (i.e. the two-sided perspective). In addition, as regards the "arm's length debt-equity mix", the 2013 Decree notes that if and to the extent the credit rating of a group company falls below BBB- (i.e. "Investment Grade") as a result of intra-group financial transactions, this is considered not arm's length results unless the taxpayer can "prove" the contrary.

Dutch tax law also provides various interest deduction limitations. Apart from transfer pricing adjustment under article 8b of the CITA,[58] the deduction of interest may also be limited on the basis of articles 8c, 10a, 10b, 13l and 15 ad of the CITA.

As regards, article 8c of the CITA, which was introduced as per 1 January 2001, this article provides that interest received and paid on loan agreements (as well as royalties received and paid on licensing/ sublicensing agreements) with related entities and individuals will not be included in the taxable basis if no real risk is incurred by the Dutch company in relation to these activities.[59] The rational for excluding these items from the taxable basis is to ensure that foreign withholding tax will not be creditable. In addition, the Dutch company will still have to report an arm's length remuneration for its services performed in relation to the financing and licensing activities. For the purpose of article 8c of the CITA, a (Dutch) company is deemed to be related if:

- it holds a one-third interest in another company;
- another company holds a one-third interest in the (Dutch) company; or
- a person (whether a company or an individual) holds interests of at least one-third interest in both the (Dutch) company and the other company.[60]

**8.1.2.2. Transfer pricing methods**

As mentioned, Dutch taxpayers may choose any of the five transfer pricing methods described in the OECD Guidelines, provided that the method applied leads to arm's length results for the specific transaction. In our experience, the arm's length character of interest rates is mainly determined on the basis of the CUP method due to the availability of vast amounts of market data. Under the CUP method, an arm's length interest rate may be determined as follows:

- Firstly, the credit rating of the debtor is determined on the basis of financial and non-financial information (e.g. using Moody's RiskCalc database).
- Secondly, the appropriate median credit spread is determined on the basis of the credit rating obtained above (i.e. at the time of granting the loan). This credit spread (generally applied on a reference rate such as LIBOR) corresponds to spreads charged by third parties on loans to debtors with similar credit ratings.
- Finally, the interest rate determined above may be adjusted on the basis of the specific terms and conditions of the intra-group loan (e.g. maturity, currency, subordination, etc.).

58. On the basis of art. 8b of the CITA, the DTAs may consider excessive interest (i.e. interest exceeding an arm's length rate) as a non-deductible deemed dividend (i.e. a "secondary transaction"). As mentioned above, such deemed dividend may be subject to Dutch withholding tax (i.e. a "secondary adjustment"). Under certain conditions, a secondary adjustment may be refrained from (*see* section 14.5.1.).
59. Although the safe harbour for "real risk" included in article 8c of the CITA is similar to the notion included in the FSC Decrees (*see* section 17.3.2.), the latter should be applied on a transaction-by-transaction basis, whereas the first should be applied at the level of the taxpayer.
60. For the definition of related entities, art. 8c of the CITA refers to art. 10a(4) of the CITA.

## 8.2. Guarantee fees

In the 2013 Decree, the State Secretary differentiates between the following situations when determining whether the provision of an intra-group guarantee constitutes a (tax-deductible) intra-group service:

(1) a debtor not being able on a stand-alone basis to attract a third-party loan; and

(2) a debtor being able on a stand-alone basis to attract a third-party loan.

In the first situation, according to the State Secretary, the intra-group guarantee is in principle only granted as a result of shareholder relation. Consequently, such guarantee does not constitute an intra-group service. This means in his view that (i) the guarantee fee is not taxable (and not tax deductible for the debtor) and (ii) a write-off of the recourse receivable of the guarantor on the debtor (i.e. following payments made by the guarantor on the guarantee) is also not tax deductible. In such situations, the State Secretary takes the view that due to the "tainted" guarantee, the third-party loans need to be considered a related-party loan for Dutch tax purposes (i.e. such may have consequences for the tax deductibility of interest payments).

In the second situation, the State Secretary indicates that an intra-group service only exists if a debtor is able to benefit from more favourable conditions following an intra-group guarantee. In such case, a guarantee fee needs to be charged by a Dutch guarantor (or can be charged by a foreign guarantor). The State Secretary indicates that such guarantee fee cannot exceed the difference between (a) the interest at which the debtor would be able to attract loans on a stand-alone basis and (b) the interest at which the debtor can actually attract funding under the guarantee. However, when determining the guarantee fee, the influence of so-called "implicit support" should be eliminated from the calculation. Implicit support relates to the fact that a group debtor potentially has a better credit rating than a "stand-alone debtor" due to being part of a group. The part of the guarantee fee resulting from this implicit support, according to the State Secretary, cannot be considered an intra-group service for which a fee should be charged. In this respect, the State Secretary refers to paragraph 7.13 of the OECD Guidelines.

As regards the determination of intra-group guarantee fees, the 2013 Decree provides the following example. In the example, the following facts are assumed:

- 6% on the basis of the stand-alone rating;
- between 4% and 6% on the basis of the "implicit rating"; and
- 4% on the basis of the group rating.

According to the 2013 Decree, if the guarantee constitutes an intra-group service (i.e. an explicit guarantee for which a third party would be willing to pay a fee), the guarantee fee can in principle not exceed the difference between (i) the interest rate based on the implicit rating and (ii) the interest rate based on the group rating. Consequently, according to the 2013 Decree, in the example, a guarantee fee for the explicit guarantee should range between 0% and 2% (i.e. it cannot exceed 2%).

Unfortunately, the State Secretary does not provide further guidance in the 2013 Decree on the determination of the actual guarantee fee and the allocation, among the debtor and guarantor, of the difference between the "stand-alone interest" and the "guaranteed interest".[61]

In the 2013 Decree, the State Secretary further states that the above guidance on intra-group guarantees is in line with the contents of a Supreme Court case.[62] In this case, the Supreme Court denied the deductibility of payments to a third-party bank based on the taxpayer's joint and several liability for the consolidated debt of the group. According to the Court, the taxpayer had accepted this joint and several liability to serve the interest of the group. The distinction made by the State Secretary (and also by the Supreme Court) in relation to the character of guarantees (i.e. that they are either based on "shareholder motives" or that they lead to more favourable terms) may under certain circumstances be artificial. For example, where a debtor has a solid financial position but a third-party lender still requires a guarantee from a group company as a condition for granting the loan (e.g. because the lender wants to prevent the borrower from becoming less solvable due to actions of the borrower's parent company).

**Case study**

Assume the following scenario: Two companies operating in your jurisdiction (Company A and Company B) belong to the same multinational group with the parent company in Country X. Both companies need some additional financing that has to be obtained from an unrelated bank. Assume that both companies would have stand-alone BBB ratings. However, Company A has obtained an explicit guarantee from the parent in relation to the financing to be obtained from the unrelated bank and as a result it has an AAA- rating for the purpose of obtaining the financing. On the other hand, Company B has not asked for such a guarantee, but merely as a result of belonging to the group is rated as BBB+ by the bank for the purpose of providing the financing. As a consequence, both companies receive loans on more favourable conditions than they would have received based on their stand-alone BBB ratings.

Compare the situation of these two companies based on the following questions:

- Is there any regulation and/or guidance from the tax authorities with regard to intercompany guarantees?

The 2013 Decree provides guidance on the tax treatment of intra-group guarantees. *See* section 8.2.

- Under what conditions is the payment of a guarantee fee considered to be consistent with the arm's length principle?

Under the guidance issued by the DTA in the 2013 Decree, one would in first instance need to consider whether the debtor (i.e. the recipient of the guarantee) would have been able to attract a third-party loan on a stand-alone basis. If this is not the case, the guarantee would not constitute an intra-group service and consequently a fee on such guarantee would not be taxable.

If the debtor would be able to attract a third-party loan on a stand-alone basis, the fee charged for the guarantee would in principle be taxable. However, when calculating the guarantee fee, one would need to eliminate the influence of implicit support (i.e. a debtor benefitting from a better credit rating than a comparable stand-alone debtor solely due to it being part of a group). In the case at hand, the implicit

61. On the basis of the *GE Capital* case (*General Electric Capital Canada, Inc. v. The Queen*, 2009 TCC 563), one may take the position that the actual guarantee fee would need to be determined on the basis of bargaining powers of the parties involved.
62. Supreme Court judgment dated 1 Mar. 2013 (BNB 2013/109).

support follows from the fact that Company B has a better credit rating (i.e. BBB+) than a comparable stand-alone debtor (i.e. BBB-) and can be quantified as the difference between the two ratings. On the basis of the guidance of the 2013 Decree, an arm's length guarantee fee for Company A cannot exceed the difference between the guaranteed rating (i.e. AAA-) and the "implicit rating" (i.e. BBB+).

In fact, economic rationale would suggest that an arm's length guarantee fee would in any case be less than the above-mentioned difference, because otherwise Company A would be indifferent between the situation with and without the parent guarantee (i.e. the interest on the loan without the guarantee would be equal to sum of (i) the guarantee fee and the (ii) interest on the loan with the guarantee). Although not reflected in the 2013 Decree, at arm's length one would expect the parties to the guarantee (Parent Company and Company A) to allocate the guarantee benefit between them on the basis of their respective bargaining powers.

- Which method could or should be used to establish an arm's length fee to be paid by Company A (CUP, cost-benefit analysis, cost of capital, analysis of fees paid on CDS on bonds with comparable characteristics as the guaranteed transaction or contingent put option)? How would the analysis differ if Company A were to have an additional source of protection?

Dutch taxpayers have a certain degree of freedom as regards their choice for any of the five transfer pricing methods included in the OECD Guidelines. However, the method applied will need to lead to arm's length results. In practice, the CUP method is often used to determine arm's length guarantee fees.

## 8.3. Cash pooling

Although no specific Dutch guidance exists in relation to the tax treatment of cash pools, the DTA show increasing interest in cash pool structures (including their transfer pricing aspects).[63] Based on practical experience, special attention is mainly required where:

(1) cash pool deposits are very large (i.e. even small corrections on interest rates applied may have a large impact on its profit);

(2) cash pool participants have consistent surpluses or deficits (i.e. it may be argued that a long-term cash pool position would for tax purposes need to be considered a long-term loan which should carry a higher long-term interest rate); and

(3) a large difference exists between cash pool interest paid and received (i.e. the DTA may challenge the arm's length character of the transaction arguing that cash pool participants could have obtained better alternatives for the use of these funds).

Although a multitude of variations in types of cash pools exists, two main forms can be distinguished: (1) the physical cash pool and (2) the notional cash pool. Both of these types are further discussed below.

Within a physical cash pool, regular transfers are made between bank accounts of the cash pool participants and the bank account of the cash pool leader (the CPL). Consequently, within this type of cash pool actual transfers of funds take place from the accounts of the participants to that of the CPL (i.e. the master account) and vice versa (i.e. it creates intra-group payables and receivables between

63. It is noted that the Netherlands provides an attractive jurisdiction for treasury and/or cash pool entities due to the absence in the Netherlands of withholding tax on interest payments and the extensive Dutch tax treaty network (providing for reduced withholding tax rates on interest), as well as the possibility to obtain the benefits of the EU Interest and Royalty Directive.

the CPL and the cash pool participants). In case of a deficit on the master account, the CPL may borrow additional funds from the bank on which it needs to pay interest. Where the master account shows a surplus, the bank will need to pay interest to the CPL.

In a notional cash pool, the funds of the individual participants are not actually transferred to a central master account, but remain in the (local) bank accounts of the cash pool participants. However, instead of calculating the (debit and credit) interest on each individual account of the cash pool participants, the bank actually calculates the interest after netting individual positive and negative accounts (i.e. the cash pool benefit).[64] The bank subsequently contributes the cash pool benefit to the CPL or, alternatively, sets off the cash pool benefit against the interest payable of the participants. In order to engage in a notional cash pool, banks usually require all cash pool participants (or the ultimate parent company) to issue guarantees for the deficits of the other participants.

As regards the tax treatment of cash pools, article 8b of the CITA requires that for the determination of taxable profit all transactions of a taxpayer with related entities should be performed under arm's length conditions. This means that one would need to substantiate and document the arm's length character of (i) the interest rates applied on cash pool accounts, (ii) the remuneration for the CPL and (iii) the allocation of the cash pool benefit. Where appropriate, a distinction will be made as regards the transfer pricing consequences of the above transactions between (a) physical cash pools and (b) notional cash pools.

**Arm's length interest rates**

With notional cash pools, interest is generally paid and received to and from third-party banks. Although these transactions are engaged in with third parties, they form part of an agreement with other related entities and may therefore be influenced by group (i.e. non-arm's length) relations. With physical cash pools, intra-group payables and receivables occur and it would therefore need to be determined whether the interest paid and received on these transactions is at arm's length.

Arm's length interest rates on cash pool deficits and surpluses would need to be determined on the basis of the creditworthiness of the debtor (i.e. the cash pool participants and/or the CPL). Stand-alone credit ratings of the debtors may be determined on the basis of financial market information (e.g. Moody's RiskCalc database). Subsequently, based on the credit rating obtained, the applicable credit spread can be determined (i.e. the margin over a base rate such as LIBOR). *See* section 8.1.2.1.

In practice, however, because the factors applied in calculating the arm's length interest rates within a cash pool will be subject to constant change, it will be quite burdensome to prepare such analysis for each individual cash pool participant. Therefore, as a practical solution, it may be decided to apply a LIBOR base rate plus and minus a limited credit spread, provided that cash pool participants have continuously changing deficit and surplus positions. Because participants in such situation would have more or less offsetting interest income and expenses, this arguably reduces the incentive of the DTA to challenge the level of the interest rates applied.

**Arm's length CPL remuneration**

As with any intercompany transaction, the remuneration for the CPL should be based on risks incurred, functions performed and assets used. With notional cash pools, which do not create intra-group

64. Further benefits of a cash pool are (i) the possibility to negotiate more favourable interest rates with a bank when all participants in a cash pool act together and (ii) increase efficiencies through central management of group cash flows.

payables and receivables, a CPL may depending on its risk profile be similar to that of a limited risk service provider. The OECD Guidelines state that for the provision of services, the cost-plus method or the TNMM with total costs as NPI is often the most reliable method to determine arm's length conditions.[65] The CPL of a physical cash pool generally plays a more important role within the cash pool. The CPL and the participants with a cash pool surplus will incur the risk that the other participants of the cash pool may default on their obligations towards the cash pool (i.e. they incur the credit risk). The arm's length remuneration for a "physical CPL" may be based on the remunerations for FSCs (*see* section 17.3.1.). Where a CPL's activities are similar to those of an in-house bank, it may be entitled to a more substantial remuneration.

**Cash pool benefit**

If, within a physical cash pool, the interest rates applied are arm's length, the cash pool benefit is by default allocated to the participants of the cash pool that incur the credit risks (i.e. due to the fact that the interest rate that these participants receive is based on the debtor risk). No separate payments are required to allocate the cash pool benefit. If, however, a practical solution is applied for the determination of the interest rates (e.g. a limited credit spread above and over LIBOR), the cash pool benefit is allocated to the participants with a cash pool deficit. The interest that they pay to the cash pool will likely be lower than the interest that they would have had to pay without a cash pool. If, however, the participants frequently switch between a cash pool surplus and deficits, the cash pool benefit should on balance be allocated correctly.

In a notional cash pool, the cash pool benefit may be distributed by the bank to the CPL. As a result, the entire cash pool benefit could be allocated to the CPL. However, a notional CPL should generally only be remunerated for the services performed, with a markup on costs. What should not be allocated is the entire cash pool benefit.[66] Where the cash pool benefit is credited with the interest payable of the cash pool participants, the benefit is allocated to the participants who have a debt to the cash pool, as they pay less interest than what they would have had to pay without the cash pool.[67] Such may not be arm's length.

# 9. Business Restructuring

## 9.1. Specific rules on business restructuring

Dutch tax law does not contain specific transfer pricing rules relating to business restructuring. However, in the 2013 Decree, reference is made to business restructurings and to the guidance included in chapter IX of the OECD Guidelines, which is applied by the DTA in practice. It is noted in this respect that although Dutch taxpayers may rely on the interpretation of Dutch tax law included in decrees issued by the State Secretary, they are not bound by them. Consequently, Dutch taxpayers are not bound by the view of the State Secretary as regards the transfer pricing aspect of business restructurings as included in the 2013 Decree. *See* section 2.3. for the legal status of decrees issued by the State Secretary on transfer pricing.

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65. It is noted that such CPL may be considered as an "agent" and could therefore not be considered the beneficial owner of the interest income by source countries. As a result, such counties may decide to deny treaty benefits to such entities.
66. This would be different if the CPL issues a guarantee to the bank for the debts of all the group companies.
67. If the participants in a notional cash pool are required by the bank to issue a guarantee for the deficits of the other participants, the credit risk shifts from the bank to the participants with a cash pool surplus. Under arm's length conditions, the cash pool benefit would therefore be allocated to the participants with a surplus on the cash pool (e.g. by charging guarantee fees to the other participants).

Chapter IX of the OECD Guidelines defines a business restructuring as “the cross-border redeployment by a multinational enterprise of functions, assets and/or risks.” It may also involve the transfer of valuable intangibles and/or the termination or substantial renegotiation of existing arrangements. In practice, the guidance included in the OECD reports (i.e. on which the current chapter IX of the OECD Guidelines is based) has been applied by the DTA in discussions with Dutch taxpayers for several years. As regards the transfer pricing aspects of business restructurings, the DTA indicate that the starting point is that the arm’s length principle should not be applied any differently to restructurings or restructurings of part of a group than to structures which were originally set up in this way.

In our experience, in discussions with Dutch taxpayers, the DTA apply the following theoretical framework as regards the application of the arm’s length principle to business restructurings:

(1) risk considerations;

(2) arm’s length restructuring; and

(3) post-restructuring remunerations.

**Risk considerations**

The DTA acknowledge that contractual arrangements between the parties form the starting point for the allocation of risks between the parties and their transfer pricing consequences. However, if these arrangements differ from economic reality, the DTA will challenge the contractual allocation of risk (i.e. whether the actual conduct of parties is in accordance with the contractual risk allocation). According to the DTA, the conduct of unrelated parties will be the result of conflicting interests, on the basis of which they generally hold each other to the contract. Since conflicting interests may not exist between related parties, their conduct may differ in practice from what has been agreed on contractually, or they may not have formalized arrangements in a contract. In such case, according to the DTA, the correspondence or communications between the parties may provide an indication of the arrangements.

The DTA further regularly question whether the contractual allocation of risks is at arm’s length. In the first instance, this will need to be determined on the basis of a comparison between the actual risk allocation and the risk allocation in a similar transaction between unrelated parties. If, however, similar transactions between unrelated parties are unavailable, one would need to determine whether unrelated parties would have allocated the risks in the same way under similar circumstances. According to the DTA, where no similar transactions between third parties are available, risks will generally be borne by the party which has relatively more control over the risk. The term “control” should be understood as the capacity to (i) take decisions about risks and (ii) decisions on how risks should be managed. In this respect, the DTA consider it necessary for the company to have employees and directors who can manage the risk (and actually do so). Although the DTA recognize that day-to-day activities in relation to risk management can be delegated, the person delegating should be in a position to interpret the outcome of the activities outsourced and take decisions on that basis.

In our experience, the DTA extend the above view to include the situation in which neither of the parties can influence the risk (e.g. political risk or economic developments). In such case, they are of the view that the risk should be borne by the party which is in a better position to spread these uncontrollable risks (i.e. the most risk-diversified party).[68] In addition, the 2013 Decree seems to suggest that “relevant functionality” is the only relevant criterion for arm’s length allocation of risk. According to the 2013

68. *See* paras. 11 and 12 of the 2013 Decree.

Decree, a party to a transaction will only be considered to have "relevant functionality" if such party has its own employees who are capable of adding value and managing the risks.[69]

### Arm's length restructuring

Due to the fact that transactions involving a business restructuring do not often take place between unrelated entities, it needs to be determined whether independent parties would have been willing to agree to the same conditions under comparable circumstances. In order to increase their understanding of the business restructuring and ultimately in order to determine whether they accept the business restructuring, the DTA generally question:

- the business reasons for the restructuring and the expected benefits;
- the other options realistically available to the parties involved; and
- how the changes influence the functions, assets and risks of the entities involved.

Subsequently, for the purpose of determining whether an arm's length compensation for the restructuring is required, it needs to be established whether (i) rights or other assets have been transferred which have a value and/or (ii) if the termination of existing agreements would require compensation.

### Transfer of rights or assets

In order to determine whether rights or assets were transferred, it will be necessary to consider whether the transaction is commercially rational for both parties involved and whether a fee/reimbursement would need to be paid. Various factors may play a role in this respect, including:

- the other commercial options available to the parties on the basis of the rights and assets each of them had before the restructuring;
- the expected yield from the transaction for each of the parties. One may argue that it would be commercially rational for both parties if risky activities with a highly volatile yield are exchanged for low-risk activities with a lower, more stable yield (i.e. specifically if the party allocated the risky activity is more diversified than the other party);
- the compensation for the transferor in connection with the transfer of valuable rights and/or assets; and
- the consequences for the conduct of the business following the transfer as a result of the new risk profiles of the transferor and transferee.

In our experience, the DTA applied the view included in the OECD Guidelines that a reimbursement may only be required in case of a transfer of assets and/or rights. A transfer of profit or loss potential or a difference in profitability does not in itself justify a reimbursement. However, it seems that the DTA have recently shifted their view in case of an "abusive situation" and approach the question from the other position. According to the DTA, in an "abusive situation", the difference in profitability before and after the business restructuring is taken as the starting point for the determination of a reimbursement. Subsequently, this amount will only be reduced to the extent that the taxpayer is able to substantiate that no assets or rights were transferred as a result of the business restructuring. This different approach

69. *See* paras. 8 and 11 of the 2013 Decree.

of the DTA will lead to a substantial increase of disputes and proper documentation of the business restructuring will consequently become more important.

As regards a transfer of rights and other intangible assets, it will be necessary to identify the intangible asset and to determine the party who owns it. Subsequently, it will be necessary to determine the value of the asset if it is transferred. Finally, the question arises as to what licence fee should be payable if the intangible asset continues to be used within the transferor's group. In addition to transfers of individual assets, a business can also be transferred as a going concern. In that event, an amount will normally be included for goodwill or bad will as part of the total compensation for the assets and liabilities.

**Termination compensations**

Where existing contractual arrangements are renegotiated or terminated, one of parties may clearly be disadvantaged. In such a case there could be grounds for making a payment for the compensation of damages. The following elements may play a role in determining whether, at arm's length, a compensation is required:

- the details of the renegotiated or terminated agreement, if any;
- whether terms of the agreement are at arm's length (i.e. the DTA require that the agreement be commercially rational);
- whether the legislation of the jurisdiction under which the agreement was concluded provides for compensation for damages to be paid (including the extent to which a party would be successful in court proceedings in obtaining such compensation); and
- the willingness of an independent party under comparable circumstances to pay compensation if the other party has suffered losses as a result of the renegotiation or termination of the agreement.

In a transaction between independent parties, these will generally hold each other to the terms of the contract due to their conflicting interests. However, even in transactions between third parties, damages may not actually be paid (e.g. because of the potential negative impact of such claim on the relevant party's image, the (high) cost involved with legal proceedings and/or the existence of significant market power of the other party). Furthermore, if either of the two parties with a view to a long-term relationship has made substantial investments in tangible fixed assets and personnel, this may be a reason to require compensation for damages. Civil (case) law provides guidance as regards the right to compensation for damages.

**Post restructuring remunerations**

The DTA agree with the guidance included in the OECD Guidelines that the arm's length principle should be applied similarly to transactions that were not part of a business restructuring. However, to the extent that transactions continue to take place between the parties after the business restructuring, in some cases the pricing of these transactions needs to be viewed in conjunction with the remuneration for participating in the business restructuring itself. In many cases, the functions of the entities involved in the business restructuring change as a result of the restructuring. Consequently, the risk incurred and the remuneration agreed will also change.

## 9.2. Use of anti-avoidance rules

According to the 2013 Decree, the arm's length principle is based on a comparison of the conditions entered into by related entities with the conditions entered into by independent entities in similar transactions under similar circumstances. If the conditions entered into between related entities differ from those which would have been agreed on between unrelated entities (i.e. the price), according to the 2013 Decree, the consequences thereof may require an adjustment of the taxable profit (i.e. an adjustment of the price). If other conditions (i.e. other than the price) differ, the consequences of such non-arm's length conditions may be either adjusted or ignored for Dutch tax purposes. According to the DTA, these adjustments are based on the arm's length principle. Dutch courts, however, are not clear on that justification.

Under paragraph 1.65 of the OECD Guidelines, in exceptional circumstances, tax authorities are allowed to disregard the transaction actually undertaken in their examination of the controlled transaction and, instead, question the structure of the transaction. According to the 2013 Decree, such exceptional circumstances occur in situations where related entities enter into transactions (i) which independent parties acting rationally in similar circumstances would not have entered into and (ii) for which no arm's length conditions can be found. In such exceptional cases, according to the 2013 Decree, it should first be examined whether the transaction can be recharacterized as a different transaction for which arm's length conditions can be found. However, if recharacterization does not lead to arm's length results, the consequences of the transaction will be completely ignored for taxable purposes.

According to the 2013 Decree,[70] the following general principles are relevant in determining whether the conditions of a transaction will need to be adjusted, recharacterized or ignored for tax purposes:

- on the basis of the arm's length principle related entities are deemed to strive for profit maximization;
- unrelated entities would only enter into a transaction if no (realistically) other more attractive alternatives are available to them;
- a comparison of the conditions of a transaction has to take place from the perspective of all parties involved in the transaction;
- factors involved with the examination of the commercial rationality of a risk allocation are the extent of control over the risk and the financial capacity to bear the risk;
- unrelated entities are considered to act rationally;
- a transaction will only be engaged in by unrelated entities if parties expect to increase their combined profits (the so-called "two-sided perspective");[71]
- a party will only be able to contribute to the increase of combined profits if it has the required functionality (i.e. if it has its own employees); and
- risk relating to a transaction will be allocated to the party which is able to manage these risks and uncontrollable risks should be borne by the "most risk-diversified" party.

70. *See* de Lange, Lankhorst & Hafkenscheid, *supra* n. 57. In this article, the authors discuss these "general principles" in more detail. It is also noted in this respect that Dutch taxpayers are not bound by the view of the State Secretary as regards the transfer pricing aspect of business restructurings as included in the 2013 Decree. *See* sec. 0.1. for the status of decrees issued by the State Secretary on transfer pricing.
71. *See* the 2013 Decree, para. 12(b).

The DTA generally apply the above interpretation of the arm's length principle in order to determine the appropriateness of business restructurings. The sham transaction doctrine, substance over form, general anti-avoidance rules and/or *fraus legis* are not usually applied by the DTA in this respect. *See* section 8.1.1., where, on the basis of Supreme Court case law, "sham loans", "bottomless pit loans" and "participating loans" are considered equity for Dutch tax purposes. Furthermore, the principle of *fraus legis* was developed in Dutch case law to prevent the consequences of abusive situations. In general terms, *fraus legis* applies where a taxpayer acts (i) contrary to purpose and object of the law and (ii) with the aim of preventing tax from being levied.

## 9.3. Transfer of a going concern

As mentioned in section 9.1., a business may also be transferred as a going concern. In such case, it would need to be determined whether an amount for goodwill or bad will needs to be recognized as part of the assets and risks transferred. Whether this is the case depends on the valuation of the business transferred.

## 9.4. Termination or substantial modification of existing arrangements

*See* section 9.1. (under "Termination compensations").

## 9.5. Permanent establishment issues

On the basis of article 17(3)(a) of the CITA, income of a Dutch PE of a foreign (corporate) taxpayer is taxable in the Netherlands.[72] It is noted in this respect that Dutch tax law does not in principle provide for a definition of "permanent establishment".[73] Due to the absence of specific guidance in Dutch tax law on "permanent establishment" and considering that most Dutch tax treaties contain a PE article in line with the OECD Model, Dutch case law refers to the OECD Model and the Commentary thereto when dealing with PEs.

As regards centralized business models (e.g. a Dutch limited risk entity performing activities under an agreement with a foreign principal and assuming that the actual activities in the Netherlands exceed the scope of the agreement), the DTA in principle have two options available to challenge the remuneration for the activities performed in the Netherlands. The DTA may claim that (i) the principal has a PE in the Netherlands alongside the Dutch entity and subsequently attribute arm's length profits of the principal to that Dutch PE (i.e. the "PE correction") or (ii) a correction to the profits of the Dutch entity considering that its remuneration is not in line with its functionality (i.e. the "transfer pricing correction").

Although these alternatives attempt to correct the profit of two different legal entities (i.e. in the first alternative the Dutch PE of the principal and in the second alternative the Dutch entity itself),[74] the amount of profit taxable in the Netherlands under both alternatives will often be the same. In our experience, the DTA have a preference for the "transfer pricing correction", arguably because this option does not require the recognition of a PE and both options in theory have the same end result.

72. For foreign individual taxpayers, Dutch taxation rights as regards a PE situated in the Netherlands are included in art. 7(2)(a) of the ITA.
73. The decree on the avoidance of double taxation 2001 contains a definition of a PE ("fixed place of an enterprise through which the activities of that enterprise are being wholly or partly carried on"). However, this definition is arguably only relevant for the purposes of the decree itself.
74. Although the "PE correction" and the "transfer pricing correction" are both based on the arm's length principle, the "PE correction type" may very well lead to a higher profit allocation compared to the latter. This is caused by the fact that these corrections are based on different notions (i.e. "significant people functions" vs "control over risk". The following example may illustrate the effects of these different notions. Suppose, on the one hand, that the directors of a company decide to subcontract the management of credit risks to a third party. This will generally result in the third party only receiving a fee for its services provided. It will generally not acquire all the profits and losses relating to these risks. On the other hand, if an entity transfers the management of credit risks to a person working in a foreign PE of the same entity, then the entire profits and losses relating to the credit risks will in generally be attributed to that PE.

This preference is currently also reflected in the PE Decree (*see* section 10.1.)[75] in which the State Secretary states that the DTA will in principle not attribute separate profits to an agency PE of a principal when the agent receives an at arm's length remuneration. Consequently, if after any type of business restructuring, the Dutch restructured company is remunerated for its (reduced) functionality on an arm's length basis, the DTA will normally not consider the existence of a PE in the Netherlands of the foreign principal company to which profits need to be allocated.

## 9.6. Conversion of full-fledged distributor into commissionaire or low-risk distributor

*See* section 9.1. for the transfer pricing aspects of business restructurings in the Netherlands.

### Case study: Conversion of a full-fledged distributor into a limited-risk distributor

#### Before conversion

The Case study group is in the business of manufacturing and distributing car spare parts. The Case study group operates in a number of countries, including the country under analysis, where it established a subsidiary (referred to here as Company *A*) which markets and sells car parts. Company *A* is considered to be a full-fledged distributor. The holding company of the group (HoldCo) is established in Country *B*.

Company *A* conducts marketing activities and performs post-sales services for customers. Company *A* is responsible for its marketing strategy and has developed its own marketing intangible (customer list). It provides warehousing and bears inventory risk, and is responsible for logistics related to inventory and sales.

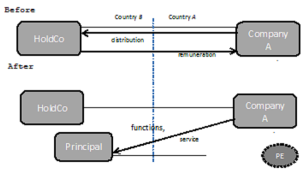
Assume that in Year 1, Company *A* made a profit of 100 per unit sold. Due to the change in business policy, the group will undergo a restructuring of certain lines of business.

#### After conversion

Company *A* is to be restructured into a limited-risk distributor by centralizing the functions in the principal located in Country *B*. Most functions – and risks (inventory, credit, currency and similar risks) – will be transferred to the principal company. After the restructuring, Company *A* will follow the marketing procedures and policies set by the principal, but it will maintain the contact with customers and execute the sales. However, the person who will be setting the marketing strategy at the principal level is a former director of Company *A*, to be employed by the principal but performing his daily activities at the premises of Company *A* in Country *A*. The customer list developed by Company *A* will be sold to the principal, but will be used daily by Company *A*. As a consequence of the conversion, in Year 2 its profit will most likely drop from 100 to 30 per unit sold.

75. Decree dated 15 Jan. 2011 (IFZ 2010/457M), para. 5.3.

The conversion can be illustrated as follows:




**Questions and answers**

As a first question, it would need to be considered whether the business restructuring itself (i.e. the conversion of the full-fledged distributer into a limited-risk distributer) is at arm's length (i.e. whether independent parties would also have been willing to agree to the same conditions in comparable circumstances). In this respect, the DTA may question the business reasons for the restructuring and whether the restructuring is commercially rational from the perspective of both parties involved. According to the 2013 Decree, in extreme cases, the DTA may argue that the consequences of the transaction will be completely ignored for taxable purposes. In the case at hand, one would expect that the business restructuring is commercially rational for both parties involved, if Company A exchanges a risky activity generating highly volatile returns with Company B (i.e. the Principal) for a less risky activity which generates lower, more stable returns. The transaction may also be rational from the perspective of Company B considering that it as the Principal (i.e. generally the most risk-diversified party) will be better able to spread the risk on the activity transferred with the other risks it incurs. In our experience, the DTA did not historically require a reimbursement to be paid just because of a change in profit potential. A change in profit, however, could be an indication that assets have been transferred or contracts have been changed without proper grounds. Currently, for "abusive situations", the DTA has indicated that it will take the view that a reimbursement will be required (i.e. consisting of the difference between the profitability before and after the business restructuring), unless the taxpayer is able to substantiate that no assets or rights were actually transferred.

Subsequently, one would need to determine whether assets and/or rights were transferred as part of the business restructuring and, if so, whether a compensation would be required. As regards the sale of customer list, Company A may recognize such transaction for Dutch tax purposes because of the existence of the contractual arrangement with Company B and the existence of similar transactions between unrelated entities. In addition, the transaction could be considered in line with the guidance included in the 2013 Decree if the transaction would also be economically rational from the perspective of Company A (assuming, for example, that the employee of company B will also manage customer lists of other countries and that it will allow Company A to benefit from marketing developments in these countries; *see* section 9.2.).

In the case at hand, the director of Company A became an employee of Company B after the business restructuring. Because the employee of Company B performs its daily activities at the premises of Company A, the DTA could claim that this employee in fact carries out the business of Company B (i.e. the Principal) at the premises of Company A. As a result thereof, Company B could be considered to have a PE in Country A under article 5(1) of the OECD Model. In such case, the DTA will arguably not consider themselves bound by the PE Decree,because the guidance included in the PE Decree only related to agency PEs under article 5(6) of the OECD Model.[76]

Furthermore, the sale to and the subsequent use of the customer list by Company A would not require a correction provided that the purchase price as well as the royalty fee payable by Company A are at arm's length. However, if at the time of transfer the value of the intangible is uncertain and if independent parties in comparable situations would only have agreed on a variable price, the DTA may take the view that the transfer against a fixed price is not at arm's length. According to the 2013 Decree, a price adjustment clause is deemed to have been concluded in case of a transfer of an intangible asset by a Dutch company to a foreign related entity, where the latter subsequently grants a licence to the Dutch company (or a related Dutch company), of at least 50% of the intangible. According to the 2013 Decree, the price adjustment clause will only not be deemed to exist if the taxpayer reasonably argues that (i) the transaction was based on business reasons and (ii) unrelated entities would have entered into a fixed price agreement as well.

As regards the arm's length remuneration of Company A after the business restructuring, in our experience, such limited risk distribution activities are generally remunerated on the basis of the TNMM with "revenue" as NPI (i.e. "return on sales").

As regards the question of termination compensations being required, this primarily depends on whether formal agreements exists and if they provide for a damages clause. Absent such clause, the remaining term of a renegotiated or terminated agreement or the amounts invested by one of the parties to the agreements could be relevant for compensation payments being required. In our experience, the DTA would generally require compensation if Company A's chances of being awarded compensation in legal proceedings are high.

In principle, the business restructuring should not have VAT consequences as Company A continues its legal relation with the customers on the one hand and the Company B (or another group supplier) on the other hand. However, in case the remuneration for Company A is not separately charged but instead is included in the purchase price of the goods sold by Company A, possible transfer pricing adjustments to such price (whether year-end adjustments or corrections suggested by the tax authorities) may give rise to VAT return filing consequences. In such case, the purchase price for the goods will need to be adjusted and consequently VAT returns. Although the DTA in the scope of the VAT generally accept such adjustments, in our experience tax authorities of other countries are not as flexible. From a practical perspective, it may therefore be considered to separately charge the remuneration for Company A (i.e. and not include it in the purchase price of the goods sold by Company A).

Finally, in practice, the DTA often disallow the deduction by Dutch companies of expenses relating to business restructurings. It is noted in this respect that (contrary to many other jurisdictions) Dutch tax law allows for losses of Dutch corporate taxpayers to be carried back 1 year (*see* section 9.10.). Consequently, expenses incurred by a Dutch company relating to a business restructuring may effectively be used to offset profits of that company of the previous year (i.e. if such expenses are considerable, the restructured company is able to reclaim a substantial part of the tax paid on the previous year's profit). The DTA may reject the deduction of these expenses for tax purposes claiming that the restructuring itself is not based on business reasons.

76. In para. 5.3 of the PE Decree, the State Secretary indicates that the DTA will in principle not consider the existence of an agency PE of a principal in the Netherlands when the agent receives an at arm's length remuneration for its activities.

## 9.7. Conversion of full-fledged manufacturer into toll or contract manufacturer

*See* section 9.1. for rules or regulations on the transfer pricing aspects of business restructurings in the Netherlands.

### Case study: Conversion of a full-fledged manufacturer into a toll manufacturer

#### Before conversion

The Case study group is in the business of manufacturing and distributing car spare parts. The Case study group operates in a number of countries, including the country under analysis, where it has a subsidiary (referred to as a Company *A*), which designs and manufactures car parts. Company *A* is considered a full-fledged manufacturer. The holding company of the group (HoldCo) is established in Country *B*.

Company *A* owns all necessary intangible property (IP)(e.g. patents, know-how) related to the products it manufactures. It is responsible for all the activities related to the design, production planning and scheduling, sourcing and procurement, inventory management, warehousing and logistics, and quality control, and bears warranty risk. Company *A* also looks for customers/new distributors and maintains/ develops the relationships with the distributors/customers. Thus, it bears all the risk related to the manufacturing process (market risk, inventory risk, warranty risk and R&D risk). Assume that in Year 1, Company *A* made a profit of 100 per unit produced. Due to the change in business policy, the group will undergo restructuring of certain lines of business, including that carried out by Company *A*.

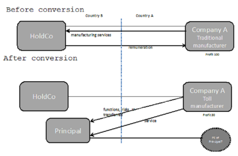
#### After conversion

As a result of the restructuring, Company *A* has been converted into a toll manufacturer. The functions (such as design, production planning and scheduling, sourcing and procurement, inventory management, warehousing and logistics, and quality control), risks (such as market risk, inventory risk, warranty risk and R&D risk) and IP have been transferred to the principal company (established in Country *B*). Company *A* was remunerated for the transferred IP. Company *A* still uses certain IP necessary for the manufacturing activities (know-how, patents, etc.).

For the (manufacturing) activities that it performs for the principal, Company *A* is remunerated on a cost-plus basis, with an arm's length cost-plus markup. As a consequence of the restructuring of its operations, its profit has dropped from 100 per unit produced in Year 1, to 30 per unit produced in Year 2.

As a consequence of the restructuring, all of company *A*'s distribution agreements with associated enterprises and independent parties were transferred to the principal.

The conversion can be illustrated as follows:




### Questions and answers

In our experience, the DTA do not differentiate between different types of business restructurings as regards the transfer pricing consequences thereof. The guidance included in section 9.7. as regards the conversion of a full-fledged distributor into a limited-risk distributor therefore also applies as regards the conversion of a full-fledged manufacturer into a toll manufacturer. However, unlike the limited-risk distributor, a toll manufacturer will generally be remunerated for its functions on the basis of the TNMM, with cost as NPI. Considering that toll manufacturers generally do not take title of the goods manufactured, the cost basis will generally consist of the conversion costs (i.e. the costs of the manufacturing process not including the costs of raw materials).

In our experience, the DTA increasingly focus on comparing the cost base of the tested party (i.e. Company A) with the cost incurred by the comparable companies included in the benchmark. If and to the extent differences exists (e.g. if it turns out that, unlike the tested party, the comparables do report raw material costs), the DTA may require the taxpayer to include comparability adjustments to the benchmarked data in order to reflect such differences (i.e. these adjustments generally result in an increase of the remuneration for the taxpayer compared to the remuneration of the comparables).

## 9.8. Centralization of intangible property rights

*See* section 9.1. for the transfer pricing aspects of intangible assets in the Netherlands.

## 9.9. Location savings

Dutch tax law does not contain specific guidance on location savings. However, on the basis of the 2013 Decree, in which the State Secretary takes the position that the OECD Guidelines have direct effect on Dutch tax law, Dutch taxpayers may apply the guidance on locations savings included in the OECD Guidelines.[77] In the OECD Guidelines, location savings are mentioned in the context of the transfer pricing aspects of business restructurings (chapter X, in paragraph 9.148 up to and including paragraph 9.153). Further guidance on the transfer pricing aspects of location savings (i.e. outside the scope of business restructurings) is provided in the OECD's Discussion Draft on BEPS Actions 8, 9 and 10, dated 19 December 2014 (the Discussion Draft).[78]

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77. E.g. Dutch taxpayers may use such guidance to claim a corresponding adjustment in the Netherlands further to a transfer pricing correction relating to location savings in another jurisdiction.
78. The Discussion Draft includes a proposed revision of chapter I of the OECD Guidelines, which includes the guidance on location savings. This guidance was initially included in the OECD's Revised Discussion Draft on the transfer pricing aspects of intangibles, dated 30 July 2014.

Under the above guidance, “location savings” may result from a relocation by a multinational enterprise of certain activities to a jurisdiction in which costs are lower compared to the initial jurisdiction.[79] Although location savings cannot be considered an intangible according to the OECD Guidelines, they may have an effect on determining the price for controlled transactions. However, in case local comparables are used, location savings will generally be reflected in the data and therefore no separate adjustments would be required. In the absence of reliable local comparables, the following considerations are relevant in determining the allocation of location savings between related entities:

(1) whether location savings exist;

(2) the amount of any location savings;

(3) the extent to which location savings are either retained by (a) member(s) of the multinational enterprise or are passed on to independent customers or suppliers; and

(4) where location savings are not fully passed on to independent customers or suppliers, the manner in which unrelated entities operating under comparable circumstances would allocate any retained net location savings.

As mentioned in section 3.4., the DTA generally allow benchmarking analyses to be based on pan-European database information. In our experience, within developed countries specific adjustments for features of the local market (i.e. location savings) are generally not required due to the availability of sufficiently reliable local comparables. However, such information may not be sufficiently available in most developing countries. In such situations, comparables from developed countries may be used and in such cases it may be necessary to examine whether location advantages are present and how these can be quantified. In practice, tax administrations in developing countries may take the view that a local related entity should be allocating (part of) the location savings under an adjustment (i.e. increase) of, for example, the local cost base on which the profit markup is applied. If such correction is suggested by the foreign authorities, Dutch taxpayers may claim a corresponding adjustment in the Netherlands on the basis of the guidance on location savings included in the OECD Guidelines.

## 9.10. Losses

Article 20 of the CITA provides that (i) losses can be carried forward for a maximum of 9 financial years and (ii) the carry back of losses is restricted to 1 financial year. Furthermore, various loss compensation restrictions apply, including restrictions relating to holding and/or financing companies, changes in the ultimate ownership of the taxpayer, mergers and tax consolidations.

As regards the transfer pricing aspects of losses, in our experience, the DTA actively focus on continuous loss incurring in Dutch group companies. In practice, the DTA may claim in such cases that the group company reporting the losses in fact incurs these losses for the benefit of the group elsewhere. Furthermore, they may claim that certain risks, which are contractually allocated to the Dutch group company, but which neither the multinational group or the loss incurring group company have any control over (e.g. risk relating to economic developments) should under arm’s length conditions be allocated to the most risk-diversified group company (i.e. often the foreign principal). Consequently, they may ignore losses relating to materialization of these uncontrollable risks for Dutch tax purposes.

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79. *See* M.A. de Lange & P.W.H. Lankhorst, *The Impact of Location Advantages on the Transfer Pricing of Multinationals: On the Chinese Love for European Designer Handbags and Lower Production Costs in India*, 21 Intl. Transfer Pricing J. 4, (2014). In the article, the authors applied the broader concept of “location advantages”, which not only accounts for cost savings, but also included revenue enhancing effects of relocating activities to another jurisdiction.

## 9.11. Market penetration

Dutch tax law does not contain specific guidance on the transfer pricing aspects of market penetration. However, because the State Secretary took the position in the 2013 Decree that the OECD Guidelines have direct effect on Dutch tax law, if beneficial, Dutch taxpayers may rely on the guidance on business strategies (in which market penetration is included) of the OECD Guidelines when taking a position in their tax return. *See* section 2.3. for the status of decrees issued by the State Secretary on transfer pricing.

## 9.12. Blocked payments

Dutch tax law does not contain specific guidance on the transfer pricing aspects of blocked payments. Reference can be made to the guidance on government policies (in which blocked payments are mentioned) of the OECD Guidelines.

## 9.13. Set-offs

According to the Supreme Court,[80] it is not mandatory to test the arm's length nature of every individual transaction or every group of transactions separately. Testing the arm's length nature of the complete set of conditions applicable to the total of transactions between a taxpayer and its shareholder(s) is allowed (*see* section 13.2.).

# 10. Tax Treatment of Intra-Company Dealings

## 10.1. General principles on attribution of profit to a permanent establishment

On 27 January 2011, the State Secretary published a decree on the allocation of profits to PEs (the PE Decree)[81] following the publication of the OECD Report on the Attribution of Profits to Permanent Establishments (the PE Report) and the amendments of the Commentary on Article 7 of the OECD Model in 2008 and the update of article 7 of the OECD Model and its Commentary in 2010. With the PE Decree the State Secretary intends to reduce the risk of disputes between taxpayers and the DTA on the attribution of profits between the head office and its PE.

According to the PE Decree, Dutch guidance intends to adhere to the arm's length principle for the determination of the allocation of profits to PEs. Profits need to be allocated to PEs based on a functional analysis (i.e. based on the functions performed, assets used and risks assumed). In performing this functional analysis, one needs to apply the so-called "functionally separate entity approach". Under this approach, the functional analysis needs to be performed under the assumption of the head office and PE are "legally distinct and separate enterprises", which are subject to general transfer pricing regulations.

The PE Decree refers to the PE Report which prescribes the so-called "Authorized OECD Approach" (the AOA). Under the AOA, the allocation of risks and assets to a PE should be based on the location of significant people functions (*see* section 10.2.).

According to the PE Decree, taxpayers are free to take positions that deviate from the Dutch preferences, provided that these positions are in line with those of the AOAs included in the PE Report and that the outcome of such approach is at arm's length.

The most important Dutch preferences are:

80. Supreme Court judgment dated 28 June 2002 (BNB 2002/343).
81. Decree dated 15 Jan. 2011 (IFZ 2010/457M).

- The Netherlands generally applies the “dynamic approach” to the interpretation of treaties and changes of the OECD Commentary. The PE Report is treated as a clarification of existing policies and therefore its outcome will be applied to all existing treaties.
- The Netherlands will in principle attribute profits in accordance with article 7 of the 2010 OECD Model, even if an existing tax treaty is not worded in accordance with article 7 of that Model, or in cases where no treaty is applicable.
- The PE Decree prefers one of the two AOAs for the attribution of a minimum equity to a PE, i.e. the “capital allocation approach”. Two examples on the application of this method are included in the Annex to the PE Decree.
- In principle, the Netherlands does not allow charging an internal interest between head office and PEs. The only exception is where there is a treasury function, in which case internal interest can be used to determine the arm’s length remuneration for this function.
- The Netherlands will in principle not attribute separate profits to a dependent agency PE of a principal when the agent receives an at arm’s length remuneration.

## 10.2. Allocation of assets and risks to a permanent establishment

As mentioned, under the AOA, to which the PE Decree adheres, the attribution of profit to a PE is determined on the basis of two steps.

In the first step of this approach, the allocation of assets and risks to the head office or the PE is based on a functional analysis. The functional analysis should be based on the presence of significant people functions (SPF). SPF depends on the people working in the PE having sufficient knowledge and authority to manage the assets attributed to the PE and the risk related to those assets. According to the PE Decree, SPF relates to day-to-day activities that are relevant for the business. The place where these activities take place determines the allocation of economical ownership of the assets and the risks incurred by the business. Subsequently, after the allocation of assets and risks, free capital and loans are allocated to the PE. Finally, interest is determined for the loans that have been attributed to the PE.

With regard to allocation of free capital, the PE Report provides for two approaches. Under the “capital allocation approach”, the allocation of free capital to the PE follows the actual capitalization of the general enterprise. Alternatively, under the “thin capitalization approach”, the allocation of free capital to the PE is based on the capitalization of independent companies comparable to the PE. In the PE Decree, the State Secretary expresses a strong preference for the capital allocation approach. This is mainly based on the assumption that the PE will have the same creditworthiness as the general enterprise. Finally, under the first step of the AOA, dealings between the PE and the head office need to be recognized as dealings influencing the profit allocation to the PE.

Subsequently, in the second step of this AOA, income and expenses are allocated to the PE on the basis of the functions, assets, risks, capital and the dealings analysed under step one. When attributing interest to the loans allocated to the PE (i.e. the difference between the assets of the PE and the free capital), the State Secretary expresses a strong preference for the “fungibility approach”. This approach leads to a pro rata allocation of the total interest costs of the general enterprise between the head office and the PE. Under the alternative “tracing approach”, reference is made to the interest on external loans obtained to finance a specific asset.

Although the State Secretary in the PE Report indicates a preference for the fungibility approach, current Supreme Court case law indicates that the tracing approach needs to be applied for the allocation of loans (and subsequently interest expenses) to a PE.[82] Consequently, Dutch taxpayers may chose the approach that is most beneficial for them.

## 10.3. Use of tangible assets

Because legal ownership does not allow assets of a general enterprise to be allocated between a PE and a head office, the PE Report adheres to the principle of economic ownership for this purpose. The PE Report therefore makes reference to SPF for the allocation of tangible assets. In the Commentary on Article 7 of the OECD Model, reference is made to the place of use of tangible assets unless special circumstances would require a different approach. In paragraph 5.1 of the PE Decree, the State Secretary considers the temporary disposal of tangible assets to a PE to constitute such special circumstance, which allows for an approach different from the place of use criterion included in the Commentary to the OECD Model. It is noted in this respect that differentiation between temporary and long-term disposal of assets follows from Supreme Court case law. For example, the Supreme Court ruled that long-term disposal of tangible assets leads to economic ownership for the PE. Temporary disposal on the other hand leads to economic ownership for the head office (i.e. the PE being considered a tenant).[83]

## 10.4. Intangible property

As regards intangible assets, the State Secretary takes the view in paragraph 4.2 of the PE Decree that for the allocation of such assets between the head office and the PE, the situation as regards comparable independent companies needs to be taken into account. According to the PE Decree, for acquired intangible assets or assets developed in-house, the allocation among the part of the general enterprise should be based on SPF (e.g. where active decisions are made relating to the management and control of risks on intangible assets).

## 10.5. Internal services

As regards internal services, in paragraph 4.1 of the PE Decree, the State Secretary takes the view that on the basis of the arm's length principle, the charge for these services should include a markup (i.e. in line with the PE Report). However, as regards situations covered by a tax treaty containing the previous version of article 7 of the OECD Model, the State Secretary allows for the allocation of costs for the services mentioned in the previous Commentary on Article 7 of the OECD Model on the basis of all actual costs (i.e. without a markup).

## 10.6. Cost contribution arrangements

The PE Decree does not provide for specific guidance for the allocation of profits to PEs in relation to CCAs. Reference is made to section 7. for guidance in relation to the transfer pricing aspects of CCAs.

## 10.7. Financing and interest payments

As mentioned, in determining the allocation of free capital to a PE, the State Secretary prefers the application of the capital allocation approach. Under this approach, the allocation of equity (and debt) to the PE will follow the allocation of assets and risks based on a functional analysis. This approach may

82. Supreme Court judgments of 23 Jan. 2004 (BNB 2004/214) and 25 Nov. 2005 (BNB 2007/117).
83. Supreme Court judgments 12 Feb. 1964 (BNB 1964/95) and 23 Jan. 1973 (BNB 1986/100).

lead to different results compared to the situation prior to the PE Decree, where interest expenses could only be allocated to a PE to the extent that these are related to external loans. However, if beneficial, a taxpayer may in its tax return still take the positions that the amount of interest expenses can be determined on the basis of the approach prior to the PE Decree.

The examples included in the PE Decree further indicate that debt (as well as interest) should be attributed on the basis of the value of the assets allocated between the head office and the PE, provided that the risks incurred assets used and functions performed by the PE are in line with those of the general enterprise. However, if the PE has a lower risk profile than the general enterprise, the example allows for less equity (i.e. free capital) and more debt to be allocated to the PE and consequently a larger part of the interest expenses.

### 10.8. Foreign permanent establishment of a resident taxpayer

Before 1 January 2012, income derived from a PE situated abroad or foreign real property was included in the taxable base (i.e. foreign losses could initially be used to offset Dutch taxable income although subject to recapture). An exemption from Dutch taxation could be obtained, which generally took the form of a proportional tax reduction. As of 1 January 2012, the method for avoidance of double taxation has changed for corporate taxpayers. Going forward, an exemption for foreign business profits (object exemption) was introduced.[84] Under this rule, the global profit of a Dutch taxpayer is reduced with the result (positive and negative) of a foreign PE. Consequently, losses of a foreign PE may no longer be off set against the Dutch tax base. For profits realized in treaty countries, the object exemption only applies to the extent that the Netherlands is required to grant an exemption to prevent double taxation under a treaty or other applicable arrangement. For non-treaty countries, a definition of “permanent establishment” has been included in the CITA. This definition is based on article 5 of the OECD Model.

As of 1 January 2012, a taxpayer outside the scope of a tax treaty is no longer required to be subject to a tax on its profits in the other country. However, the object exemption does not apply to low-taxed foreign investment income unless the Netherlands is required to grant an exemption from tax under the applicable tax treaty. Unlike normal losses, a loss arising on the termination of a PE may be deductible under certain circumstances.

### 10.9. Specific industries

No guidance exists in the Netherlands in relation to specific industry groups.

## 11. Specific Treatment of Transactions in Certain Sectors

### 11.1. E-commerce

There is no specific guidance and no case law on e-commerce activities.

### 11.2. Pharmaceutical sector

There is no specific guidance and no case law with respect to the pharmaceutical sector.

### 11.3. Global trading

There is no specific guidance and no case law with respect to global trading.

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84. *See* art. 15e of the CITA.

## 11.4. Insurance

In the 2013 Decree, the State Secretary states that although group companies may "formally" act as internal insurance and/or reinsurance companies, they often lack the ability to execute the necessary insurance functions and control the associated risks. According to the 2013 Decree, these companies are generally also not engaged in "active" risk diversification. In the 2013 Decree, based on his practical experience, the State Secretary identifies two types of captive insurance companies: (i) so-called "passive poolers" and (ii) companies that combine insurances with other products. The view of the State Secretary as regards these companies is further set out below.

An entity is considered a passive pooler, in the view of the State Secretary, if it only insures group-related risks. Such a company generally insures risks that are not insured by third parties and it does not diversify any risks. Such companies are considered to perform administrative/auxiliary insurance-related services activities that only justify a limited remuneration.

According to the State Secretary "insurance as a by-product" is encountered where insurance is provided to third-party clients if they purchase a product that is not insurance related (e.g. cancellation insurances or an insurance to obtain extended product guarantees). The insurance policy is generally issued in the name of a third-party insurance company that in turn reinsures this risk with a captive reinsurance company of the group. In the view of the State Secretary, such a captive reinsurance company does not in fact perform an insurance function. Consequently, as such company is deemed to only perform auxiliary/administrative services, the remuneration for the services of such a company should be modest.

Both examples clearly aim at avoiding "abusive situations" where foreign captive insurance companies have limited substance. In the paragraph above, the State Secretary explicitly refers to a judgment of The Hague Lower Court.[85] The (*Irish Captive*) case concerned an Irish captive insurance company of a Dutch group. The taxpayer in the case was a Dutch holding company of a group that operated bungalow parks and camping sites in the Netherlands. As part of its services (renting out of accommodation on its vacation parks), the taxpayer also allowed its customers to purchase cancellation insurance policies. Up to and including the year 2000, these "cancellation insurances"' were concluded with another Dutch company (BV; a subsidiary of the taxpayer). However, as of the year 2001, the insurance policies were concluded with an independent third party (Insurer). In turn, the latter concluded a reinsurance agreement with an Irish subsidiary of the taxpayer (Captive). BV still acted as an intermediary and for that purpose, it receives a commission of 3.5% of the insurance premiums, whereas Insurer received a commission of 1.5% of the insurance premiums. The remainder of the (re)insurance profit was reported by the Captive. The Lower Court ruled that, in fact, the Captive did not engage in reinsurance activities due to the fact that it did not have own personnel and that it only incurred limited expenses. As a result, the Lower Court ruled that the profit in relation to the (re)insurance activities should be allocated to the taxpayer. The Lower Court further ruled that the Captive should be remunerated on the basis of the cost-plus method and the proceeds of the investment portfolio, which was owned by the Captive, should not be allocated to the taxpayer.

85. The Hague Lower Court judgment dated 11 July 2011 (VN 2011/47). Further reference is made to the Zeeland-West Brabant Lower Court judgment dated 17 Jan. 2014 (AWB11/3717).

Although not referred to explicitly, the State Secretary arguably attempts with the above "passive poolers" to "correct" the Supreme Court ruling dated 21 October 2005.[86] This (*Antilles Captive*) case concerned a travel compensation fund that provides insurance to tourists against bankruptcy of travel agencies. The fund reinsured its obligations toward the insured persons with an Antilles captive insurance company. In its judgment, the Supreme Court accepted the verdict of the Court of Appeal that the risk relating to the insurance activities had indeed been transferred to the captive and the fact that the fund as parent company maintained a financial interest in the captive was not considered relevant.

### 11.5. Other

There is no specific guidance with respect to other sectors.

## 12. Safe Harbour

The Netherlands does not provide for safe harbours or *de minimis* rules in relation to transfer pricing. However, in practice, reference can be made to the EU Joint Transfer Pricing Forum's 2010 report on guidelines on low-value-adding intra-group services[87] and the OECD's BEPS Action 10 dealing with transfer pricing guidelines to low-value-adding intra-group services.[88]

## 13. Documentation Requirements

### 13.1. Introduction

Article 8b of the CITA requires taxpayers to maintain transfer pricing documentation. Further guidance on transfer pricing documentation is included in section 13.2.

### 13.2. Statutory requirements and regulations

Together with the explicit codification of the arm's length principle in Dutch tax law (in article 8b of the CITA as per 1 January 2002), the Dutch legislator introduced a documentation requirement relating to transfer pricing. The intention of the legislator was to alleviate the heavy burden of proof resting on the DTA when challenging a taxpayer's transfer prices. Going forward, the entities mentioned in the second and third paragraph of article 8b of the CITA (related entities) are required to include information in their administration:

- which shows the manner in which transfer prices were established; and
- from which it can be deduced these prices would have been agreed between independent entities.

With regard to the above documentation requirement, the Explanatory Memorandum[89] states the following:

> In chapter 1 of the OECD Guidelines, guidelines are provided for the application of the arm's length principle (paragraphs 1.15-1.70). In paragraph 1.15 it is indicated that the application of

86. Supreme Court judgment of 21 Oct. 2005 (BNB 2006/114). Further reference is made to the Supreme Court judgment of 21 Aug. 1985 (BNB 1985/301).
87. *See* http://ec.europa.eu/taxation_customs/resources/documents/taxation/company_tax/transfer_pricing/forum/jtpf/2010/jtpf_020_rev3_2009.pdf.
88. *See* http://www.oecd.org/ctp/transfer-pricing/discussion-draft-action-10-low-value-adding-intra-group-services.pdf.
89. *MvT*, *Kamerstukken* II 2001/02, 28 034, no. 3, pp. 7-8 and 19-23.

the arm's length principle is generally based on a comparison of the conditions of a related-party transaction with the conditions of a transaction between independent enterprises. The facts that could be of importance in relation to the comparability are mentioned in paragraphs 1.19-1.41. It includes the characteristics of the goods and services, the functional analysis, the contractual terms, the economic conditions and the business strategies. As shown in the OECD Guidelines, the importance of these facts is determined by the facts and circumstances of the specific case. On the basis of the relevant facts, the taxpayer should be able to support its decision for the applied transfer pricing method. It is explicitly not the intention that the taxpayer contemplates each method and subsequently substantiates why the chosen method leads to the best results under the specific circumstances (best method rule).

According to the wording of article 8b of the CITA, transfer pricing documentation requirements apply to "entities". Consequently, as a result of the use of the term "entities" (i.e. instead of taxpayer), transfer pricing documentation requirements also apply to each Dutch company included in a tax consolidation for Dutch tax purposes. This has been confirmed in the decree of the State Secretary dated of 3 June 2014,[90] in which it was indicated that within a tax consolidation article 8b of the CITA needs to be separately applied to each entity. Furthermore, one may question whether "dealings" between a PE and its head office are covered by article 8b of the CITA.[91] However, the legislator seems to have had this intention.

The State Secretary indicated that the information should include the factual information about the transaction and the relationship. According to the State Secretary, such information will generally be available within the group as such information is also necessary for the management of the group. He confirmed that article 8b(3) of the CITA does not require that the entity actually shows that transfer prices applied would have been agreed between independent entities. Consequently, it is not required to carry out a benchmark analysis to confirm the arm's length nature of the transaction.

In general, taxpayers in the Netherlands have a solid position in terms of defence against transfer pricing adjustments because (i) the DTA often have the burden of proof in relation to a proposed adjustment, (ii) both entities involved in the transaction need to be (or should have been) aware of the incorrect prices, (iii) the DTA are restricted to a marginal verification of the soundness of a business decision, (iv) market share strategies can be used to explain pricing and (v) set-offs are possible.

On 28 June 2002, the Supreme Court rendered a landmark decision concerning a taxpayer's defence to transfer pricing adjustments.[92] It concerned the arm's length nature of prices charged for goods supplied by a Japanese car manufacturer to its Dutch subsidiary (i.e. a car importer). The shares in the Dutch BV and the Japanese production company were both held by the same Japanese parent company. The goods sold to the Dutch subsidiary mainly involved four different products and their spare and replacement parts for which the Japanese parent company set the pricing. The four products had a similar element (which element was undisclosed in the published version of the Court's decision). Overall, the BV was profitable but the budgeted and actual results for one product (cars) were negative for a substantial period of time. The distribution of the spare and replacement parts of the cars was modestly profitable. In summary, the Supreme Court ruled that:

90. Decree dated 3 June 2014, no. DGB 2014/3102 (i.e. part of the FSC Decrees mentioned in sec. 17.3.1.).
91. *See* sec. 2.4.
92. Supreme Court judgment dated 28 June 2002 (BNB 2002/343).

- Even if transfer prices “were not negotiated on arm’s length terms” or “the profit deviates from what is customary”, the tax inspector has the burden of proof to show that the transactions were not arm’s length.
- It is not mandatory to test the arm’s length nature of every individual transaction or every group of transactions separately. Testing the arm’s length nature of the complete set of conditions applicable to the total of transactions between a taxpayer and its shareholder(s) is allowed.
- Treaty provisions regarding the arm’s length principle do not have direct effect. The arm’s length principle is effective in the Netherlands by virtue of article 3.8 of the ITA. For this reason an adjustment may only be made when the taxpayer has surrendered a benefit based on the shareholder relationship (so-called “awareness requirement”).

## 13.3. Documents required

In order to reduce the additional administrative burden as much as possible for taxpayers following the introduction of article 8b of the CITA, the Dutch legislator specifically intended to apply an open standard as regards the transfer pricing documentation requirements. It was indicated in the Explanatory Memorandum that the documentation should at least consist of:

- a description of the five comparability factors mentioned in the chapter I of the OECD Guidelines;
- a substantiation of the transfer pricing method applied; and
- a substantiation of the conditions to the transaction (including the price).

Under the 2013 Decree, taxpayers may request the DTA to provide certainty in advance as regards the compliance with transfer pricing documentation requirements.[93] In practice, the DTA accept transfer pricing documentation following international standards.

Furthermore, in our experience, discussions with the DTA on transfer pricing documentation generally focus on the question whether the intra-group transaction can be considered economically rational. Furthermore, the DTA have indicated their intention to subject data included in transfer pricing benchmarking analyses to random checks in order to assess their validity.

On 30 December 2015, chapter VIIa (additional transfer pricing documentation requirements) was included in the CITA (i.e. containing article 29b-h of the CITA). These new requirements are based on the guidance issued by the OECD on transfer pricing documentation (i.e. the Master File and Local File and country-by-county reporting (CbCR)).[94] On the same date, the State Secretary published a ministerial regulation[95] in which further instructions on these additional transfer pricing documentation requirements are provided. The new requirements enter into force on 1 January 2016 and apply to financial years starting on or after that date.

**Master File and Local File requirements**

On the basis of article 29g of the CITA, Dutch Master File and Local File requirements apply if:

- a Dutch taxpayer exists;

93. *See* para. 14 of the 2013 Decree.
94. In the scope of the OECD/G20 Base Erosion and Profit Shifting (BEPS) project, the OECD issued guidance in relation to transfer pricing documentation requirements and a newly introduced concept of Country-by-Country Reporting (i.e. BEPS Action 13).
95. Regulation of the State Secretary dated 30 Dec. 2015, no. DB/2015/462M.

- the Dutch taxpayer forms part of a group of entities (Multinational Group), including taxable permanent establishments, which:
  - are resident of different jurisdictions; and
  - includes an entity that is required to prepare consolidated financial statements, or would have had this requirement if shares of an entity of the Multinational Group were listed on a stock exchange; and
- the Multinational Group has a consolidated revenue (Consolidated Group Revenue[96]) of at least EUR 50 million in the year preceding the year for which the tax return is filed.

All Dutch taxpayers meeting the above conditions will be required to include the Master and Local File in their administration (i.e. the Master File and Local File will not need to be filed with the DTA).

The Master File and Local File need to be included in the administration of the taxpayer by the due date of the tax return (i.e. if a calendar year is applied, 1 June 2017 or, if an extension is requested, 1 May 2018). The Master File and Local File will need to form part of the administration of the Dutch taxpayer. Not including the documents in the administration may be punished with (i) imprisonment of up to 6 months or (ii) a fine of up to EUR 8,100.

The Master File needs to contain a high-level overview of the Multinational Group's global business structure and its transfer pricing policies. The Local File is meant to supplement the Master File and is intended to deliver a more detailed overview of the specific intra-group transactions that are entered into by the taxpayer. The objective of the Local File is to assure that the Multinational Group has complied with the arm's length principle in its material transfer pricing positions affecting a specific jurisdiction.

**Country-by-country reporting requirements**

On the basis of article 29c of the CITA, Dutch CbCR requirements apply if:

- a Dutch taxpayers exists;
- the Dutch taxpayer forms part of a Multinational Group (*see* Master File and Local File requirements above);
- the Multinational Group has a Consolidated Group Revenue of at least EUR 750 million in the year preceding the year for which Consolidated Financial Statements are prepared (the Reporting Year); and
- no foreign entity of the Multinational Group (an Ultimate Parent Company) exists that:
  (1) is required to prepare Consolidated Financial Statements on the basis of the ownership of shares in other entities of the Multinational Group, or would have had this requirement if its shares would be listed on a stock exchange in its jurisdiction of residence;
  (2) is the only entity of a Multinational Group that directly or indirectly owns shares qualifying under (1) above;
  (3) is resident of a jurisdiction that has introduced CbCR obligations;

96. According to parliementiary proceedings (i.e. *NV*, *Kamerstukken* II 2015/2016, 34 305, no. 6, pp. 20.) Consolidated Group Revenue includes revenues from sales of inventory and properties, services, royalties, interest, premiums and any other amounts, and excludes payments received from Multinational Group entities that are treated as dividends in the payer's tax jurisdiction.

(4) is resident of a jurisdiction that has concluded an agreement with the Netherlands as regards the automatic exchange of CbCR;

(5) is resident of a jurisdiction that has not suspended the automatic exchange of CbCR with the Netherlands or, for other reasons, systematically fails to exchange CbCR with the Netherlands (Systematic Failure); or

- no foreign entity of the Multinational Group (a Surrogate Parent Entity) exists that:
  - has been appointed by the Multinational Group to file the CbCR in its jurisdiction of residence;
  - is resident of a jurisdiction that has introduced CbCR obligations and that has filed a CbCR in that jurisdiction within a period of 12 months after the end of the Reporting Year;
  - is resident of a jurisdiction that has concluded an agreement with the Netherlands as regards the automatic exchange of CbCR;
  - is resident of a jurisdiction that is not in Systematic Failure; and
  - has notified its jurisdiction of residence and the Dutch tax inspector of its status as the entity of the Multinational Group that files the CbCR in the Netherlands.

The Dutch taxpayer meeting the above conditions (the Reporting Entity) will be required to (i) notify the DTA of its status as Reporting Entity ultimately before the end of the Reporting Year and (ii) file the CbCR with the DTA within a period of 12 months after the end of the Reporting Year. If more than one Dutch taxpayer meets the above conditions, the Multinational Group may appoint one of these Dutch taxpayers to file the CbCR with the DTA within the above term.

If a calendar year is applied as the Reporting Year, the first notification as Reporting Entity must ultimately be made on 31 December 2016 (i.e. and each subsequent year if the facts remain the same). As regards the filing of the CbCR, if a calendar year is applied as the Reporting Year, the first filing must ultimately be made on 31 December 2017 (and each subsequent year if the facts remain the same).

Not filing the CbCR within the above term can be punished with (i) imprisonment of up to 4 years or (ii) a fine of up to EUR 20,250. In addition, deliberately not complying with the CbCR obligations can be prosecuted as a criminal offence.

The country-by-country report will need to contain the following elements:

(1) For each country where the Multinational Group is active:
  - revenues (both within the Multinational Group and with third parties);
  - profit before income tax;
  - income tax paid;
  - income tax accrued;
  - stated capital;
  - accumulated earnings;
  - number of employees; and

- tangible assets other than cash and cash equivalents.

(2) For each Multinational Group entity:

- country where the entity is a tax resident;
- if deviating from the tax resident country, the country of residency on the basis of incorporation or organization; and
- main business activities.

## 13.4. Contemporaneous documentation

*See* section 13.5.

## 13.5. Timing issues

According to the Explanatory Memorandum the documentation should be established at the moment the transaction is entered into. If, however, a taxpayer is unable to provide the documentation when requested, the DTA are required to grant such taxpayer a reasonable period of time to establish proper documentation. Depending on the complexity of the transaction, such reasonable period may range between 4 weeks and 3 months.

## 13.6. Penalties

Penalties of 50% of the additional tax due may be imposed if the DTA can show that the taxpayer intentionally misrepresented the profit reported in the tax return. A rate of 25% applies where the taxpayer can be blamed for misrepresentation. However, it is noted in the Explanatory Memorandum to article 8b of the CITA that penalties would only apply in the case of intentional misrepresentation. In case of fraud, penalties may amount to as high as 100% of the additional tax due.

In case the taxpayer does not have the required documentation available, the burden of proof in relation to the correctness of the taxable profit reported may shift to the taxpayer (*see* section 13.7. for further guidance in this respect). In addition, the DTA could also initiate a criminal procedure against the taxpayer. The Explanatory Memorandum indicates that the criminal procedure will only be used as an ultimate solution.

In a recent case involving transfer pricing, the Zeeland-West-Brabant Lower Court maintained penalties imposed by the tax inspector (although for reduced but nevertheless considerable amounts) on the grounds that the taxpayer had intended, with the legal structure applied, to file incorrect tax returns, or that too little tax was levied.[97] In this case, a Dutch insurance company established a subsidiary (a captive) in Switzerland and subsequently allowed the captive to perform reinsurance activities. The tax inspector corrected the premiums paid to the captive. The court followed an expert witness in his statement that the premiums charged would not have been concluded between independent parties under the similar conditions and, on the basis of article 8b(1) of the CITA, only allowed for a deduction of the actual costs of the captive plus a return on the captive's (deemed) capital of 5%. The taxpayer appealed against the judgment of the Lower Court.

97. Zeeland-West-Brabant Lower Court judgment dated 17 Jan. 2014 (AWB 11/3717).

## 13.7. Burden of proof

As mentioned, the documentation requirement included in article 8b(3) of the CITA intends to ensure that the taxpayer's administration contains the relevant information in order to determine the transfer pricing between related entities. It does not in itself deal with the allocation among the taxpayer and the tax authorities of the burden of proof. It is noted in this respect that Dutch tax law does not contain strict rules as regards the allocation of the burden of proof. The burden of proof is generally allocated in accordance with the principles of reasonableness and fairness (i.e. the party claiming an adjustment should demonstrate that it is likely that the transfer price was not at arm's length). However, because transfer pricing documentation forms part of the general documentation requirements of article 52(1) of the General Tax Act (GTA), not meeting transfer pricing documentation requirements may have consequences as regards the allocation of the burden of proof.

If, however, the taxpayer does not comply with the obligations included in article 52(1) of the GTA (i.e. this provision requires taxpayers to maintain an administration which, inter alia, shows the taxpayer's rights and obligations as well as any other data considered relevant for tax purposes), the tax inspector is allowed to issue an irrevocable information decision. On the basis of such decision, the court is required to shift the burden of proof to the taxpayer (i.e. it will reject the appeal of a taxpayer unless the taxpayer is able to prove the contrary).

On the basis of the Explanatory Memorandumto the introduction of article 8b of the CITA, one may take the position that the burden of proof will only shift to the taxpayer if he is clearly in default as regards its transfer pricing documentation requirements and provided such default is substantial. In case of a shift in the burden of proof, a result of a failure to meet the documentation requirements of article 8b(3) of the CITA, the taxpayer does not need to "prove" that prices are at arm's length. He only needs to "make it plausible" (i.e. the latter being considered a lighter form of evidence). Furthermore, the State Secretary confirmed that taxpayers are specifically not required to carry out an examination or benchmarking analysis to determine the price that would have been payable for a similar transaction between independent parties. The State Secretary explicitly indicated that the absence of a transfer pricing benchmark will not result in a shift of the burden of proof to the taxpayer.

The allocation of the burden of proof was under discussion in a judgment of the Den Bosch Court of Appeal.[98] The case concerned a taxpayer, X, who concluded a contract with a company, H, which would render services to X in relation to direct mail and marketing. X paid a fee to H and allowed H to acquire 20% of the shares in X for an amount of EUR 1 as consideration for these services. The Court of Appeal did not follow the tax inspector in his view that the fees could not be considered business expenses. The Court of Appeal also did not accept the view of tax inspector that the taxpayer had not fulfilled its documentation requirements as laid down in article 8b(3) of the CITA. X made plausible that the payments were related to the business interests of the company and that there was no disparity between the expenses and the obtained services. Therefore, article 8b(3) of the CITA was not considered infringed. The judgment shows that a taxpayer is not required to include a transfer pricing benchmarking analysis in his administration in order to prevent the burden of proof from shifting in connection with article 8b(3) of the CITA.

98. Den Bosch Court of Appeal judgment dated 19 May 2011 (BA 2011/19.7).

According to the Explanatory Memorandum to article 8b of the CITA, the rule that an adjustment may only be made if the parties were aware[99] that a transaction was not undertaken under arm's length conditions should be interpreted objectively in the case of transfer pricing corrections. In this respect, the Explanatory Memorandum mentions that only if a price falls outside a range,[100] will it be presumed that this is due to the fact that the parties are related and were aware of non-arm's length conditions.

### 13.8. Position of small and medium-sized enterprises

The documentation requirements as laid down in article 8b(3) of the CITA apply to all taxpayers irrespective of their size.

### 13.9. Further exceptions

No exceptions apply.

### 13.10. Multilateral rules and guidance

As regards transfer pricing documentation requirements, the 2013 Decree makes specific reference to the EU Code of Conduct on Transfer Pricing Documentation for Associated Enterprises in the European Union.[101] According to the State Secretary, Dutch taxpayers may choose to comply with the documentation requirements on the basis of "EU Transfer Pricing Documentation".

### 13.11. Differences between domestic and multilateral requirements

No differences apply.

## 14. Compliance

### 14.1. Main features and jurisdiction of tax authorities

The tax inspector is the competent authority as regards the assessment of the taxpayer's corporate income tax returns filed. Taxpayers are governed by the inspector who is located in a tax office of the region in which the taxpayer resides (i.e. the "competent inspector"). As per 1 March 1998, the DTA established the Coordination Group Transfer Pricing (CGTP). The CGTP forms part of the DTA's Rotterdam office. Its main activities consist of:

- ensuring that the practical application of transfer pricing rules is coordinated;
- coordinating knowledge on transfer pricing in the Netherlands;
- providing local tax offices with support in transfer pricing matters;
- providing advice to the Ministry of Finance in relation to transfer pricing policy and implementation; and
- providing advice to the authorities in relation to MAPs.

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99. In respect to transfer pricing disputes for taxable years prior to 2002 and consistent with case law, a deemed dividend can only be taken into account in case double awareness is present (i.e. the company intends to benefit its shareholder and the shareholder reasonably should have been aware of that intention; *see* sec. 2.1.).

100. Considering that the Explanatory Memorandum does specify the type of range mentioned (i.e. it does not mention that this range should be interpreted as an 'interquartile range') one may take the position that any point within a range of prices (even outside the interquartile range) will not lead to a transfer pricing adjustment.

101. Resolution of the Council and of the representatives of the governments of the Member States, meeting within the Council, of 27 June 2006 on a code of conduct on transfer pricing documentation for associated enterprises in the European Union (EU TPD), (2006/C 176/01).

The DTA's APA/ATR Team, forming part of the Large Company Department, also resides in the Rotterdam office of the DTA. The APA/ATR Team has the authority to conclude APAs if a taxpayer prefers to obtain certainty in advance in respect of the arm's length character of transactions between related entities and ATRs in case of certainty in advance as regards the application of Dutch tax law. In case of certain types of financial group service companies (and similar types of companies),[102] the APA/ATR Team is responsible for the taxpayer's entire tax assessment process (i.e. levying, assessment and collection of tax) in addition to the issuing of APAs and/or ATRs to these companies. All other companies requesting APAs and/or ATRs remain under the authority of the competent inspector. However, as regards the issuance of APAs and/or ATRs, the competent inspector is required to seek binding advice from the APA/ATR Team.

## 14.2. Position of taxpayers

CIT is levied by way of an annual tax assessment. A company is obliged to file a CIT return for every financial year, irrespective of whether the company has realized a profit or a loss. The GTA provides that the tax inspector sets the deadline for the filing of the CIT return.[103] Currently, the CIT return should be filed within 5 months after the end of the financial year concerned (i.e. 31 May of the following year where a calendar year is applied for tax purposes). In practice, a filing extension may be obtained for 11 months if returns are prepared by tax advisers. If a CIT return is not filed within the relevant period (whether or not extended), the tax inspector will send a reminder to file the CIT return within 10 working days after the date of the reminder.[104] If the CIT return is not filed within this 10-day term, the inspector will issue an ex officio CIT assessment[105] based on his estimate of the taxable profit (which is likely to be on the high side) and a fine of in principle EUR 2,639 will be included. In exceptional cases, the amount of the fine can be up to a maximum of EUR 5,278 (e.g. in case a company is systematically in default).[106]

The DTA also issue preliminary CIT assessments, in principle payable over 11 instalments, of which the first one is (generally) issued on 31 January of the relevant year. Such preliminary assessment will be based on the information available to the tax authorities over the last 2 years, e.g. an estimation provided by the company (or its tax adviser). A final CIT assessment for a financial year will be issued after the CIT return has been examined by the tax inspector. A final assessment must in general be issued within a period of 3 years after the financial year concerned.[107] However, this 3-year period is extended by the period during which the company was granted a fling extension. The amounts paid on the preliminary CIT assessments will be offset against the amount due on the final CIT assessment. If an amount remains due, this amount will generally have to be paid within 6 weeks after the date on which the final assessment is issued. If the amount(s) paid on the preliminary assessment(s) exceed(s) the amount due on the final assessment, in case certain conditions are met, a refund will be granted together with interest.

As per the year 2012, tax interest is due as of 1 July of the year following the financial year concerned. The tax interest becomes due on the total outstanding amount of CIT that is due on the basis of the preliminary and the final CIT assessments for that year. The tax inspector will in general refund tax interest over the amount of CIT receivable in case an assessment is not issued within 8 weeks after a

102. *See* sec. 17.3.1.
103. Art. 9(1) of the GTA.
104. Art. 9(3) of the GTA.
105. Art. 11(2) of the GTA provides for the possibility to issue an ex officio adjustment.
106. Reference is made to art. 67a of the GTA for the amount of the fines.
107. Art. 11(3) of the GTA.

request for an assessment or within 13 weeks after a return has been filed. Pursuant to article 30hb of the GTA, the rate of the tax interest on CIT assessments is equal to the legal interest on commercial transactions, with a minimum of 8%.

After a final assessment has been issued, the tax inspector may under certain conditions issue an additional assessment (*navorderingsaanslag*).[108] In general, an additional assessment can only be issued within a period of 5 years[109] (to be prolonged with the above-mentioned extension period) after the end of the relevant financial year if new information, a so-called "new fact", has come to light of which the tax inspector was not aware (and could not reasonably have been aware) at the time that the original final assessment was issued. The 5-year period may be extended to 12 years if the company paid insufficient tax in respect of an asset held, or profit that arose, abroad. The tax inspector does not need to prove that a "new fact" has come to light, in the event the company has not acted in good faith and knows, or should have known, that the original final assessment was too low or that, erroneously, no assessment was issued at all.

The tax inspector may also issue an additional assessment if (i) the final assessment was issued incorrectly due to an error (or a final assessment was not issued due to an error) and (ii) the taxpayer was aware or reasonably should have been aware that the assessment was incorrect.[110] If the amount of tax due on the assessment is at least 30% lower than the amount due based on tax law, the taxpayer is deemed to be aware of the incorrectness. Furthermore, the tax inspector may issue an additional assessment in case a preliminary assessment has been wrongfully refunded or an incorrect amount.

In case of an additional assessment, the additional amount of CIT due will in principle be increased by tax interest and a penalty. No penalty is due if the fact that the amount of the original assessment was too low cannot be held against the company. The amount of the penalty depends on the amount of CIT due and the degree of guilt or negligence of the company and varies between zero and 100% of the additional assessment.[111] No interest will be charged on the penalty included in the additional assessment.

*See* section 15. for further guidance on the appeal procedure in the Netherlands.

## 14.3. Specific instructions for tax administration

The DTA does not provide information in respect of specific transfer pricing issues or current focus areas. However, one may assume that the topics included in the 2013 Decree can expect the full attention of the DTA. Most notably, the 2013 Decree focuses on business restructurings (specifically involving transfers of part of the business out of the Netherlands), (the transfer of) intangibles, intra-group services (specifically where such charges result in a decreased Dutch taxable basis), procurement activities, intra-group guarantees, captive insurance companies and Dutch participants in CCAs. In our experience, the DTA also focus on the transfer pricing of continuous loss incurring group companies.

Furthermore, the DTA established protocols for the benchmarking of intra-group back-to-back financing activities (*see* section 17.3.1. for the practical approach required by the DTA in the scope of an APA request) and other group activities. These protocols have not been published.

108. Art. 16 of the GTA.
109. Art. 16(3) of the GTA.
110. Art. 16(2) of the GTA.
111. Art. 67e of the GTA.

## 14.4. Audits and other review procedures

### 14.4.1. Authorities involved

In general, a tax audit is performed by a special tax inspector (i.e. a tax auditor). This tax auditor (in case of transfer pricing issues, usually a member of the CGTP) remains in close contact with the competent inspector over the course of the tax audit. The DTA are obliged to inform the taxpayer on the purpose of the tax audit. In most cases, the tax audit is intended to establish the tax position of the company itself. However, tax audits may also be performed to obtain information on other taxpayers (e.g. at the request of foreign tax administrations). Once a tax audit has been announced, or an announcement can reasonably be expected, adjustments to tax returns that have already been filed will be regarded as adjustments following the outcome of the audit. This may result in penalties that would not have been applicable if there had been no announcement of a tax audit.

At the introductory meeting, the DTA should inform the taxpayer on which article of the tax law the tax audit is based. This allows the taxpayer to determine whether the audit involves its own tax position or a third-party inspection. The DTA should also inform the taxpayer on years and taxes involved with the tax audit. It is advisable to make clear working agreements during the introductory meeting and formalizing these in writing. This provides the taxpayer with clarity and may also be of use in a later stage. If certain issues were the subject of a tax audit, the taxpayer can rely on the conclusions of the audit for tax treatment of these issues in later years.

In the Netherlands, audits are generally conducted after the filing of the tax return; however, this is not a requirement. The DTA are entitled in the context of an APA request to determine whether the description of the facts included in an APA is correct (a “forward audit”).[112] In practice, however, the DTA rarely use this possibility. Instead, APAs normally include a critical assumption stating that the description of the facts and circumstances is correct. During a regular audit (or a post-filing audit), the DTA verify whether the critical assumptions are still met.

The DTA normally start an audit for a number of years for which the tax returns have been filed. If the audit concerns potential transfer pricing adjustments, before discussing these adjustments, the tax authorities generally review the impact these adjustments would have in the years for which tax returns have not yet been filed.

At the end of the audit process, an audit report is drafted which contains the tax consequences of the audit in the view of the DTA. The taxpayer receives the general part of the audit report. It is advised to discuss the outcome of the audit before the final audit report is prepared. In practice, discussion generally takes place based on a draft audit report. At that time, all suggested profits adjustments are still negotiable. Generally, the draft serves as a tool to make the taxpayer aware of its maximum exposure, considering the outcome of the audit. To avoid undesired surprises, the taxpayer should try to regularly inform the tax inspector as regards the progress of the audit process. As such, it may be possible to anticipate difficulties at an early stage and possibly prevent or limit profit adjustments. If the discussion is only started after the final audit report has been completed (describing the conclusions of both parties in detail), the company may either accept the conclusions of the audit or alternatively file an objection to the assessments issued on the basis of the final report (if any).

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112. *See* para. 7 of the decree dated 3 June 2014, no. DGB 2014/3098 (i.e. the APA Decree).

Nowadays, the DTA pursue a high level of transparency with taxpayers (so-called "enhanced cooperation") and are prepared to commit themselves to high(er) speed of resolution on material issues (including transfer pricing). Enhanced cooperation requires taxpayers to establish a tax control framework. The documentation and determination of transfer prices need to be included in such tax control framework.

### 14.4.2. Primary current controversies

*See* section 14.3.

### 14.4.3. Audit timeline

In general, audit processes (specifically involving transfer pricing) can and often are very lengthy. In our experience, the DTA show a tendency to increase the scope of the audit beyond what was initially indicated. This may specifically concern (i) transfer pricing issue under review, (ii) entities involved and (iii) years concerned.

### 14.4.4. Rights and obligations of taxpayers

The obligations to the DTA are included in the GTA. It is noted in this respect that obligations to the tax inspector also apply to other officers of the tax administration. Articles 47 to 50 of the GTA deal with the obligation to provide information and to allow inspection. The obligation to provide information on request of the tax inspector applies to data and explanations of data that could be relevant for taxation. The taxpayer should allow inspection of all records, documents and other data relevant for taxation. This also includes electronic data storage, microfilms and sound recordings (e.g. of board meetings). These two obligations can even involve the records, documents and other data of foreign subsidiaries.

The obligations apply to:

- the taxpayer's own liability to taxation;
- the liability to wage tax on behalf of the taxpayer's employees; and
- the liability for taxation of third parties (e.g. suppliers and clients).

Article 47a of the GTA provides that the obligations to provide information also extend towards a foreign parent company of a Dutch taxpayer (and foreign subsidiaries of the parent company) provided that a share interest of more than 50% is held in the Dutch taxpayer.

The company has the legal obligation to "administer", which is much broader than bookkeeping as it is not limited to financial data but also involves other documents and data. The data should be maintained by the company for 7 years.[113]

Refusal of access or insufficient access to required data, which also involves providing incomplete information, can lead to a reversal of the burden of proof and can be considered a criminal offense committed by the company with punishments ranging from fines to imprisonment (i.e. criminal charges are generally only initiated in cases of serious fraud). Missing data also leads to a reversal of the burden of proof and can be considered a criminal offense, unless the taxpayer can make a plausible case that the absence is caused by circumstances beyond its control. The information has to be provided clearly, completely and without reservation. According to the case law, it is not allowed to show just a part of a

113. Art. 52(4) of the GTA.

document. Moreover, the inspector can demand that information is provided in writing. The information does not have to stem from the period that is being audited.

### 14.4.5. Rights and obligations of tax authorities

As mentioned in section 14.4.4., the rights of the DTA to request information extends towards all information that can be relevant for taxation. However, clergymen, notaries, attorneys, medical doctors and pharmacists may refuse to provide information on others (i.e. they are required to provide all information concerning their own liability to tax) on the basis of their right to non-disclosure (*verschoningsrecht*).

The position of the tax advisor and the public accountant is somewhat complex. In principle, they have to provide information and allow inspection of books and data with respect to the tax positions of their clients. However, a code of conduct has been agreed to by the DTA and confirmed by the Supreme Court,[114] stating that the tax inspector will not review files with correspondence covering solely tax advice and/or tax considerations. It is therefore advisable for taxpayers to store all external correspondence on tax advice and tax considerations separately from files covering tax compliance and facts. However, this separation in practice is hard to implement. In practice, the DTA do not often request advisory correspondence from taxpayers.

### 14.4.6. Information used in tax audits

In addition to the information referred to above, the DTA generally also use information from annual accounts, which most Dutch companies are required to file with the trade register of the Dutch Chamber of Commerce, as well as notarial deeds filed with the trade register (in general, all documents relating to the articles of association of legal entities may be requested from the trade register). The DTA furthermore use other publicly available information, such as information obtained from external databases and information shared on the Internet and information included in tax returns and tax audits relating to other taxpayers.

### 14.4.7. Confidentiality of information

Article 67 of the GTA requires the DTA to maintain confidentiality of all information with respect to Dutch taxpayers. This obligation, however, does not apply to the extent that international conventions or EU legislation obliges the Netherlands to provide such information. *See* section 16.2.

### 14.4.8. Right of access to information

As mentioned, the DTA have extensive rights to request and review taxpayer information. However, an important limitation to these the right relates to the fact that the tax inspector is not allowed to “nose about” (i.e. although he may request to review specific books, information or data, he is not allowed on his own to open files, books and closets). In other words, he may ask for information but he may not take the liberty to obtain that information by his own actions.

### 14.4.9. Penalties

*See* section 14.4.4.

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114. Supreme Court judgment dated 23 Sept. 2005 (BNB 2006/21), in which the Court ruled that on the basis of the fair play principle, a taxpayer does not need to share with the authorities third-party correspondence in which the taxpayer is informed and/or advised as regards his tax position.

### 14.4.10. Burden of proof

*See* section 13.7.

### 14.4.11. Statute of limitations

*See* section 14.2. for the tax assessment process. As mentioned above, Dutch companies are required to maintain data for 7 years.

### 14.4.12. Other review procedures

Not applicable.

## 14.5. Adjustments

### 14.5.1. Primary adjustment

In the Netherlands, taxpayers are not required to amend the commercial terms of a transaction when, following a transfer pricing adjustment, the taxpayer's taxable profit is increased or decreased (i.e. referred to as a "primary adjustment" in the OECD Guidelines). However, as included in the 2013 Decree,[115] in order to reconcile the equity for tax purposes with the profit correction, Dutch taxpayers are required to also apply a "secondary transaction" (i.e. a deemed dividend, a deemed capital contribution or a constructive loan).[116] In line with the OECD Guidelines, such secondary transaction may also have Dutch tax consequences (i.e. a secondary adjustment), e.g. an interest imputation on a constructed loan or Dutch dividend withholding tax on a deemed divided. However, the State Secretary indicated in the 2013 Decree that a secondary adjustment in the form of a deemed dividend can be refrained from if the taxpayer is able to demonstrate that dividend withholding tax paid cannot be credited in the other state (i.e. in the light of difference in tax systems used between two states) unless the avoidance of dividend withholding tax is intended.

### 14.5.2. Corresponding adjustment

On the basis of general principles of Dutch tax (i.e. article 3.8 of the ITA and article 10 of the CITA) profits derived from a business are required to be determined on the basis of the arm's length principle. Consequently, the possibility to apply corresponding adjustments follows from these general principles and such adjustment is not limited to an increase of the taxable profit. Dutch tax law may also require for such adjustment to reduce the taxable profit (*see* section 2.1.).

The above view is also included in the 2011 Tax Treaty Policy Note,[117] where the State Secretary indicates that in case of different views between two states on transfer pricing corrections following article 9 of the OECD Model, the taxpayer should be allowed access to MAP and possibly arbitrage.

### 14.5.3. Secondary adjustment

Dutch tax consequences, if any, of secondary adjustments are discussed below under the following five scenarios:

(1) a foreign parent company granting a benefit to a Dutch subsidiary;

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115. *See* para. 4 of the 2013 Decree.
116. Para. 4 of the 2013 Decree shows that the DTA also apply the distinction, included in paras. 4.66 to 4.76 of the OECD Guidelines, between a "secondary transaction" (i.e. the "accounting" correction) and a "secondary adjustment"' (i.e. the tax consequences of the secondary transaction).
117. *Notitie Fiscaal Verdragsbeleid*' dated 11 Feb. 2011.

(2) a Dutch subsidiary granting a benefit to its foreign parent company;

(3) a Dutch parent company granting a benefit to its foreign subsidiary;

(4) a foreign subsidiary granting a benefit to a Dutch parent company; and

(5) a Dutch company granting a benefit to an unrelated person.

**Indent (1)**

If a foreign parent company grants a non-arm's length benefit to a Dutch subsidiary company, acting in the course of a business, such benefit will need to be eliminated from the taxable profit of the Dutch subsidiary. Consequently, the CIT due of the Dutch subsidiary will be reduced with the non-arm's length benefit. Such amount will be considered as a deemed capital contribution by the parent company to the Dutch subsidiary.[118]

**Indent (2)**

If a Dutch subsidiary company grants a non-arm's length benefit to its foreign parent company, the benefit should be taken into account by the Dutch subsidiary company as a business profit.[119] The CIT due will consequently need to be increased. Such amount will be considered as a deemed dividend distribution to the parent company. In principle, such deemed dividend is subject to a 15% Dutch dividend withholding tax, which may need to be grossed up, unless a reduction applies under tax treaties or EU regulations. In addition, withholding tax on such deemed dividend may be refrained from provided the requirements stated in section 14.5.1. are met. Furthermore, penalties of 0%-100% of the dividend withholding tax due may apply.

Where a Dutch subsidiary company grants a non-arm's length benefit to its (foreign) sister company, the above equally applies followed by a deemed capital contribution of the (joint) parent company to the sister company. In case of a Dutch sister company, such deemed capital contribution will eliminate the benefit from the taxable profit of that company.

**Indent (i3)**

If a Dutch parent company grants a non-arm's length benefit to its foreign subsidiary company, such benefit will need to be take into account by the Dutch parent company as a profit from its business.[120] The CIT due will therefore increase. In addition, such benefit will need to be treated as a deemed capital contribution to the subsidiary company, which will increase the cost price of the shares in the subsidiary company for Dutch CIT purposes.

**Indent (4)**

If a foreign subsidiary company grants a non-arm's length benefit to its Dutch parent company, the benefit will need to be taken into account by the Dutch parent company as a deemed dividend from the subsidiary company.[121] Such a deemed dividend may qualify for the Dutch participation exemption, provided that the participation exemption applies in respect of that subsidiary company. If the participation exemption applies, the deemed dividend will be exempt from Dutch CIT.

118. *See* the Supreme Court judgment dated 31 May 1978 (BNB 1978/252).
119. *See* the Supreme Court judgment dated 27 Mar. 1968 (BNB 1968/112).
120. *See* the Supreme Court judgment dated 3 Apr. 1957 (BNB 1957/165).
121. *See* the Supreme Court judgment dated 23 Apr. 1958 (BNB 1958/179).

**Indent (5)**

If a Dutch company grants a non-arm's length benefit to an unrelated person, the DTA could take the position that the amount should be taken into account by the Dutch company as a business profit (i.e. the expenses are not deductible). In its judgment of 21 September 1994 (BNB 1995/15), the Supreme Court ruled that these expenses were not deductible, although it was not clear that the shareholder of the company (deliberately) benefited from these expenses. The Court did not indicate whether the expenses should be treated as a deemed dividend.

### 14.6. Use of secret comparables

Under paragraph 3.36 of the OECD Guidelines it is considered unfair to a taxpayer when tax authorities apply a transfer pricing method on the basis of secret information, including information obtained by a tax administration during its examinations of other taxpayers. The OECD Guidelines therefore recommend that tax authorities do not use secret comparables when making transfer pricing adjustments.

However, the OECD guidelines further state that tax authorities may apply a transfer pricing method on the basis of such data if "the tax administration was able, within the limits of its domestic confidentiality requirements, to disclose such data to the taxpayer so that there would be an adequate opportunity for the taxpayer to defend its own position and to safeguard effective judicial control by the courts."

As regards the use of secret comparables in the Netherlands, the DTA may claim on the basis of article 67 of the GTA that they are required to maintain the confidentiality of all information with respect to Dutch taxpayers and that, as a consequence, data on comparable transactions of other taxpayers cannot be shared with the taxpayer for which a transfer pricing correction was made. Furthermore, on the basis of article 8:29 of the General Administrative Tax Act, which deals with the appeal procedure at the Lower Court, either of the parties to the procedure may reject that information is shared with the other party in case sufficient reasons to do so exist. However, the Lower Court will only take into account such rejected information in its judgment if the other party agrees to its use. Therefore, in practice, a taxpayer will only allow for the use of secret comparables in court proceedings if it is in his own benefit.

In a letter to the parliament dated 21 December 2001,[122] the State Secretary indicated that as per the introduction of the Procedural Tax Law Reorganization Act (i.e. 29 October 1998), the DTA will refrain from the use of secret comparables when substantiating transfer pricing corrections, except in cases which involve a shift of the burden of proof.

## 15. Litigation

Disputes concerning transfer pricing corrections are often settled with the DTA before the audit is finalized (i.e. before the final audit report is issued). In determining the taxpayer's approach in a tax audit, it may, however, be beneficial to apply a strategy which is based on the option of brining the dispute to court (even if the taxpayer does not expect to pursue such course of action in the end).

In our experience, transfer pricing disputes are hardly ever brought to court because the outcome of such proceedings is highly uncertain (i.e. taxpayers generally tend to even avoid a remote risk that high corrections will be imposed). Furthermore, taxpayers generally prefer to settle transfer pricing disputes because this allows them to restrict the dispute to the transaction (or transactions) under review. If brought in from of a court, the judgment of such court may, apart from the transaction under review, also

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122. Letter of the State Secretary dated 21 Dec. 2001 (no. AFP 2001/933).

have adverse consequences for the transfer pricing system applied by the group to which the Dutch taxpayer forms a part.

If a taxpayer disagrees with an assessment in which a transfer pricing correction is included, he may proceed as follows (respectively):

(1) object against the assessment;

(2) appeal against the tax inspector's decision on the objection with the Lower Court;

(3) appeal against the decision of the Lower Court with the (regional) Court of Appeal; and finally

(4) appeal against the decision of the Court of Appeal with the Supreme Court.

## Indent (1)

An objection against the assessment must be signed and filed in writing with the responsible tax inspector within 6 weeks after the date of the assessment.[123] Together with the objection the taxpayer can file a request for deferral of payment of the amount of the assessment. No administrative fees are due. The taxpayer may represent himself or he may ask anyone else to represent him. A representative does not need to meet specific requirements (i.e. he does not need to an attorney).

The objection, which must be signed and filed in writing, has to meet the following formal requirements:

- the name and address of the person filing the objection;
- the date on which the objection is filed;
- a description of the decision to which objection is filed; and
- the reasons for the objection.

If any of these requirements is not met, the objection may be dismissed. Although a decision to dismiss can be appealed, if it was taken on the correct grounds, the substantive issue of the objection can no longer be reviewed by a court.

The objection against a tax assessment must be reviewed by a tax inspector other than the one who issued the assessment. Failure to do so will result in a reversal of the decision taken on the objection. A different tax inspector will then have to decide on the objection.

In principle, the DTA must decide on the objection filed within 6 weeks, although this period may be extended by an additional 6 weeks.[124] If the statutory term for rendering a decision is exceeded, the taxpayer can file an appeal on the basis that no decision has been rendered.

## Indent (2)

An appeal against the decision on the objection of the DTA may be made with a Lower Court (*rechtbank*) that resides over the region in which the company concerned was incorporated. Such appeal must be filed in writing. The term for filing the appeal is 6 weeks. The taxpayer is not required to have legal representation before the Lower Court.

123. Art. 6:7 General Act on Administrative Law (*Algemene wet bestuursrecht*', GAAL).
124. Art. 7:10 GAAL. The taxpayer and tax inspector can agree to further extend this period.

## Indent (3)

The decision of the Lower Court may be appealed against at the Court of Appeals (*Gerechtshof*). The term for filing the appeal is 6 weeks. An appeal against a decision of a Lower Court postpones the execution of the decision so appealed. There is also no requirement of legal representation before the Court of Appeals.

As the Court of Appeals (and the Lower Court) decide both on facts and issues of law, a taxpayer can bring up factual as well as judicial issues before these courts. Although both courts are limited in their examination to the issues of dispute brought by the parties, they are not bound to the legal interpretation of the parties. It does not expand the dispute beyond the borders set by the parties when it gives a legal qualification to the facts that differs from the legal qualification given by the parties. It has to apply the law and complement the legal bases of the dispute ex officio. In principle, a court is not allowed to judge on facts that are not disputed by the parties. However, if a court doubts the correctness of facts presented by the parties, it can raise questions about them or supplement the facts ex officio, but it is still not allowed to expand the dispute beyond the borders set by the parties.

If the appeal is founded, the judgment can either replace the decision against which the appeal was made or it can invalidate that decision with an order to the DTA to render a new decision taking into account the decision of the court and subject to other conditions (such as timing). The Court of Appeals can decide that the case must be reviewed again by a Lower Court.

## Indent (4)

The decision of the Court of Appeals can be appealed to the Supreme Court in The Hague. If both parties agree, a judgment of the Lower Court can be appealed to the Supreme Court (i.e. bypassing the Court of Appeals). The term for filing the appeal is 6 weeks. An appeal against a decision of the Court of Appeals postpones the execution of the decision so appealed.

In principle, there is no mandatory legal representation for cases brought before the Supreme Court. However, if a taxpayer wishes to explain his view as regards the case under examination, he may only do so under representation of an attorney (*advocaat*). The Supreme Court renders its decision solely on the basis of the facts established by the Court of Appeals (or the Lower Court); it does not establish facts itself. It decides the case on the basis of the grounds raised in the notice of appeal and reviews solely whether the Court of Appeals (or the Lower Court) has correctly applied the law and whether it has used arguments that can carry its decision. The Supreme Court, however, can supplement the grounds of the appeal. If the Court of Appeals (or the Lower Court) has based its decision on facts that have not been established or if the reasoning of such court is unclear, the Supreme Court will invalidate the decision of the court and will send the case back for further review.

A judgment of the Supreme Court is always in writing. The Supreme Court either decides the case itself or, if the decision is dependent on facts that have not yet been established, refers the case back to the Court of Appeals (or the Lower Court) for further review, taking into account the judgment of the Supreme Court. If the Supreme Court is of the opinion that the Court of Appeals (or the Lower Court) has rendered the correct decision on the correct grounds, the Supreme Court may decide that the grounds for the appeal are unfounded and that the lower court judgment needs no further elaboration. There is no term within which the Supreme Court must render a judgment. The decision is passed in public.

If a taxpayer succeeds in his legal action, even partly, the court will in general order the DTA to reimburse legal costs incurred by the taxpayer. For obtaining a reimbursement of legal costs, it is not necessary, but nevertheless advisable, to file a request as part of the appeal procedure. Generally, the legal costs of the taxpayer will not be reimbursed for the full amount, but will only be reimbursed for a fixed amount depending on the various procedural acts involved and the importance of the case. Under certain circumstances, e.g. when the tax authorities had no grounds at all for their assessment, a court can decide that a taxpayer should receive a reimbursement in excess of the fixed amount.

# 16. Tax Treaty Aspects

## 16.1. Standard provisions in conformity with article 9 of the OECD Model/UN Model

The Netherlands strives to include article 9 of the OECD Model in all bilateral treaties that it concludes. Furthermore, as regards corresponding adjustments, the Netherlands prefers to resolve resulting double taxation through mutual agreement or arbitration procedures (*see* section 17.1.1.).

## 16.2. Bilateral and multilateral exchange of information

As mentioned, article 67 of the GTA requires the DTA to maintain the confidentiality of all information with respect to Dutch taxpayers.[125] However, this obligation does not apply to the extent that international conventions or EU legislation obliges the Netherlands to provide such information. Such obligations can be found in:

- the EU directive on mutual assistance (2011/16/EU, the EU Directive), as implemented in the Act on international assistance in levying taxes (*Wet op de internationale bijstandsverlening bij de heffing van belasting*, the WIB);
- a bilateral tax treaty;
- tax information exchange agreements; and
- OECD/Council of Europe Convention on Mutual Administrative Assistance in Tax Matters.

Apart from implementing the EU Directive, the WIB regulates the procedure and restrictions that apply to the exchange of information on the basis of the above-mentioned sources. On the basis of the WIB, information may be provided upon request of a foreign authority, automatically or spontaneously.

The Fiscal Information and Investigation Service (de *Fiscale inlichtingen- en opsporingsdienst – Economische controledienst*', FIOD) will deal with a request and will formally have to decide thereon. Normally, the FIOD will send the questions to the tax inspector who deals with the tax issues of the "person concerned" (i.e. the Dutch resident person/legal entity that originally produced the information). If the tax inspector does not readily have available the requested information, the FIOD may instruct him to start a survey/investigation (article 8 of the WIB). It should be borne in mind that the tax inspector is formally not competent to decide himself upon the request of the foreign authority or to provide fiscal information regarding a Dutch resident taxpayer to foreign authorities (*see* article 67 of the GTA).

In case a survey/investigation on the basis of article 8 of the WIB is initiated, two stages must be distinguished:

125. Art. 67 of the GTA.

(1) the collection of information by the Dutch tax inspector under a survey on the basis of article 8 of the WIB; and

(2) the examination of the collected information by the FIOD in order to formally decide whether this information can be rightfully provided to the foreign authority.

**Indent (1)**

As stated above, if the Dutch authorities do not readily have available the information requested by a foreign authority, article 8 of the WIB provides that the Minister of Finance (i.e. the FIOD) may instruct the tax inspector to conduct a survey in order to collect the requested information.[126] This is a normal procedure. Article 8 of the WIB stipulates that such a survey is covered by section VIII(2) of the GTA. This means that the information rights/obligations under national tax law apply mutatis mutandis to such a survey. Under national information obligations, a Dutch taxpayer is required to provide to the tax authorities all information which could (hypothetically) be reasonably relevant for the levying of Dutch taxes on the taxpayer.[127] The information obligations therefore have a very broad scope. Under the WIB, these obligations are extended for the purposes of foreign taxation. Note that, in general, it is under Dutch tax law and published defendable policy that a Dutch taxpayer is not obliged to provide to the tax authorities:

- correspondence between the taxpayer and his attorney (in his function as an attorney); and
- advice received by the taxpayer from a tax advisor or accountant (*see* section 14.4.5.).

The parliamentary history of article 8 of the WIB is not clear as to the scope of the term "survey" in the context of collecting information. It is generally believed to include an investigation at the office of the taxpayer (to inspect the relevant files of the Dutch taxpayer)[128] and also requests for information made to the Dutch taxpayer. If a Dutch resident does not cooperate with a survey/investigation or under such a survey provides incomplete or false information, a criminal penalty (fine or imprisonment) can be imposed.[129]

**Indent (2)**

The information collected under a survey will in general be sent by the tax inspector to the FIOD. The FIOD will thereafter formally decide whether the collected information, taking into account the applicable material restrictions and formalities, will be provided to the foreign tax authority. There are five basic methods of assistance:

- exchange of information at the request of a foreign tax authority;
- spontaneous exchange of information by the Dutch tax authorities to a foreign tax authority;
- automatic exchange of information;
- presence of foreign officials during a tax audit; and
- a joint coordinated tax audit.

126. As of 1 Jan. 2002, it is also possible under the WIB to start a survey for the spontaneous exchange of information.
127. Note that Dutch corporate bodies (*administratieplichtigen*) are also obliged to provide information to the DTA that could be relevant for the levying of Dutch taxes from third parties.
128. Art. 10 of the WIB specifically states that the taxpayer is obliged to give access to his office for the survey within the meaning of art. 8 of the WIB.
129. *See* art. 11 of the WIB, which refers to sec. IX of the GTA (i.e. the Criminal Provisions in the GTA). Hence, the taxpayer could be prosecuted.

The relevant treaty or EC directive should be consulted to determine which of the above methods are permissible in a particular context.

Up to 1 January 2014, the FIOD was in principle required to notify the Dutch resident who is the source of the information of its decision to provide information to the foreign tax authority (a notification letter). The requested information was not provided within 10 days after the date of the notification letter. Following on this notification, the Dutch resident could file objections against the decision of the FIOD within 6 weeks after the date of the notification of the decision that information will be provided.

As of 1 January 2014, articles 5 and 7 of the WIB have been changed such that the FIOD is no longer obliged to notify the Dutch resident of its decision to provide information to a foreign tax authority. It is also no longer possible to file objections on the basis of this notification against the exchange of information.

The provision of information to a foreign authority can be denied by the Minister of Finance on the basis of one or more of the following reasons, which are based on the provisions of the WIB and/or relevant income tax treaty:

- the provision of the information is not based on the obligations of EU regulation 77/799/EEG or other obligations of international or interregional law;
- the exchange of information violates the public interest of the Netherlands;
- the information cannot be obtained in the Netherlands on legal grounds or on grounds of administrative practice;
- the other country's tax administration has not used the normally available means to obtain the information requested;
- the other country's tax administration is not able to provide similar information to the Netherlands in the reverse case;
- the other country's legislation does not contain an obligation to keep the information confidential;
- the information to be provided by the Netherlands originates from a third country and that third country has not authorized the Netherlands tax authorities to provide the information to the other country;
- the information contains a commercial, industrial or professional secret; or
- the information to be exchanged will be used for other than tax purposes (except in certain circumstances).

Besides the restrictions set forth above, in theory the exchange of information should also be in accordance with the "general principles of proper conduct", such as, for instance, the "(anti) abuse of power principle" or the "principle of proportionality".

As regards developments in the field of the exchange of information, the OECD (with its BEPS Actions 5, 12 and 13) and the European Commission (EC) have made a priority of improving corporate tax transparency, in order to re-establish the link between taxation and "real" economic activity, and to contribute to fair burden-sharing among taxpayers and fair competition between businesses. The OECD's Actions and the EU initiatives are discussed in the paragraphs below.

BEPS Action 5, published in September 2014, includes the compulsory spontaneous exchange on rulings related to preferential regimes. On 31 March 2015, the OECD released its discussion draft on BEPS Action 12: Mandatory Disclosure Rules. The draft contains recommendations regarding the design of mandatory disclosure rules for potentially aggressive or abusive tax planning arrangements, including international tax schemes. BEPS Action 13 proposes to amend the Guidance on Transfer Pricing Documentation and to introduce Country-by-Country Reporting (CbC). This Guidance will replace the current text of chapter V of the OECD Guidelines. It contains a three-tiered approach. First, a Master file is proposed, containing standardized information (blueprint relevant for all group members); secondly, a Local file is proposed, containing an overview of all material transactions per group company, including the reconciliation between the transfer pricing system and the actual results and, finally, a CbC report is proposed containing information regarding the allocation of income, taxes and business activities per jurisdiction.

On 18 March 2015, the EC presented the Tax Transparency Package (i.e. a package of measures which aims at boosting tax transparency). A key element is a proposal to introduce the automatic exchange of information between EU Member States on their tax rulings by amending EU Directive 2011/16/EU). The EU Directive lays down the rules and procedures under which Member States are required to cooperate with each other to exchange information that is foreseeably relevant to the domestic tax laws of the Member States.

A majority of the Member States, including the Netherlands, are of the view that the current proposal goes beyond what is necessary to achieve its goal of combatting aggressive tax planning and tax avoidance. They fear the extensive definition of rulings will give rise to high (implementation) costs without a corresponding benefit for other Member States. Certain Member States prefer a more limited model by exchanging information to the Member States for which this information is relevant (and not to all Member States as is currently proposed). In addition, some Member States already indicated that the deadline for exchanging existing rulings (ultimately on 31 December 2016) is much too short for them. Finally, the proposal for a central database (with information regarding the rulings) to which the EC gets access was generally not received well by the Member States.

In line with this trend of increased transparency, the European Parliament, in February 2015, approved the introduction of a special parliamentary committee (TAXE) to look into “tax rulings and other measures similar in nature or effect” of Member States and make recommendations for the future. The tasks of the TAXE will include (i) looking into tax ruling practices as far back as 1 January 1991, (ii) review the way the EC treats State aid in Member States, (iii) review the extent to which Member States are transparent about their tax rulings and (iv) seeking to ascertain the negative impact of aggressive tax planning on public finances.

# 17. Dispute Resolution

## 17.1. Mutual agreement procedure

### 17.1.1. Guidance

As indicated in the 2011 Tax Treaty Policy Note,[130] it is the intention of the Netherlands to include in all of its tax treaties a provision regarding the MAP identical to article 25 of the OECD Model. Although

130. *See* n. 118.

there are no domestic statutory provisions regulating MAPs, the DTA did publish a Decree[131] which deals with the practical application of MAPs under tax treaties and the EU Arbitrage Convention (the Convention)[132] (the MAP Decree).

### 17.1.2. Competent authority

MAP requests should be filed to the Dutch competent authorities; i.e. the Directorate of Fiscal Affairs with the Ministry of Finance. The competent authority will send copies of MAP applications to the TPCG of the DTA for its advice.

A request for a MAP does not have a set form. However, according to the MAP Decree, a written request should at least contain the following information:

- the name, address and identification number of the taxpayer as well as those of any related foreign taxpayer involved;
- information on the relevant facts and circumstances of the issues for which competent authority assistance is requested (including information on the relationship between the taxpayer and foreign related parties involved);
- the other country or countries included in the request;
- the tax treaty article(s), or article 4 of the EU Arbitrage Convention, that the taxpayer asserts is not being correctly applied, and the taxpayer's interpretation of the application of these articles;
- the legal basis for the request (i.e. a bilateral tax treaty or the EU Arbitrage Convention);
- the procedure applied (i.e. the regular procedure, the pre-emptive procedure or the extra pre-emptive procedure, *see* section 17.1.3.);
- the taxation years or periods involved;
- the foreign tax administrations involved;
- copies of the tax assessment notices, tax audit report or equivalent leading to the alleged double taxation;
- details of any appeals and litigation procedures initiated by the taxpayer or the other parties to the relevant transactions and any court decisions concerning the case;
- an undertaking that the taxpayer will respond as completely and quickly as possible to all reasonable and appropriate requests made by a competent authority and have documentation at the disposal of the competent authorities; and, in case of a pre-emptive procedure;
- a letter to the tax authorities, signed by the taxpayer, whereby extension for decision on appeal is requested for the period of mutual agreement and, if applicable, arbitrage.

131. Decree dated 29 Sept. 2008, IFZ2008/248M.
132. Convention on the elimination of double taxation in connection with the adjustment of profits of associated enterprises, dated 23 July 1990 (90/436/EEC). The Convention was in force from 1 Jan. 1995 until 31 Dec. 1999 for an initial period of 5 years and re-entered into force in Nov. 2004, with retroactive effect from 1 Jan. 2000. The Protocol that arranged for the re-entry into force of the Convention provides for an automatic extension of the Convention by periods of 5 years, unless a contracting state opposes (Protocol of 25 May 1999). With the enlargement of the European Union, the Convention was successively extended through different Conventions and Acts of Accession.

### 17.1.3. Conditions for requesting

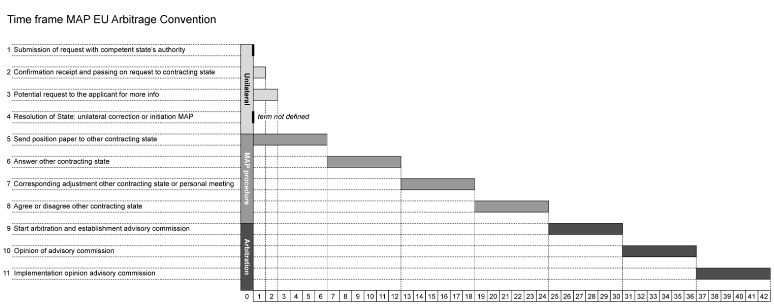
Article 25 of the OECD Model provides that the request must be presented within 3 years from the first notification of the action resulting in double taxation. In the MAP Decree, the State Secretary takes the position that a MAP request is considered to be filed in time if the request is received within 3 years of the date of the assessment in which the adjustment was incorporated or, if later, the date on which the adjustment was substantiated. According to the MAP Decree, a taxpayer may already request MAP to be initiated as soon as he may reasonably assume that he will be faced with taxation not in line with a tax treaty concluded by the Netherlands (i.e. such request may very well be made prior to date of the assessment).

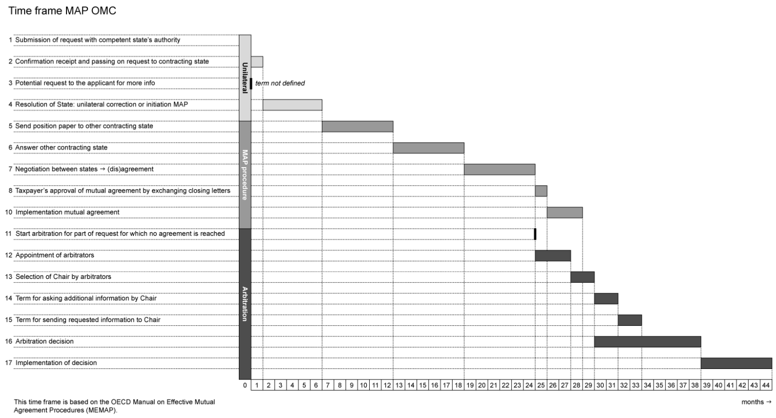
As regards the moment at which the DTA will initiate the procedure, the MAP Decree provides for three procedures: (i) the regular procedure; (ii) the pre-emptive procedure and, under exceptional circumstances (iii) the extra pre-emptive procedure.

The regular procedure is initiated if the tax assessment has become final (i.e. if and all possibilities for filing an objection and application for review have been exhausted or the time limits for doing so have expired). Consequently, a request will typically need to be filed before legal proceedings against the assessment have been exhausted. The pre-emptive procedure is initiated before a decision is taken on an objection and application for review. In these cases, double taxation can usually be avoided. A request must be submitted before the tax inspector takes a decision on any objection. A copy of the request must be sent to the tax inspector in order to ask not to take a decision on any objection. A decision should not be taken during the MAP or any subsequent arbitration procedure. In exceptional cases, the Netherlands is prepared to approach the other state at even earlier stages (the extra pre-emptive procedure).

### 17.1.4. Overview of process

The table below provides the steps and an indicative time frame for MAP under the Convention. The second table relates to the MAP process under bilateral tax treaties.






### 17.1.5. Interaction with domestic proceedings

*See* section 17.1.3.

### 17.1.6. Time limits

*See* section 17.1.4.

### 17.1.7. Penalties and interest

Dutch legislation[133] includes the possibility of including interest payments in any compromise reached in a MAP. When conducting MAPs, the Dutch authorities will try to ensure that the assessment and collection of interest charged by one state and paid by the other state match with each other. These attempts are sometimes successful.

If the Netherlands is the state making the adjustment, the DTA, upon request, will grant a deferral of payment on that part of the tax charge that is related to the adjustment. In principle, deferral will be granted until the date on which both the domestic and the international procedures for resolving the dispute have been completed.

### 17.1.8. Average processing time

*See* section 17.1.4.

### 17.1.9. Consequences of MAP with positive result for taxpayer

The MAP Decree indicates that taxpayers are informed in writing on the outcome of competent authority negotiations as soon as possible. If the competent authorities have reached agreement, the taxpayer may decide to either accept or decline, in its entirety, the outcome of the negotiations. He will need to inform in writing the competent authorities with whom he made the request for MAP on such decision. It should be noted that the outcome of a MAP under the Convention is binding for both the competent authorities and the taxpayer (i.e. contrary to MAP under bilateral treaties, a taxpayer cannot decline the outcome under the Convention).

On the basis of article 65 of the GTA, a taxpayer may request the Dutch tax inspector to make an "ex officio adjustment" (e.g. if an assessment was made for an incorrect amount and the taxpayer is no longer able to file an objection against the assessment). In principle, if a Dutch taxpayer obtained

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133. *See* art. 30k of the GTA and art. 31a of the Dutch Tax Collection Act.

success in a MAP, he has to request an ex officio adjustment if the MAP concerns financial years which are final (i.e. relating to assessments for which an objection can no longer be filed).

When a foreign state makes a transfer pricing adjustment, it often occurs that the official statute of limitations to request an adjustment of the Dutch tax assessment has lapsed. In such an event, a corresponding adjustment will, if necessary, be made in the form of a reduction ex officio in the tax assessment. According to a decree dated 16 December 2010,[134] such request has to be made within a period of 5 years after the end of the taxable year for which the request is made. However, on the basis of the MAP Decree, this 5-year term is extended in the scope of a MAP.

## 17.2. Arbitration

The position of the Dutch tax authorities as regards the application of the Convention is included in the MAP Decree.[135]

## 17.3. Advance pricing agreement

### 17.3.1. Government agency having jurisdiction

The request procedure for an APA is included in the Decree of the State Secretary dated 3 June 2014 (the APA Decree).[136] The APA Decree indicates that an APA request has to be addressed to the competent tax inspector and a copy of such request should be simultaneously sent to the APA/ATR Team of the Rotterdam office of the DTA. The APA Decree requires the competent inspector to submit the request to the APA/ATR Team for binding advice.

The ruling process of the DTA, which includes the APA process, is further based on the following decrees of the State Secretary:

- Decrees dated 3 June 2014 (the FSC Decrees) relating to companies performing intra-group financing, licensing and/or leasing activities (FSCs);[137]
- the 2013 Decree; and
- the Decree dated 7 January 2015 (i.e. the Decree on Fiscal Policy),[138] which indicates that certainty in advance will not be provided in cases where such certainty may violate the principle of good faith towards treaty partners or in cases that are predominately motivated by tax savings.

**FSC Decrees**

The FSC Decrees apply to Dutch companies (i.e. FSCs) the activities of which consist, legally or in fact, directly or indirectly, mainly[139] of receiving and (on-)paying interest, royalties, rent and/or lease amounts within a group[140] on the basis of interrelated transactions in whatever form or under whatever

134. Decree dated 16 Dec. 2010 (DGB2010/6799M).
135. Decree dated 29 Sept. 2008 (IFZ2008/ 248M).
136. Decree dated 3 June 2014, no. DGB 2014/3098. The Decree dated 3 June 2014, no. DGB 2014/3099, which deals with the request for certainty in advance as regards the Dutch tax consequences of a (set of) transactions in the form of an advance tax ruling, is not discussed in more detail.
137. Decrees dated 3 June 2014, nos. DGB 2014/3101 and DGB 2014/3102.
138. The Decree dated 7 Jan. 2015, no. BLKB2015/62M. This decree is not discussed in more detail.
139. In order for the company to qualify as an FSC, its activities should "mainly" consist of financial service activities. "Mainly" should be interpreted as "70% or more" and activities in relation to the holding of participations will not be taken into account. Furthermore, in the view of the DTA, a company borrowing from third parties under a parent guarantee and lending the proceeds to related entities will in principle be considered to have in fact borrowed from a related party. It will therefore be considered an FSC. If the company can demonstrate that it would have been able to borrow the same amount on a stand-alone basis and that the guarantee only serves to enhance the terms and conditions of the borrowing (e.g. the interest rate), then no such deemed related borrowing will be taken into account.
140. The FSC Decrees also refer to art. 10a(4) of the CITA for the definition of related entities.

name (financial service activities). The FSC Decrees ensure that advance certainty in the form of an APA as regards the tax treatment of financial service activities will not be provided if:

(1) the FSC does not comply with one or more of the conditions with respect to real substance in the Netherlands; or

(2) the functions performed by the FSC associated with financial service activities on balance involve no, or hardly any, real risk (the substance and real risk requirements will be set out further below).

Similar to the outcome of article 8c of the CITA (*see* section 8.1.2.1.), foreign withholding tax on interest and royalties received by an FSC will not be creditable against Dutch CIT if the company does not incur sufficient risk. The rationale for such denial is that an FSC that does not incur sufficient risk in fact functions as an intermediary and, as a consequence thereof, its transactions are not included in its Dutch tax base. The FSC Decrees further indicate that the Netherlands intends to spontaneously exchange information with the relevant foreign tax authorities on any APA requested after 13 June 2014 involving FSCs, where the related corporate group does not have any other activities in the Netherlands or does not have genuine plans to engage in such activities. Requests for certainty in advance will also be denied where such would be in conflict with good faith towards treaty partners.

**Substance requirements**

The substance requirements must be complied with on a cumulative basis (i.e. no *de minimis* exception applies as regards any of these requirements):

(a) At least 50% of the total number of statutory directors – corporate or individual – with decision-making authority are resident in the Netherlands.

(b) The directors of the company that are resident in the Netherlands have sufficient expertise to carry out their functions. The tax authorities have stated that the directors should be able to manage the transactions performed by the FSC and the risks that are being incurred. The functions of the local board of directors include at least decision-making (on the basis of their own responsibility for the company and within the framework of normal group control) with respect to transactions to be entered into by the company and also arranging for the further handling of transactions.

(c) The company must have qualified personnel (by itself or through a third party) for the adequate execution and registration of the transactions entered into by the company.

(d) The management decisions are taken in the Netherlands. This requirement entails a material test, meaning that the board meetings must be held regularly in the Netherlands with physical presence of directors. All important decisions must be made during such meetings.

(e) The main bank account of the company is in the Netherlands. This is interpreted to mean that at least 50% of the company's directors are Dutch residents who have decision-making powers in respect of the bank accounts. It is not required that the account is kept with a Dutch bank.

(f) The bookkeeping of the company is performed in the Netherlands. This entails that the bookkeeping must be physically present in the Netherlands and the transactions must be accounted entirely in the Netherlands. It is not required for the company to have the bookkeeping conducted in the Netherlands if the corporate group of the company has centralized its bookkeeping activities outside of the Netherlands and this group has sufficient operational activities in the Netherlands.

(g) The company has met all of its tax filing obligations. These can be corporate tax, wage tax, value added tax, etc.

(h) The business address of the company is in the Netherlands.

(i) The company is – to the best of its knowledge – not (also) considered a resident for tax purposes in another country than the Netherlands.

(j) The company has equity which is adequate in relation to the functions performed by it (taking into account the risks incurred).

**Real risk requirements**

As mentioned, an FSC will only be able to obtain certainty in advance as regards the tax treatment of its activities if it incurs a certain level of risk. The risks related to financial service activities consist in particular of credit risks (debtor and currency risks), market risks and operational risks. Incurring operational risks only will generally not result in the existence of real risk as provided for in the FSC Decrees. Risks subcontracted to third parties (i.e. to third parties) will be considered risks incurred by the FSC. According to the FSC Decrees, whether or not the FSC incurs any of the aforementioned risks and whether it has sufficient equity to bear the consequences of these risks materializing are relevant factors in determining whether or not an FSC incurs real risks.

Where its activities consist of granting loans, the FSC Decrees provide, as a safe harbour, that the FSC will be considered to incur real risks if the risks require to maintain an amount of equity equal to at least the lower of (i) 1% of the loan or loans extended and (ii) EUR 2 million. A further requirement consists of the existence of a realistic possibility that the equity of the company will be called upon if risks to which it is exposed materialize. With regard to companies receiving and on paying royalties, rents or lease amounts, the determination of the minimum equity at risk relating to those activities should be based on specific circumstances. However, the FSC Decrees provide for a rule of thumb as regards minimum equity for such activities. The minimum equity to be maintained to cover the risk should be equal at least to 50% of the yearly royalties, rent or lease amounts received by the company. At least half of the risks incurred should be related to market risks.

In the FSC Decrees, the DTA have issued further guidance on determination of an arm's length remuneration for an FSC performing intra-group back-to-back financing activities (i.e. in- and on lending of funds). Such remuneration is determined on the basis of two components:

- premium for equity "at risk" (risk premium); and
- compensation for the activities in respect of the funds borrowed and the funds on lent (handling fee).

Under this conceptual approach, both results need to be aggregated and accounted for in an interest margin (i.e. the difference between the interest rate on loans payable and loans receivable. This remuneration also needs to cover (other) expenses incurred by the Dutch entity.

On the basis of the FSC Decrees, the risk premium component can be calculated by multiplying the difference between (i) the interest on subordinated loans (RA) and (ii) the interest on comparable secured loans (RS) with the equity at risk (EV) and dividing the result by the amount of loans outstanding

(LUG). In order to express the subordinated character of the equity capital in relation to the remainder of the loan, the following formula can be used.

| |
|---|
| *Risk premium* = ((RA-RS) x (EV))/LUG) |

The determination of the RS and RA components is set out in more detail below.

**RA**

On the basis of the method applied by the DTA, the RA is computed by the applicable interest rate on the loans receivable increased with a margin for subordination. In practice, this margin for subordination is often computed as the difference between (i) the interest rate on subordinated loans and (ii) the interest rate on secured loans. The guidance issued by the DTA states that the RS can be calculated by benchmarking comparable secured loans. However, on the basis of the method of the DTA, the RS component should be compared to the interest rate on a risk-free loan. Pursuant to the FSC Decrees, the applicable range has to preferably be composed of well-chosen comparable transactions. If less accurate reference material is available, the FSC Decrees state that the reliability of the reference material can be increased by calculating an inter-quartile range.

**RS**

For the RS component, the DTA prescribe that this element should be benchmarked against a risk-free loan. The website of the Dutch Central Bank (*De Nederlandsche Bank*; www.dnb.nl) can be used to search for comparable loans.

The handling fee component is comparable with a remuneration which is charged by banks and other financial institutions when raising funds from the capital markets for corporate clients. The activities in respect of such a transaction will generally not all be conducted by the Dutch entity. Consequently, this requires an allocation of the remuneration between the Dutch entity and the treasury department, taking into account objective criteria. An allocation of 50% will generally be considered acceptable, but a taxpayer may still demonstrate that a different allocation is at arm's length. The resulting number of basis points on the outstanding loans forms the handling fee component.

On the basis of the above conceptual approach, the interest on the loans receivable consists of the interest on the loans payable increased with the EER and the FR.

No specific guidance is provided with regard to arm's length remunerations of FSCs receiving and on paying royalties, rent and/or lease amounts. However, a number of practical benchmark methods are available, such as methods using the Capital Asset Pricing Model, methods using the Loanconnector database or methods using royalty databases. The most appropriate model should be determined on a case-by-case basis.

**Summary of the decision from the European Commission concerning the Starbucks tax ruling**[141]

**Introduction**

In the decision dated 21 October 2015 (the decision), the European Commission determined that the APA entered into between the DTA and Starbucks Manufacturing EMEA B.V. (SMBV) on 28 April 2008,

**141. The below is a summary of the decision of the European Commission on the Starbucks ruling. The summary is published on the website of the Dutch government (https://www.government.nl/documents/decrees/2015/11/30/summary-of-the-decision-from-the-european-commission-concerning-the-starbucks-tax-ruling).**

relating to the period 1 October 2007 to 31 October 2017, includes prohibited State aid (State aid number SA.38374).

An APA is an agreement between tax authorities and a taxpayer concerning the application of the tax legislation in relation to (future) transactions. Set out in such an agreement are the criteria suitable for determining the corporate transfer prices for intra-group transactions during a specific period. Calculations are made based on that to determine how much profit from a taxpayer's activities will be taken into consideration in that fiscal jurisdiction and how much corporation tax is payable annually thereby. An APA is initiated through an application from a taxpayer.

**Assessment by the European Commission of the APA with SMBV**

**Conditions for the existence of State aid**

According to article 107(1) of the Treaty on the Functioning of the European Union (TFEU), State aid measures are (i) from a Member State or funded by state means in whatever manner, which (ii) could have an unfavourable influence on the trade between Member States (iii) by giving advantages to certain companies or certain productions and (iv) thus distort the competition or threaten to do so, which is incompatible with the internal market.

The first condition is fulfilled. The APA was entered into by the tax authorities, which are part of the Dutch government. The APA can therefore be attributed to the Netherlands. In addition, the APA leads to a loss of tax income, which the Netherlands would otherwise have at its disposal. This means that the APA is considered to lead to a loss of state means.

The second condition is also fulfilled. SMBV is part of the Starbucks Group, which is active worldwide and in all EU Member States, which means that aid could affect trade within the Union.

Furthermore, the third condition is fulfilled. The APA allows Starbucks a selective advantage, in so far as that measure leads to a reduction in the tax payable by SMBV in the Netherlands. The greater part of the decision is dedicated to this condition in the Commission's assessment.

Finally, the fourth condition is also fulfilled. Since the APA discharges SMBV from payable taxes, which it would otherwise have been required to pay, this measure strengthens the financial position of Starbucks in respect of other competing companies, whereby the competition is distorted or threatens to be distorted.

Since all the conditions are fulfilled, the APA amounts to State aid within the meaning of article 107(1) of the TFEU.

**Existence of a selective advantage**

**Fiscal State aid test**

In order to determine whether a specific tax measure contains a selective advantage, a fiscal State aid test has been developed in European case law, comprising three steps. The first step entails determining which general or normal tax regulations are applicable in the Member State: "the reference system". The second step entails determining whether the tax measure involved forms a deviation from that reference system. If the measure does form a deviation from the reference system, then it is determined during the third step of the analysis whether that measure is justified by the nature and general scheme of the reference system.

**Reference system**

The reference system is formed by the general Dutch system of corporation tax, which is targeted at the tax on profits of all tax-paying companies in the Netherlands, irrespective of whether that concerns a group of companies or an independent company. That the taxable profits for integrated and non-integrated companies are calculated in a different manner out of necessity is not important for determining the reference system.

Contrary to the argument put forward by the Netherlands, the reference system is not formed through section 8b of the Corporation Tax Act and the Transfer Pricing Decree, which contain specific rules for group companies. By assuming, in the manner used by the Netherlands, that the reference system only concerns group companies, then an artificial distinction is made between companies on the basis of their company structure. That is all the more true, since the Transfer Pricing Decree is intended to ensure that group companies and independent companies are handled in a similar manner on grounds of the Dutch system of corporation tax. If the Transfer Pricing Decree, however, is intended to establish special rules for integrated companies, which deviate from the general Dutch rules concerning corporation tax, then its implementation is selective in itself, which means that all advantages given on grounds of those regulations are selective.

**Arm's length principle**

Since it has now been established that the general Dutch system of corporation tax is the reference system against which the APA should be tested, then it must be ascertained whether that APA forms a deviation from that system, whereby companies that are in a comparable situation, actually and legally, are handled unequally. This is on the basis of the arm's length principle. The system applied by the Commission in the State aid assessment does not follow from the non-binding OECD Model relating to taxes, but concerns a general principle under European law of equal fiscal treatment.

The methodological choices in the transfer pricing report provided by the tax adviser for Starbucks, which were accepted by the tax authorities in the APA, do not lead to a reliable approach to a market result and thereby do not fulfil the arm's length principle. More specifically, this concerns:

- the choice to apply the transactional net margin method (TNMM) in order to forecast a taxable profit, while the OECD Guidelines and the Transfer Pricing Decree show a preference for the comparable uncontrolled price method (CUP);
- if the CUP was applied, then the taxable profit of SMBV would be substantially higher, because:
  - the royalties paid by SMBV to Alki LP for know-how in the area of coffee roasting are too high;
  - the purchase price paid by SMBV for green beans to a company established in Switzerland and belonging to the Starbucks Group, Starbucks Coffee Trading Company SARL (SCTC), is too high.

Alternatively, the Commission is of the opinion that the TNMM is applied incorrectly:

- it was incorrectly assumed that SMBV (in comparison with a company established in the United Kingdom and belonging to the Starbucks Group: Alki LP) should be designated as "least complex function" and therefore applies for the application of the TNMM as the "tested party"; and

- in connection with the comparability of SMBV with other market participants in the coffee trade sector, two corrections in the cost base were wrongly carried out.

These choices resulted in SMBV's taxable basis being too limited, whereby SMBV enjoys a tax advantage in the Netherlands.

**Royalties**

The payment of royalties by SMBV to Alki LP does not provide a correct representation of the value of the intellectual property rights and therefore cannot be deemed to be arm's length.

The royalties comprise an adjustment variable, the level of which is determined by the accounting profits of SMBV combined with the compensation agreed in the APA in the form of a fixed markup on the operational costs of SMBV. This means that the APA contains no method of being able to assess the arm's length nature of the level of the royalties. In addition, on the basis of a CUP test, the actual price that SMBV would have been willing to pay for the royalties – in an arm' s length transaction – would have amounted to nil. This can be deduced from a few comparable agreements for roasting coffee, which Starbucks had entered into with other coffee roasters worldwide. Alki LP should not have been paid any royalties. Those royalties, which were paid for years, therefore cannot be arm's length, even more so because SMBV does not appear to gain any business advantage itself from the use of the intellectual property in the area of roasting coffee. An independent company would not have been prepared to pay for licences if it was unable to earn back the royalties paid.

In addition, the payment for royalties does not represent a payment for taking over the company risks. The argument from the tax authorities that Alki LP (and not SMBV) carried the economic risk of loss of stock is not accepted by the Commission.

By accepting this reasoning, the application of the arm's length principle for the pricing policy for intra-group transactions would be pointless since the economic reality could in fact be reasoned away or contracted out of as an alternative. Moreover, Alki LP's capacity is too limited for actually being able to carry such risks. This can be illustrated by the fact that the latter company has no employees itself. The level of the royalty payments also cannot be justified by the amounts Alki LP pays to Starbucks US for technology.

**Purchase of green beans**

The purchase price of green beans paid by SMBV to SCTC is abnormally high and therefore does not comply with the arm's length principle.

In the first place, there was a failure to investigate the extent to which the transactions between SCTC and SMBV – the purchase and delivery of green coffee beans – actually take place arm's length. Starbucks has also not provided any grounds for justification of the significant increase as from 2011 of the markup in the costs for the coffee beans supplied by SCTC. The tax authorities should also not have accepted this deduction from the accounting profits. That SCTC's activities became increasingly important, partly due to the evolving "C.A.F.E. Practices" programme, does not form grounds for justification. Taking similar fair-trade programmes into account (and the costs of those), the figures provided by Starbucks in connection with that are problematic both in terms of consistency as well as the arm's length nature. Moreover, the losses incurred through SMBV's coffee roasting activities since 2010 can be connected directly to the increased markup. This also highlights the non-arm's length of this markup. SMBV's profits are reduced artificially by purchasing green coffee beans at a non-arm's length price, due to its high level.

#### Least complex function

SMBV was wrongly designated as the "least complex function" for the application of the TNMM.

Determining the least complex function takes place prior to the application of the TNMM as transfer price method. In order to determine the entity with the least complex function, a function comparison must be made. The outcome of the function comparison indicates an entity to which the transfer price method can be applied in the most reliable manner and for which the most reliable comparison points can be found.

In its coffee roasting function, SMBV does not only carry out routine activities. SMBV conducts market research (outgoings were paid for market research) and it holds significant intellectual property (there is amortization of intangible assets). Moreover, SMBV performs an important resale function. A routine producer is not involved in such activities.

Alki LP's activities are very limited in comparison with that. Besides the fact that Alki LP has no employees as well as a limited operational capacity, the financial capacity of Alki LP cannot be equated with the total financial capacity of the worldwide Starbucks Group.

#### Alternative standpoint of the Commission

Even if section 8 of the Corporation Tax Act and the Transfer Pricing Decree are used as the reference system, a selective advantage is given by means of the APA agreed with SMBV. Also, in that case, the APA cannot be deemed to provide a reliable approach to a market result in accordance with the arm's length principle and the payable tax is reduced in comparison with other group companies that are required to pay tax in the Netherlands.

#### Conclusion

The APA amounts to State aid within the meaning of article 107(1) of the TFEU and is incompatible with the internal market. Since the Netherlands has not notified to the Commission any intention to grant the contested aid measure, there is a case of illegal aid being provided to SMBV and the Starbucks Group, which is carried out contrary to article 108(3) of the TFEU.

This illegal aid, including interest from the date on which it became available until the date of repayment in full, must be claimed back immediately and effectively from SMBV (or otherwise from the Starbucks Group). The decision must be implemented by the Netherlands within 4 months of the date of notification.

### 17.3.2. Unilateral, bilateral, multilateral

According to the State Secretary,[142] an APA provides certainty in advance on the determination of an arm's length remuneration or the method applied to determine such remuneration for (i) cross-border transactions between related entities and (ii) the profit allocation to a PE of such entities.

In principle, a taxpayer is not limited in his choice for a certain type of APA (multilateral, bilateral or unilateral), the DTA expressed their preference in the APA Decree for bilateral APAs based on article 25 of the OECD Model. Obviously, the latter is only applicable in cases where a cross-border transaction

142. Reference is made to the introduction of the APA Decree.

is in relation to a country with which the Netherlands has concluded a tax treaty that provides for mutual agreement. In addition, in order for a bilateral APA to be approved, the authorities of the other country will have to be willing to cooperate.

In case of a request for a bilateral APA, the DTA's APA/ATR Team will forward such request to the Directorate of Fiscal Affairs with the Dutch Ministry of Finance. The Directorate, as Dutch competent authorities, will inform the competent authorities of the other contracting state on the request in order to initiate the bilateral procedure.

Where less complex transactions are involved (i.e. limited functions performed, limited risks incurred or availability of sufficient uncontrolled comparables), unilateral APAs may be preferable. In practice, the majority of APAs concluded by the DTA are unilateral APAs.

The DTA are also willing to initiate a request for a multilateral APA where a taxpayer intends to obtain certainty in advance in more than two states. If, however, it turns out that a request for a multilateral APA invokes unsurmountable concerns with treaty partners, the DTA are willing to split such multilateral APA into several bilateral APAs.

### 17.3.3. Coverage

According to the State Secretary, an APA ruling may cover all transfer pricing issues of a taxpayer, although APA requests may also be limited to certain specified transactions. Although most APAs provide for a validity period of 4 to 5 years, a taxpayer is in principle free to request a period that he deems fit. Such period will depend on the nature of the activities and the term of relevance of the facts and circumstances applied on which the pricing was based. An extended validity period may e.g. be accepted for long-term contracts.

An APA may have limited retroactive effect, provided that the relevant facts and circumstances included in the APA request are comparable to prior years' facts and circumstances. Retroactive effect as regards unilateral APAs will only be accepted by the DTA if it is determined that such effect will not result in a reduction of taxable profits of open years which could effectively lead to part of such profits not being taxed at all. As regards bilateral and multilateral APAs, retroactive effect will only be possible upon agreement of the other countries involved.

### 17.3.4. Process

The APA Decree describes various measures to further develop and streamline the APA process. These measures include (i) a pre-filing meeting and (ii) a joint case management plan.

A pre-filing meeting provides the taxpayer the option to discuss the APA request with the APA/ATR Team prior to filing the request. It allows the taxpayer to obtain clarity on which information is actually necessary (reducing the administrative burden) and what elements are essential for the outcome of the formal APA request.

The joint case management plan can be prepared together with the APA/ATR Team in which the process and timing between the filing and the completion of the request is described. Although the DTA aim to finalize a procedure as efficiently as possible, the plan should provide the taxpayer more certainty on the time frame of the handling of the APA request.

An APA request must meet extensive documentation requirements. According to the APA Decree, the following information must be provided:

- information on the transactions, products, business or arrangements that will be covered by the request (including, if applicable, a brief explanation of why not all of the transactions, products, businesses or arrangements of the taxpayer(s) involved in the request have been included);
- information about the enterprises and PEs involved in these transactions or arrangements;
- the names of the other state or states to which the request relates;
- information regarding the worldwide organizational structure of the applicant's group (including information on the beneficial owners of the applicant's capital), information on the history, financial data, products and functions of the applicant, and information on the assets (tangible and intangible) and risks of any of the associated enterprises involved;
- a description of the proposed transfer pricing methodology, including a comparability analysis which includes comparable data from unrelated market parties and possible adjustments;[143]
- the assumptions underpinning the request and a discussion of the effect of changes in those assumptions or other events, such as unexpected results, which might affect the continuing validity of the request;
- the financial years to be covered; and
- a general description of market conditions, including industry trends and the competitive environment.

Contrary to the regular transfer pricing documentation requirements (*see* section 13.), the APA request should include a comparability analysis and comparable data from unrelated market parties and possible adjustments. It is furthermore noted that in order to obtain an APA, the taxpayer has the burden of proof that transfer pricing included in the APA request is correct. To the contrary, outside the scope of an APA, the burden of proof as regards the correctness of the transfer pricing applied is with the DTA, provided that the taxpayer has met its documentation requirements.

Although the DTA do not require a set form in respect of the format and content of the comparability analysis and data (including possible adjustments), the DTA in practice appear to prefer TNMM benchmark reports based on a large database samples. Practice shows that the process of obtaining an APA will be more efficient if the following information is included in the APA request:

(1) A description of the transactions between the affiliated entities, which includes the specifics of the goods and services, the functions performed by the parties, the economic environment, the business strategy, and, if so desired, an analysis of the industry.

(2) The choice for a pricing system; depending on the method applied, a net profit indicator (or NPI) should also be included.

(3) A description of the search strategy, i.e. the criteria that third-party transactions had to meet.

(4) The years which were included in the search (and the reason for including these years).

(5) The sources used. Sources should be publicly available; the DTA are familiar with Bureau van Dijk's Amadeus and Orbis Databases and Thomson Reuters LPC's DealScan.

143. In order to reduce administrative burdens, the DTA are willing to assist so-called "small companies" (i.e. according to art. 2:396 of the Dutch civil code, companies with total asset value less than EUR 4.4 million, net turnover less than EUR 8.8 million and, on average, less than 50 employees during the year) in providing comparability data.

(6) The comparables used. The reference group is determined on the basis of a qualitative comparison of the uncontrolled transactions and the transactions identified in (1). Once the reference group is set, it needs to be determined whether corrections are needed to improve comparability.

(7) How the data has been corrected based on "financial adjustments".

(8) An analysis of the data and a determination of a reliable range. The assumption is that loss-making companies should be excluded. If loss-making companies are included in the search, an explanation is required.

According to the EU Joint Transfer Pricing Forum 2013 statistical report, a total number of 323 APAs were requested in 2013 (no separation is made between bi-/multilateral APAs and unilateral APAs). During the year 2013, 228 APAs were granted by the DTA, 5 were rejected and 65 were withdrawn by the taxpayer. Average lead time for bi-/multilateral APAs during 2013 was 24 months.[144]

### 17.3.5. Fees

No fees are due for the filing of APA (and ATR) requests.

### 17.3.6. Timing of APA process

Generally, notwithstanding the possibility of limited retroactive effect, APAs cover future periods whereas tax audits deal with past events. Although the two do not generally coincide, agreements reached with the DTA in the scope of a tax audit (i.e. provided that the dispute concerns issues of transfer pricing) may be extended to future periods in the form of an APA.

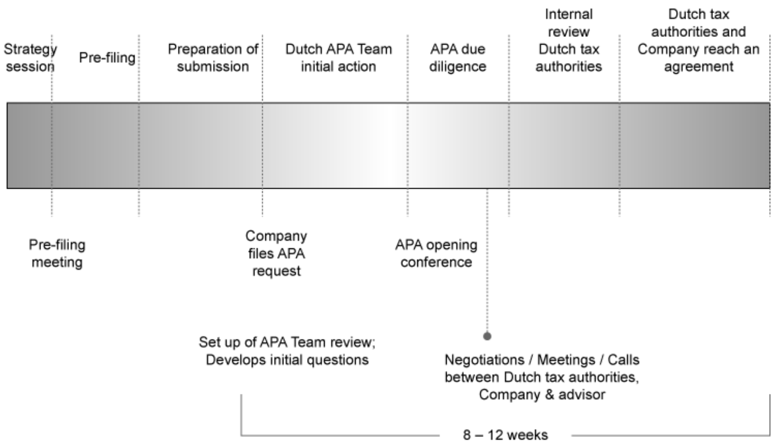
### 17.3.7. Timeline for unilateral APA

The duration of a unilateral APA is subject to the facts and circumstances of the case. In general, the APA filing process can be divided among four phases. These are mentioned below together with an indicative timing:

- pre-filing meeting (1 month preparation);
- request (2 weeks after meeting);
- input APA/ATR Team (4 weeks after request); and
- finalization (2 weeks)

144. EU JTPF's statistical report for 2013; available at: http://ec.europa.eu/taxation_customs/taxation/company_tax/transfer_pricing/forum/index_en.htm#new.

The estimated timeline for a Dutch unilateral APA is depicted below:




### 17.3.8. Timeline for bilateral APA

Bilateral APAs generally take more time than the indicative duration mentioned for unilateral APAs (*see* section 17.3.7.).

### 17.3.9. Withdrawal

The DTA may withdraw an APA if a taxpayer no longer applies the critical assumptions included in the APA. As a consequence, the taxpayer may no longer rely on the tax treatment of the transactions covered in the APA.

### 17.3.10. Agreement with taxpayer

Under the APA policy, certainty in advance is provided in the form of a settlement agreement (*vaststellingsovereenkomst*). Such agreement is binding on both the DTA and the taxpayer. APAs may include transfer pricing issues covering different types of related-party transactions, including transfers of tangible or intangible assets, financing or licensing activities and the provision of intra-group services. APAs may cover all the taxpayer's transfer pricing issues or may be limited to one or more specific issues. An APA will only be granted if the taxpayer waives its right to object to an exchange of information with a foreign country.

Because APAs generally cover future transactions, they include critical assumptions on the circumstances that are of influence on the remuneration of these transactions. Including critical assumptions in the APA reduces the risk for the taxpayer and the DTA of the agreement no longer resulting in an arm's length remuneration. In order to prevent the agreement from being reconsidered or revised for every single deviation from the starting position, the APA Decree allows for the elements covered by the assumptions to move within a certain range. It is assumed in the APA that deviations of these elements within the range do not affect the pricing.

### 17.3.11. Revocation, revision, renewal

*See* section 17.3.3.

### 17.3.12. Annual compliance

Dutch tax law or policy does not require Dutch taxpayers that obtained an APA to prepare and file an annual APA compliance. The taxpayer does need to specify in its CIT returns if it has obtained an

APA. In addition, FSCs without an APA are required to state in their tax returns whether or not they complied with the substance requirements (*see* section 17.3.1.).[145] If not all substance requirements are complied with, the taxpayer is required – separate from its tax return – to indicate which of the substance requirements have not been met. Furthermore, a “defaulting” taxpayer will need to provide additional information on payments received and to specify in which of the source countries a request is made to rely on the Dutch treaty network or the EU Interest & Royalty Directive. The DTA intend to spontaneously exchange such information with the relevant source countries in order to allow them opportunity to assess whether FSCs should be entitled to the aforementioned benefits. Not providing the information may result in a penalty for an amount up to EUR 19,500.

#### 17.3.13. Number of APA requests and APAs concluded; timeline

The number of APA requests and the number of APAs concluded are listed below:

| **APAs** | **2010** | **2011** | **2012** | **2013** | **2014** |
|---|---|---|---|---|---|
| Concluded | 205 | 248 | 247 | 228 | 203 |
| Rejected | 0 | 7 | 9 | 5 | 3 |
| Withdrawn/no longer processed | 67 | 64 | 65 | 67 | 58 |
| Total filed | 272 | 319 | 321 | 300 | 264 |

### 17.4. Engagement with tax authorities on pricing matters outside a formal APA process

It is possible to rely on the treatment of past positions as regards future years (i.e. under the principle of legitimate expectations) provided that facts and circumstances have not changed.

## 18. Transfer Pricing and Customs Valuation

### 18.1. Competent authorities

The Appraisement Team Value and Tariffs (*Landelijk Waarde Team*) of the Dutch Customs authorities deals e.g. with transfer pricing issues in relation to the imports of goods and performs audits on customs values where these are based on transfer prices. Parties concerned can request the Appraisement Team Value and Tariffs for a ruling, whereby parties concerned and customs agree upon the methods to be used for determining the customs value of goods to be imported.

### 18.2. Arm’s length value for customs duty purposes

Customs duties for most goods to be imported in the Netherlands will be calculated as a percentage of the customs value of these goods. The customs value of goods is based on article VII of the General Agreement on Tariffs and Trade. The EU has implemented this article in the European Community Customs Code (CCC).[146]

The main valuation method is the transaction value. The transaction value is defined as follows under article 29 of the CCC: “The price actually paid or payable for the goods when sold for export to the customs territory of the Community, adjusted, where necessary, in accordance with Articles 32 and

145. Art. 3a of the decree to the WIB (*international bijstandsverlening bij de heffing van international belastingen*).
146. Arts. 29-33 of Regulation (EEC) no. 2913/92.

33." However, the transaction value can only form the basis for the determination of the customs value provided certain conditions are met. One of these conditions states that the buyer and seller are not related or, alternatively, where they are, that the transaction value is acceptable for customs purposes.

The fact that the buyer and the seller are related will not in itself be a sufficient basis for regarding the transaction value as unacceptable. The transaction value must be arm's length. It will be considered as such provided that the relationship did not have an effect on the price. Where a sale takes place between related persons, the transaction value is acceptable if it is demonstrated that such value is similar to:[147]

- the transaction value in sales between buyers and sellers who are not related in any particular case, of identical or similar goods for export to the Community (i.e. equivalent to the CUP Method); or
- the customs value of identical or similar goods, as determined by using the method of article 30(2)(c) or (d) of the CCC (i.e. the resale minus method or cost-plus method).

Where the customs value is based on the transaction value, certain conditions apply with regard to the costs that need to be included or excluded from the customs value. Examples of costs that need to be included in the customs value are:

- royalty payments related to the goods being valued which the buyer must pay as a condition of sale;
- services supplied at reduced or no costs by the buyer for use in connection with the production and sale for export of the imported goods; and
- cost of freight and insurance of the imported goods.

Examples of excluded costs are:

- buying commissions;
- transport of products after their arrival at the place of introduction into the EC customs territory; and
- financing costs,

provided that these costs can be distinguished from the price paid or payable.

In case the value cannot be determined on the basis of the above methods, the customs value can be determined on the basis of reasonable means. One of these reasonable means is the TNMM, a method often applied for the valuation of goods for CIT purposes. The customs value of goods has to be determined under strict compliance with the rules described above. The value of goods for CIT purposes on the other hand is not determined on basis of strict methods. Therefore, the TNMM is often used for CIT purposes whereas for customs purposes this method can only be applied as a last resort.

As regards the interests in relation to customs valuation possibly conflicting with the interests in relation to income taxation, the following is noted. Where an importer will prefer to have a lower customs value resulting in lower customs duties, a taxpayer will generally want to attribute a high value to those goods for income tax purposes (i.e. a high "transfer price"). As a result of these diverging interests, care should

147. If based on the transaction value, certain conditions apply with regard to the costs that have to be included or excluded from the customs value.

be taken when calculating the value for customs or income tax purposes; e.g. benefits that can be achieved for CIT may on the other hand lead to losses for customs duties (and vice versa).

## 18.3. Transfer pricing adjustments

Importers are obliged to correctly declare the customs value of goods in import declarations. Declaring an incorrect customs value in import declarations will result in incorrect import declarations. According to article 10:5 of the General Customs Act, filing incorrect import declarations is a punishable event. As a result thereof fines can be imposed. The amount of the fine is at maximum equal to 100% of the underpaid duty. In general, the amount of fines will be mitigated. Dutch customs will in general not impose fines in case the customs value of goods decreases and no additional import duty is due.

In case of a retroactive price adjustment that leads to a decreased customs value, one could conclude that in fact too much import duty has been paid. Importers are not required to report a too high incorrect customs value, but can report it and request for refund of duty. Such request can be filed within 3 years after the date that the import duty became due. Note that a request for refund can be successful only in case the price adjustment has been agreed in advance and is assignable to past imports.

Where, as a result of a retroactive price adjustment, the reported customs value increases, importers should report this price adjustment and pay additional import duties. Not reporting the correct customs value could lead to a duty assessment and imposing of fines. Customs can levy additional import duties over a period of 3 years. However, in case customs has the view that the importer underpaid import duty intentionally, the period for levying import duty with retrospective effect can be extended to 5 years.

## 18.4. Change to customs value

A change in the customs value of a product or of products will impact the amount of customs duties due; however, it will in principle not have any consequences from a transfer pricing perspective.

## 18.5. VAT or GST treatment of transfer pricing

### 18.5.1. Competent authority

No separate tax authorities are competent for VAT. VAT specialists are assigned to all 13 offices of the DTA that are competent for national taxes. Which specific office is competent in principle depends on the place of establishment of the company. For foreign-established companies, the DTA for foreign companies in Heerlen (*Belastingdienst Buitenland*) is competent.

### 18.5.2. Cooperation between competent authorities for VAT and transfer pricing

No standard procedures are prescribed on how transfer pricing and VAT departments have to cooperate or exchange information. In principle, the departments work separately from each other. Nevertheless they can, and sometimes do, work together and exchange information. It is not precluded to conduct joint audits, although such audits do not take place regularly.

### 18.5.3. Transfer pricing adjustments

No specific rules for the VAT treatment of transfer pricing adjustments are implemented in the Dutch VAT legislation.

VAT implications occur if the transfer pricing adjustment leads to actual correction between parties involved of the initial prices invoiced. In case the initial price was too low, the adjustment will be seen as a price increase, which increase is an "ordinary" part of the taxable amount as defined in article 8 of the Dutch VAT Act 1968. In the mirror situation, a decrease of the price, the supplier is, based on article 29(b), first paragraph, of the Dutch VAT Act 1968, entitled to a refund of the VAT included in the price decrease. According to administrative guidelines, this refund can be claimed via the ordinary VAT return instead of filing a separate request. The customer in such situation is due the VAT included in the decrease if and to the extent that the customer deducted the VAT relating to the supply. In case of such price adjustment, the invoicing rules should be taken into consideration and the supplementary invoices should meet the invoice requirements of article 35a of the Dutch VAT Act 1968.

In case a supplier or customer has not taken into account a price increase or decrease as a consequence of which too less VAT was remitted or too much VAT was refunded, the DTA can impose penalties. In the event that the taxpayer voluntarily corrects its return before the DTA are aware or reasonably could be aware of the omission, no penalty is imposed provided that the VAT too less remitted or too much refunded is less than EUR 20,000 or less than 10% of the remitted or refunded VAT (article 67c of the General Tax Act and paragraph 24A under 3 of the Administrative Fine Decree).[148] In other voluntary cases the penalty is 5% of the amount involved with a maximum of EUR 5,278 (article 67c of the Dutch General Tax Act and paragraph 24A under 3 of the Administrative Fine Decree). In non-voluntary cases the fine varies between 25% (in case of omission) and 50%/100% (gross negligence/ intention) according article 67f of the General Tax Act and paragraphs 25 and 28 of the Administrative Fine Decree. Since 2012, not informing the DTA about a discovered omission is a separate finable conduct for which a fine of a maximum 100% of the amount involved can be imposed according to article 10a of the General Tax Act, article 15 of the VAT Implementing Decree 1968 and paragraphs 28A and 28E of the Administrative Fine Decree.

Filing an incorrect EC Sales Listing can be fined by the DTA with a fine of a maximum EUR 5,278 according to article 40 of the Dutch VAT Act 1968.

### 18.5.4. Open market value or arm's length price

In principle, the transaction value in the Netherlands is the taxable amount for supplies of goods and services (according to article 8, first and second paragraphs, of the Dutch VAT Act 1968) as well as for intra-community acquisitions (article 17b of the Dutch VAT Act 1968). For importation of goods, the customs value, including import duties, excises and ancillary costs, is the taxable amount (article 19 of the Dutch VAT Act 1968).

An exception to the transactional value applies to:

- Deemed supplies of goods:[149] For these supplies, the taxable amount is the purchase price of the goods or of similar goods or, in the absence of a purchase price, the cost price determined at the time those deemed supplies take place.

148. Decree dated *16 Dec. 2013 (BLKB2013/1814M).*
149. A deemed supply of goods is (i) the withdrawal by an entrepreneur of goods forming part of his business assets for his private purposes or those of his staff, which he provides free of charge or, more generally, their use for purposes other than those of his business, where the tax on the goods in question or their component parts was wholly or partly deductible, or (ii) the transfer of own goods by an entrepreneur from the Netherlands to another EU Member State.

- Deemed supplies of services:[150] For deemed supplies of services, the taxable amount is formed by the expenses incurred by the entrepreneur for the performance of the services.

The Dutch VAT legislation also contains the “normal value” as taxable amount. Currently, the normal value only applies as taxable amount for the situation in which a car is given in use for non-business purposes to a customer who is connected[151] to the supplier and who does not have a full right to deduct input VAT, while the remuneration is lower than the normal value.

The normal value in this regard is (according to article 2a, first paragraph, under s of the Dutch VAT Act 1968): “The full amount, excluding VAT, that the customer of the goods or services would have to pay to a supplier at arm’s length in the Netherlands to obtain the goods or services in question at the time the goods or services are supplied, at the same marketing stage at which the supply of goods or services is made, under conditions of free competition.” In absence of a comparable supply of goods or services, the normal value is, in respect of goods, a value that is not less than the purchase price of the goods or of similar goods or, in the absence of a purchase price, the cost price determined at the time the supply of goods is made. In respect of services, the normal value is then a value that is not less than the full cost to the entrepreneur of providing the service.

Finally, a proposal to apply the normal value also in cases of the supply or lease of investment goods between related parties has been presented by the Ministry of Finance in 2005.[152] Until now, this proposal was not further pushed into the legislative process as the Ministry of Finance first wanted to explore the possibility to stop undesirable situations with the concept of “abuse of law” as developed by ECJ case law.[153]

# 19. Other Transfer Pricing Issues

Not applicable.

# 20. Texts of Relevant Provisions

## 20.1. Basic transfer pricing provisions in tax laws

Article 8b CITA

(1) If an entity, directly or indirectly, participates in the management or supervision, or in the capital of another entity, and the agreed or imposed conditions (transfer prices) of the transactions between these entities deviate from the conditions that would have applied in the market between independent parties, the entities’ profit is determined as if the arm’s length conditions had been agreed upon.

(2) The first paragraph applies in a similar manner if a person, directly or indirectly, participates in the management or supervision, or the capital of the one and the other entity.

(3) The entities mentioned in the first and second paragraph shall include information in their administration, which shows the manner in which the transfer prices that are referred to in the

150. A deemed supply of service is (i) the use of goods forming part of the assets of a business for the private purposes of the entrepreneur or of his staff or, more generally, for purposes other than those of his business, where, in respect of those goods, the entitlement has arisen to deduct the tax, in full or in part and (ii) the supply of services provided free of charge by the entrepreneur for his private purposes or for those of his staff or, more generally, for purposes other than those of his business.
151. A connected customer in this respect is an employee, a family member or a person who has an administrative relationship with the entrepreneur.
152. Based on art. 80 of the EU VAT Directive.
153. E.g. European Court of Justice (ECJ), 21 Feb. 2006, Case C-255/02 (*Halifax*).

first paragraph were established, and from which it can be deduced if, in the market, the transfer prices that were established would have been agreed upon between independent entities.

## 20.2. Guidance issued by tax authorities or Ministry of Finance

### 1. Unofficial translation of the 2013 Decree

International Tax Law. Transfer prices, application of the arm's length principle and the Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations (OECD Guidelines).

Directorate-General for Fiscal Affairs, Directorate International Fiscal Affairs

Decree of 14 November 2013 no. IFZ 2013/184M

With respect to cross-border transactions there is consensus within the OECD member countries on the arm's length principle as included in Article 9 of the OECD Model Convention. The OECD Commentary on Article 9 of the OECD Model Convention and the Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations (OECD Guidelines) outline the arm's length principle in more detail.

In the Netherlands, the introduction of Section 8b Corporate Income Tax Act 1969 (CITA) in 2002 codified the arm's length principle in Dutch law.

Because the interpretation of the arm's length principle provided in the OECD Guidelines is internationally accepted, I regard the OECD Guidelines as an appropriate interpretation and clarification of the principle described in Section 8b CITA.

This Decree is a further elaboration of the arm's length principle. It focuses in particular on those aspects of the OECD Guidelines that leave room for interpretation or are unclear.

### 1. Introduction

### 1.1. Key to abbreviations and terms

| | |
|---|---|
| OECD Guidelines | Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations |
| OECD | Organisation for Economic Co-operation and Development |

The term "function(s)", in so far as used in this Decree, refers to: function(s), taking into account assets employed and risks assumed.

For the purposes of clarification, the corresponding chapter or paragraph numbers of the OECD Guidelines to which the text of this Decree refers are enclosed in parentheses.

### 1.2. Background to Decree

This Decree replaces the Decrees dated 30 March 2001, no. IFZ 2001/295 and 21 August 2004, no. IFZ 2004/680M on the arm's length principle. This Decree also deals with recent developments.

Important changes in relation to the above-mentioned two Decrees are:

- A more detailed description of the applicability of the arm's length principle (para. 2.1).
- Changes resulting from relevant amendments to legislation and case law (various paragraphs).

- Changes resulting from changes to the OECD Guidelines (new 2010 version).
- A narrow explanation of the use of the various transfer pricing methods described in the OECD Guidelines (para. 3).
- Clarification of the list of shareholder activities: these are not regarded as group services in so far as they do not add any economic or commercial value to the group members and if, and to the extent that, a group member would ordinarily not be willing to pay for these services (para. 6.2).This clarification is in line with the findings of the Joint Transfer Pricing Forum on group services as reported in its publication “Guidelines on low-value-adding services”.
- A clarification that corporate governance costs can also be mixed costs (para. 6.2.).
- The text on financial services in paragraph 12 has been replaced with text on financing transactions (partly in response to BNB 2012/37).

Situations involving non-arm’s length profit-shifting transactions can arise, which would be better avoided. This Decree outlines how avoidance is being dealt with in some situations:

- Intangible assets (para. 8).
- Intra-company purchases (para. 9).
- Internal reinsurance activities (para. 11).

The following new issues are also addressed:

- The relationship with the EU Joint Transfer Pricing Forum (para. 1.5).
- Guarantees for loan agreements (para. 10).
- The documentation obligation (para. 14).
- Early consultation (para. 15).

The following issues are no longer included:

- Administrative approaches for avoiding and resolving transfer pricing disputes (para. 3 Decree IFZ 2001/295). Its exclusion is a result of the publication of Decree IFZ 2008/248.
- Profit attribution to a head office and permanent establishment (para. 10 Decree IFZ 2001/205). Its exclusion is a result of the publication of Decree IFZ 2010/457.
- Withholding tax set-off (para. 6 Decree 2004).

In comparison to the text of the Decrees dated 30 March 2001, no. IFZ 2001/295M and 21 August 2004, no. IFZ 2004/680M, textual changes have also been made to clarify content or to make the text more understandable without the need for substantive changes.

**1.3. Transfer prices and monitoring**

As stated in the OECD Guidelines, transfer pricing is not an exact science and this should be borne in mind when assessing transfer prices. The Guidelines also encourage tax authorities to adopt a flexible approach for the very reason that transfer pricing is not an exact science and not require taxpayers to set their transfer prices with a precision that, given the facts and circumstances, is unrealistic. The Dutch Tax and Customs Administration will also take these basic assumptions into account.

The Dutch Tax and Customs Administration and the taxpayer need to cooperate constructively on the matter of transfer pricing and it is important that both parties appreciate the other party's position and what is at stake for them. Uncertainty can be avoided by making agreements in advance.

The above does not mean that situations of non-arm's length profit-shifting will never arise and they need to be avoided. This Decree outlines how avoidance is being dealt with in some situations. In working to avoid such situations, the Dutch Tax and Customs Administration's Coordination Group on Transfer Pricing will, if necessary, join forces with the Coordination Group on Tax Havens and Group Financing and the Coordination Group on Construction Avoidance.

### 1.4. Relationship with OECD Guidelines

The OECD Guidelines leave a number of issues open to interpretation, while on other issues the OECD Guidelines require clarification. This Decree sets out the Dutch position on these issues and, where possible, removes existing ambiguities.

The OECD Guidelines are an ongoing project and are regularly expanded and amended. The 2010 version of the OECD Guidelines amended Chapters 1 through 3, and added a new Chapter 9. If necessary, this Decree will also be amended to reflect new developments.

For the purposes of clarification, the corresponding chapter or paragraph numbers of the OECD Guidelines to which the text of this Decree refers are enclosed in parentheses. The version of the OECD Guidelines referred to thereby is that published by the OECD in July 2010.

### 1.5. Relationship with EU Joint Transfer Pricing Forum

One of the important tasks of the EU Joint Transfer Pricing Forum is to remove double taxation and administrative obstacles that impede an efficient application of transfer pricing rules. In general, the Netherlands follows the recommendations made by the EU Joint Transfer Pricing Forum; the exception being those cases where it has expressed reservations.

### 1.6. Implementation coordination

The Dutch Tax and Customs Administration's Coordination Group on Transfer Pricing is responsible for the implementation of transfer pricing policy. I refer, in this respect, to the Decree dated 11 August 2004, no. DGB2004/1339M.

## 2. The Arm's Length Principle (Chapters I and III)

### 2.1. General

#### Introduction

The arm's length principle is defined in Article 9 of the OECD Model Convention (*see also* para. 1.6 of the OECD Guidelines).

In the Netherlands, the introduction of Section 8b CITA in 2002 codified the arm's length principle in Dutch law.

The basic assumption of the arm's length principle is that, for tax purposes, associated enterprises are regarded as transacting with each other under the same conditions established by independent parties in comparable situations.

This means that the result achieved must be one in which the taxable profit achieved by associated enterprises on group transactions is comparable to the profit independent enterprises would achieve with comparable transactions carried out under comparable conditions.

The OECD Guidelines aim to provide insight into how the arm's length principle should be applied in practice.

In light of the above, I have assumed that the OECD Guidelines, in principle, directly impact Dutch law.

The OECD Guidelines also play an important international role in respect of the application of tax treaties and the avoidance of double taxation.

In light of the importance of the arm's length principle, this paragraph will first address the overall position presented in the OECD Guidelines with regard to the principle's application.

**The application of the arm's length principle**

The basic assumption underlying the application of the arm's length principle is the transaction as it has been structured by associated enterprises (para. 1.64 OECD Guidelines). The contract is the starting point, unless the actual conduct of the parties involved deviates therefrom (para. 1.48 and para. 1.53 OECD Guidelines). In cases where there is no written contract, the contractual relationship must be deduced from the conduct of the parties and the economic principles governing their relationship (para. 1.52 OECD Guidelines).

The starting point for the arm's length test is the comparability analysis − the search for comparable transactions under comparable conditions. The functional analysis of the parties involved in the transaction is central to this comparability analysis. The compensation the parties involved will receive is determined by the functions performed, the risks assumed and the assets employed.

The arm's length test described in paragraph 6 is applied to the conditions under which the associated enterprises entered into a transaction. These conditions are compared to the conditions that independent parties engaged in comparable transactions under comparable conditions would have agreed upon. In this respect, the price is only one aspect of the conditions (para. 1.7 OECD Guidelines). Where the conditions between the associated enterprises deviate from those that independent parties would have agreed, the impact on the taxable profit can still be corrected.

This comparison of conditions involves a number of basic assumptions. Paragraph 1.34 of the OECD Guidelines states that the "Options Realistically Available" to the parties involved under the arm's length conditions and the fact that independent parties will only enter into a transaction if there is clearly no alternative that is more attractive, must be taken into account. Paragraph 9.63 of the OECD Guidelines states that the conditions must be compared from the perspective of all the parties involved in the transaction.

If it is only the price of the controlled transaction that differs from the price that independent parties would have agreed on, a pricing adjustment should be made for tax purposes. If conditions other than the price differ and it is not possible to correct the taxable profit by way of a pricing adjustment, then, for tax purposes, the consequences of such non-arm's length conditions can be adjusted or disregarded (paras. 1.47-150 OECD Guidelines and para. 9.38 OECD Guidelines). In practice, situations can arise where it cannot be demonstrated that conditions comparable to those applied [to the transaction], for example risk allocation, would also apply (and how they would apply) to unrelated entities. Certain conditions are applied, for example risk allocation, where it cannot be demonstrated that (and not in which manner) such conditions apply in unrelated entities. Paragraph 9.36 states that although this is, of itself, no reason to disregard such a risk allocation, it could give cause to examine the economic logic of such a risk allocation. According to the OECD Guidelines, important factors thereby are the level of control and the financial capacity to assume the respective risk.

Paragraph 1.11 of the OECD Guidelines acknowledges the fact that associated parties undertake transactions that independent parties would not. In such situations, the comparison of conditions referred to in paragraph 1.6 is not possible, i.e. comparing the conditions with those that third parties would have agreed in respect of comparable transactions. However, the simple fact that no comparable transactions between third parties can be found does not mean that the controlled transaction could not be at arm's length. In such a situation, it should be considered whether there are indeed conditions under which it is conceivable that independent parties would undertake such a transaction under comparable conditions. The OECD Guidelines also provide guidance on such situations. Paragraph 9.173 of the OECD Guidelines states that a business restructuring can lead to a business model being implemented that would not be used between independent parties. Paragraph 9.174 of the OECD Guidelines therefore states that it needs to be ascertained whether the transaction accords with what would result from the normal commercial behaviour of independent parties. This paragraph goes on to state that taking the options realistically available into account can be relevant for the question whether the structure given to the transaction by the associated parties differs from what would have been adopted by independent parties behaving in a commercially rational manner. If this allows arm's length conditions to be found for the transaction, they must be applied and the transaction must be respected as being at arm's length.

In exceptional circumstances, whereby associated parties not only undertake a transaction that independent parties behaving in a commercially rational manner also would have undertaken under comparable circumstances, but for which no arm's length conditions can be found given the form and substance of the transaction, the Dutch Tax and Customs Administration may dispute the transaction (*see* para. 1.65 OECD Guidelines).

If paragraph 1.65 had not made it possible to dispute the transaction, in such cases the contractual structure would have made application of the arm's length principle impossible. Pursuant to paragraph 1.65, in such exceptional circumstances it should be ascertained whether the transaction can be requalified as a transaction for which arm's length conditions can be found. If requalification fails to lead to an arm's length outcome, then there is no option other than to completely disregard the consequences the transaction may have for the taxable profit. Completely disregarding the consequences is only relevant if the structure of the transaction, also after any requalification, is such that the Dutch Tax and Customs Administration cannot determine appropriate arm's length conditions. Requalification or disregarding [the consequences] only takes place in respect of determining the taxable profit.

### 2.2. Aggregating transactions (paragraphs 3.9-3.12)

According to the OECD Guidelines, arm's length compensation must, in principle, be determined on a transaction-by-transaction basis. However, there are often practical problems attached to such an evaluation. For example, if the large number of comparable transactions makes it difficult to carry out an evaluation on a transaction-by-transaction basis, the transactions may be evaluated together to determine whether the conditions are at arm's length. In such situations, the taxpayer is expected to be able to substantiate that the transfer price applied to the aggregated transactions as a whole is in line with the arm's length principle.

### 2.3. The use of a range (paragraphs 3.55-3.66)

In some cases it is not possible to arrive at a single figure for a transfer price. Because transfer pricing is not an exact science, the application of the chosen transfer pricing method will often lead to a range of figures within which the transfer price can be found. The range is the difference between the smallest and largest figures. The question that arises once the arm's length range has been determined and is in use, is which observations in the range can be selected as comparables and which comparability defects need to be adjusted.

In setting the range, a distinction must be made between situations whereby the reference material comprises variables with a relatively equal degree of comparability and situations where there is a lesser degree of comparability between the variables. If the reference material comprises variables with a relatively equal degree of comparability, then the range will be made up of these variables. If the reference material comprises variables with a lesser degree of comparability, then it will be necessary to enhance the reliability of the reference material through the use of statistical tools. An example is the interquartile range approach (interquartile deviation). Such statistical methods narrow the range, so that a relative range remains whose reference material is more reliable.

After the range has been set, it must be ascertained whether the payment for the controlled transaction falls within this range. If this is the case, no adjustment has to be made. If the payment falls outside the range and the taxpayer cannot present arguments to explain this deviation, an adjustment will be made. In such a situation, the OECD Guidelines provide for an adjustment up to the point in the range that is most consistent with the facts and circumstances of the relevant group transaction. If it can be demonstrated that a specific point in the range is the most consistent with the conditions of the group transaction, adjustments can only be made up to this point. If no such specific point can be identified, the Netherlands takes the position that adjustments should be made up to the median (the middle point in the range) (*see* para. 3.63 OECD Guidelines). It is possible that the State of residence of the associated enterprise will reject an adjustment up to the median of the range. In those cases, if so requested by the taxpayer, the competent authority in the Netherlands will enter into negotiations with the relevant State in order to reach agreement on a point within the range that is acceptable for both States.

Sometimes, shifts in the range will occur, due to an upward or downward adjustment of the initial transfer price. In such situations, the taxpayer must be able to demonstrate that the changed circumstances justify the transfer price having been adjusted. If no change in circumstances can be identified that would justify the adjusted transfer price, then the adjusted transfer price will generally have been indexed for tax purposes. In such cases, the Dutch Tax and Customs Administration will reject the adjusted transfer price. A prerequisite for accepting such a shift in the range is that the adjusted price is not only laid down in the agreement concluded between parties, but is also actually charged.

### 2.4. Use of multiple year data (paragraphs 3.75-3.79)

Examining multiple-year data can be useful when analysing a transaction. By using multiple-year data, adjustments in a particular year can be avoided where, considered over a number of years, the group received payments that were in line with the arm's length principle. Using multiple-year data can, however, also result in repeat situations being evaluated with the benefit of hindsight. The OECD Guidelines state that tax authorities must steer clear of hindsight and therefore multiple-year data must only relate to the year in question and preceding years. An example is the use of multiple-year averages, which leads to the following method:

- First, the controlled transaction will have to be analysed to see whether it falls within the arm's length range for that particular year. If this is the case, no adjustment has to be made.
- If the payment falls outside the range for that particular year, this analysis will be repeated on the basis of the average of a number of years (multiple-year averages). The length of the relevant period will in part depend on the product's life cycle. If the average payment for the controlled transaction falls within the multiple-year average, no adjustment will have to be made.
- If the controlled transaction falls outside both the arm's length range for that particular year and the arm's length multiple-year range, an adjustment is made in accordance with that described under 2.3.

### 2.5. The effect of government policies (paragraphs 1.73-1.77)

Some government intervention can be regarded as conditions of the market in a particular country and should be taken into account as such in the transfer price.

Paragraph 1.77 of the OECD Guidelines outlines two possible approaches for dealing with the situation whereby a country, for example, prevents or blocks a monetary payment. According to Dutch law, the payment related to the service provided must be accounted for in the result, but in accordance with sound business practice it is possible to partly or fully write down the claim arising from the services provided. The costs related to the transaction can also be taken into account. At the time the receivable arose it is, of course, necessary to ascertain whether circumstances can be identified which would lead to the conclusion that involves a provision of capital rather than a receivable (cf. for example Supreme Court, 27 January 1988, case no. 23.919) or a non-business motivated loan, whereby the write-down cannot be deducted from the result (cf. for example Supreme Court, 25 November 2011, 08/05323). Furthermore, the taxpayer must be able to substantiate the write-down.

### 2.6. Requests for reducing a transfer pricing adjustment (paragraphs 3.13-3.17)

As a result of a taxpayer audit by the Dutch Tax and Customs Administration, a taxpayer can file a request to have the proposed adjustment of a transfer price reduced, if it considers that the adjustment proposed by the Dutch Tax and Customs Administration has failed to take account of corresponding transactions. According to the OECD Guidelines, tax authorities have the discretionary authority to accept or reject the request. The distinction the OECD Guidelines makes between the moment evidence must be provided to demonstrate that the compensation was a conscious choice − at the time the tax return is filed or at the time the tax authorities present their proposals for adjustments as a result of an audit − is of no practical relevance for the Netherlands. In both cases, the taxpayer retains its legal right to file notices of objection against and appeal any decision.

## 3. Transfer Pricing Methods (Chapter II)

### 3.1. Introduction

The three traditional transaction methods (the comparable uncontrolled price method, the resale price method and the cost-plus method) and the transaction profit methods (the profit split method and the transactional net margin method or TNMM) are discussed in Chapter II of the OECD Guidelines.

Circumstances will dictate which of the five acceptable methods is applied.[154] The OECD Guidelines state that tax authorities should conduct their transfer pricing analysis from the perspective of the method chosen by the taxpayer (para. 4.9 OECD Guidelines).

Pursuant to paragraph 4.9 of the OECD Guidelines, the Dutch Tax and Customs Administration must always conduct its transfer pricing analysis from the perspective of the method applied by the taxpayer at the time of the transaction. The taxpayer is free to choose the transfer pricing method, provided the method leads to an arm's length outcome for the particular transaction. However, one method may be more suitable in certain situations. Although it can be expected that a taxpayer will take into account whether the method is appropriate to the particular situation when choosing which transfer pricing method to apply, it is most definitely not the intention that the taxpayer evaluate all the methods and subsequently substantiate why the method chosen will lead to the best results in the given circumstances (the "best method rule"). Although some situations may require the application of a combination of methods, the taxpayer is not obliged to apply multiple methods. The taxpayer will, however, have to substantiate its choice.

### 3.2. Points to consider when applying the cost-plus method

#### *Budgeted versus actual costs*

In general, prices are determined in advance based on budgeted costs. Whether a price adjustment will have to be made if the actual costs of the transactions are higher than budgeted is dependent on what caused this increase. In general, it can be assumed that the contracting party supplying the services will bear the increased costs resulting from inefficiencies. After all, it is the contracting party that can influence these costs and therefore an independent purchaser would not accept a price adjustment.

A prerequisite for correctly determining transfer prices based on budgeted figures is that there is a sound business basis for these budgeted figures.

#### *Pass-through costs*

Pass-through costs do not have to be included in the cost base. Pass-through costs refer to costs initially paid by the contracting party providing the service; these include administrative charges, court costs and service costs. In general, they should be charged separately to the principal. Although these costs are related to the services provided by the contracting party and are recharged, they do not warrant a separate reimbursement payment. Whether such costs should be regarded as pass-through costs depends on whether an unassociated contracting party would recharge these costs without markup. I refer to paragraph 2.93 of the OECD Guidelines.

### 4. Secondary adjustments (paragraphs 4.66-4.76)

Paragraphs 4.66-4.76 of the OECD Guidelines address the consequences of secondary transactions. In many countries, a transfer pricing adjustment is not limited to a profit adjustment, but requires a secondary adjustment to be made so that the financial records clearly show how the adjustment was accounted for in the taxpayer's income statement and balance sheet. Examples of secondary transactions are current account settlements, profit distributions or informal capital contributions. From a Dutch perspective, a transfer pricing adjustment must always be accounted for by way of a secondary transaction. A secondary adjustment therefore arises from a secondary transaction, for example, taking

154. *See* para. 2.9 OECD Guidelines for exceptions to the above.

into account the interest on a receivable or an additional assessment for dividend withholding tax in respect of a profit distribution. Not all countries apply the same system. As a result, the other State may not be prepared, for example, to set off the additional dividend withholding tax levied as a secondary adjustment, because the hypothetical dividend distribution is not recognized. If the taxpayer can convincingly demonstrate that − given the different tax systems of the States involved − the dividend withholding tax cannot be set off, and this does not involve abuse aimed at avoiding dividend withholding tax, then no secondary adjustment has to be made.

**5. Arm's length pricing when valuation is highly uncertain at the time of the transaction (paragraphs 6.28-6.35)**

Determining the value of intangible property, such as, for example, patents, at the moment it is transferred can be complicated if the anticipated benefits and risks are not sufficiently clear. According to paragraph 6.34 of the OECD Guidelines, the rule of thumb to be applied in such cases is that if independent enterprises would have insisted on a price adjustment clause in comparable circumstances, the tax authorities should be permitted to determine the pricing on the basis of such a clause.[155] This refers to an arrangement whereby the payment is in keeping with the benefits the intangible property will generate in future. Agreeing on a benefit-dependent payment helps to ensure that the tax better reflects the actual benefits earned. The Dutch Tax and Customs Administration will, in certain circumstances, also take the position that agreeing on a fixed price is not at arm’s length if the valuation at the moment of the transaction is highly uncertain, because independent third parties in comparable situations would not have agreed to a fixed price. In such cases, an adjustment clause must be included in the agreement concluded between associated parties, whereby the price is in part dependent on future income. An example of such a situation is where a new intangible asset is developed, which is transferred to an associated enterprise at a time when it is difficult to foresee how successful it will be, for example, because the intangible asset has not yet generated any income and there are significant uncertainties attached to any estimates of anticipated income. In such a situation, the valuation at the time of the transaction is highly uncertain and it is advisable to include a price adjustment clause in an agreement (cf. for example Supreme Court, 17 August 1998, no. 32.997).

I would like to elaborate on the above. Where an intangible asset is transferred to a (foreign) group company and a large part (i.e. more than 50%) of this intangible asset is subsequently licensed to the transferring Dutch company and/or a Dutch resident entity associated with this company, a price adjustment clause will be regarded as having been agreed, unless the taxpayer can convincingly prove that (i) the transaction was business-motivated and (ii) the valuation at the time the agreement was concluded was to such an extent determinable that independent enterprises would have not required a price adjustment clause.

All other situations must be evaluated on the basis of whether independent enterprises in comparable situations would have demanded a price adjustment clause. It will be appreciated that a price adjustment clause can result in either an upward or a downward adjustment of the price initially agreed.

Situations that are effectively the same as the aforementioned are those where a Dutch group company, after the transfer of an intangible asset, starts making payments, in an economic sense, to a foreign group company for the use of the transferred intangible asset. This may be the case where the payment has been included in the price of a good or service.

155. Para. 9.88 of the OECD Guidelines also leaves open the possibility of renegotiating the transaction, if independent parties would also have renegotiated the transaction as a result of differing values.

The “for the most part” test referred to above should be applied in a corresponding manner.

## 6. Intra-group services (Chapter VII)

### 6.1. Introduction

According to the OECD Guidelines, a group service has been rendered if an activity is performed for a group member that adds economic or commercial value to the group member and for which that group member would ordinarily be willing to pay. This does not relate to shareholder activities.

The transfer pricing method to be applied can be one of the methods discussed under 2.1 above. In practice, it appears that a cost-based payment is the preferred choice. Firstly, it will have to be determined whether this method is appropriate for determining the payment for the particular group services; this is done on the basis of a functional analysis. As a rule, this method can only be applied to more routine services.

The application of this method will, in principle, only involve an arm’s length payment if an appropriate profit margin was taken into account when determining the payment. Only specific situations such as also described in paragraph 7.33 of the OECD Guidelines would give cause to forgo a profit margin.

The OECD Guidelines express a clear preference for basing the recharging of group services on a direct charge method (para. 7.20). In practice, an indirect method is also often applied because of the practical problems associated with applying the direct charge method. Where such practical problems arise, the Netherlands will follow the indirect method chosen by the taxpayer. The method must, of course, also lead to a reliable result whereby the outcomes are in line with the arm’s length principle. An allocation key could be based on factors such as the relationship between, for example, turnover, the number of employees or staff costs. An allocation key whereby the payment to be charged is dependent on the profit will very quickly lead to an outcome that is in line with the arm’s length principle.

### 6.2. Group services and shareholder activities

Paragraph 6.1 states that under the arm’s length principle, a group service has been rendered if an activity is performed for a group member that adds economic or commercial value to the group member and for which that group member would ordinarily be willing to pay. This does not relate to activities performed in a shareholder capacity.

The shareholder activities listed below are regarded as being performed in a shareholder capacity and are therefore not regarded as group services in so far as they do not add any economic or commercial value to the group members and if and to the extent that the group member would ordinarily not be willing to pay for these services. Therefore, the taxpayer should not charge the other group companies for that particular part of the activities. Each category of activity includes examples of the relevant activities.

**List of shareholder activities**

1. Activities relating to the legal structure of the company itself

    1.1. Implementing the conditions of Book 2 Dutch Civil Code

    - organizing, preparing and holding the shareholders’ meeting;
    - activities involved with the preparation and approval of the annual financial statements and their filing with the Chamber of Commerce;

- activities performed by the Supervisory Board, in so far as they involve the implementation of statutory supervisory duties; and
- the activities of the Staff Council (*Ondernemingsraad*).

1.2. Implementation of the General Taxes Act, to the extent that this relates to the tax obligations of the company itself

2. Activities associated with the flotation/issuance/share split of shares in the company itself, or similar securities, on the capital market, and activities related to requesting/retaining the company's listing on domestic and foreign stock exchanges

3. Activities associated with the implementation and enforcement of the legal rules in respect of share transactions
   - implementing and maintaining a registration system pursuant to the Dutch Financial Supervision Act; and
   - the reporting of share transactions by staff of the company subject to this legislation.

4. Activities associated with the implementation and fulfilment of legal corporate governance rules and corporate governance codes of conduct at the company itself or the group as a whole[156]
   - the implementation of corporate governance monitoring as required by law, including a paragraph thereon in the annual report; and
   - reporting on the implemented/to be implemented environmental policy, social policy and policy on corporate responsibility.

5. Activities associated with preparing reports on the company itself or the group as a whole for circulation to various interested parties
   - press conferences and other communication costs in respect of communications to shareholders and other interested parties, such as financial analysts, in so far as the communication relates to external reports, the financial performance of, and expectations for, the company itself and the group as a whole.

The above list is not exhaustive. This means that activities not appearing on the list will have to be assessed on an individual basis to determine whether they are a group service or an activity performed in a shareholder capacity.

Qualifying the activities as group services or shareholder activities may give rise to “mixed” activities. Mixed activities refer to activities performed by a department or other group of individuals operating within the group, which partly qualify as group services and partly as shareholder activities. Examples of group activities are consolidation activities, merger and acquisition (M&A) activities, activities associated with the implementation and fulfilment of legal corporate governance rules and corporate governance codes of conduct, and activities of the Board of Directors. The qualification of the activities as group services or shareholder activities can be based on any method that leads to an outcome in line with the arm’s length principle.

The following are examples of situations involving mixed activities.

156. The group as a whole consists of the company itself and its direct and indirect subsidiaries.

*Example A (consolidation activities)*

A group uses a management information system that includes the results of all the group companies. This information is used for budget decisions, the management and evaluation of the respective group companies, as well as for the preparation of the quarterly, half-yearly and annual consolidation reports that form the basis for the annual financial statements. Setting up and maintaining the management information system and processing the information that is relevant to the management of the group companies involves a group service. The preparation of the regular consolidation figures for the holding company/intermediate holding company, which are prepared on the basis of the information supplied by the management information system, is a shareholder activity.

*Example B (merger and acquisition activities)*

The European head office of a group has a Mergers & Acquisitions Department. The group needs an additional production facility in Europe. It is the task of the department to analyse which businesses in the various European countries are candidates for a potential acquisition that will be carried out by the European head office. The analysis carried out by the Mergers & Acquisitions Department is an activity performed in a shareholder capacity and therefore the group companies cannot be expected to pay for this activity.

*Example C (merger and acquisition activities)*

The Mergers & Acquisitions Department referred to in the above example analyses which businesses on continent X (not Europe) are candidates for a potential acquisition geared to expanding the market share on that continent. On the basis of the analysis, a business on continent X is acquired by the regional office. The regional head office on continent X was the recipient of a group service. The fee to be charged for this activity must be at arm's length.

*Example D (merger and acquisition activities)*

The group has a department that deals with mergers and acquisitions. This department assists an acquired business with the legal implementation of the acquisition (e.g. delisting the shares), with making changes to the system and house style of the group, and preparing and implementing the staff guidelines. This assistance adds economic and/or commercial value to the acquired group company for which an independent third party in comparable circumstances would be willing to pay. A group service has been provided to the particular group company. The fee to be charged for this activity must be at arm's length.

**Advance certainty**

If so desired, the tax inspector can be requested to provide advance certainty on the type of activity involved: is it a group service performed for the group companies or a shareholder activity? Such requests are regarded as requests made under the Decree establishing the Coordination Group on Transfer Pricing dated 11 August 2004, no. DGB2004/1339M. Should the taxpayer not only wish to receive advance certainty on the qualification of the activities, but also on the arm's length nature of the transfer price, it can request an Advance Pricing Agreement (*see* the Decree on the Procedure for dealing with requests for advance certainty in respect of the transfer prices to be applied in cross-border transactions dated 11 August 2004, no. IFZ 2004/124M).

### 6.3. "Support" services

Paragraph 6.1 of this Decree states that, in principle, payments for the provision of group services are only at arm's length if an appropriate profit margin was taken into account when determining the payment. In practice, such an arm's length payment for group services is often determined by applying the cost-plus method (i.e. the markup is a percentage of the costs) and a cost base derived from (estimated) direct and indirect costs. In principle, the markup must be sufficient to cover the overhead costs and allow an appropriate profit to be achieved.

The basic assumption underlying an arm's length payment based on an appropriate profit margin is retained. On the basis of a cost-benefit analysis as referred to in paragraph 7.37 of the OECD Guidelines, it was decided which ancillary services, in principle, do not have to be adjusted by the Dutch Tax and Customs Administration, in those cases where the taxpayer has opted to charge all the relevant actual costs, rather than determine an arm's length payment. The conclusion was that ancillary services generally refer to accounting services, legal services, tax services and services provided by Human Resources departments. In these cases, an adjustment will nevertheless be made if (i) the activities involved are part of and add more than marginal value to the primary business of the group or (ii) the particular services are provided on a recurring basis to non-associated parties.

It is conceivable that for services other than those listed above, a cost-benefit analysis as referred to in paragraph 7.37 of the OECD Guidelines would justify charging the relevant actual costs, as opposed to determining an arm's length payment. It is, however, not possible to make a general statement on what these other services are, given the complexity of global businesses, their different structures and business processes.

Further to the above, if a taxpayer requests permission in advance to charge the relevant actual costs for services other than those listed above, rather than determine an arm's length payment for those services, I give approval for the Dutch Tax and Customs Administration to accept such a situation pursuant to paragraph 7.37 of the OECD Guidelines, provided the taxpayer can convincingly demonstrate that the activities (i) are not part of, or only add marginal value to, the primary business of the group and (ii) are performed for third parties on a non-recurring basis. Such requests are regarded as requests made under the Decree establishing the Coordination Group on Transfer Pricing dated 11 August 2004, no. DGB2004/1339M.

In determining whether this involves the primary business of the group, the Dutch Tax and Customs Administration will determine this on the basis of the following elements:

- *What type of activities are involved?*

  In general, primary business activities refer to: production, purchasing, sales, marketing, product development and research and development.

- *What is the relative scale of the activities within the group?*

  The relative scale of the activities is evaluated on the basis of the total scale of comparable activities and activities that go hand in hand with the particular activities performed in the group as a whole. Factors taken into account are the number of staff involved, the costs related to the activities, the investment (equity and debt) required to perform the activity or a combination of these factors.

- *What is the added value of the activities?*

### Relevant actual costs

The chargeable relevant actual costs include direct and indirect costs related to the respective ancillary services and overhead costs. Therefore, relevant costs also include financing and exceptional costs (such as redundancy and reorganization costs, and salary in kind). The functional analysis underlying the taxpayer's transfer pricing system will determine which costs are relevant.

### Separate legal entity

The above applies regardless of which legal entity within the group provides the ancillary services. As such, no adjustment will be imposed in cases where all the relevant costs in respect of ancillary services performed by an entity that also performs other activities are charged, nor in cases where the ancillary services are performed by a separate legal entity (this could include, for example, a shared service centre).

The following examples will serve to illustrate the above.

Examples

*Example E*

A group provides legal services to third parties. A foreign group company that is involved with advising a client on an international transaction receives advice on the local legal aspects of the transaction from an employee of one of the group companies. The charge for this activity should be at arm's length because the activities performed form part of the primary business of the group. Moreover, the particular services are provided to non-associated parties on a recurring basis.

*Example F*

The legal department of a bank is actively involved with the design of a bank product that another group company wants to offer. The activity performed by the legal department is an activity that adds more than marginal value to the primary business of the group. For that reason, an arm's length payment must be determined and charged to the other group company. It is not sufficient to charge all the relevant actual costs.

*Example G*

The only activity performed by a help desk department is answering the questions posed by employees of the different group companies regarding the computer system, the software and helping solve minor user problems. On the basis of the type of activities involved, the relative scale of the activities within the group and the added value of the activities, the taxpayer convincingly demonstrates that this does not involve the primary business of the group. It also convincingly demonstrates that the value added to the primary business of the group by the activities is only marginal. At the taxpayer's request, the Dutch Tax and Customs Administration can approve the relevant actual costs being charged, rather than an arm's length payment.

*Example H*

A group operates an international hotel chain. One department is concerned with the implementation and maintenance of an intra-group computer application that will make the reservations, invoicing and inventory procedures available online. Although these activities presumably are not part of the primary business of the group, they do add significant (more than marginal) value to the primary business. The fee charged by the taxpayer for this activity must be at arm's length.

*Example I*

A company is a contract manufacturer that performs its activities under the management and for the risk of another group company. These types of manufacturing activities generally form part of the primary business of the group. Furthermore, these activities, together with similar activities or activities that go hand in hand with these activities (such as, for example, the manufacturing activities of the principal) generally are an important part, in absolute or relative terms, of the total activities of the group. The fact that the added value of these activities is only marginal is not sufficient reason to regard them as ancillary activities. The fee charged by the taxpayer for these activities must be at arm's length.

**6.4. Contract research**

In certain situations where a group company A (the developer) concludes a contract with a group company B (principal) and carries out contract research (the design of intangible fixed assets) on a contractual basis for the account and risk of group company B, a payment based on the cost-plus method can be regarded as being at arm's length. This is the case if the contract research activities are developed by group company A, while group company B manages the research activities, bears the costs and risks and will have the economic ownership of the developed assets. This must be evaluated on the basis of the facts and circumstances.

The following elements are factors in answering the question who manages the research activities: the decision-making, planning, budgeting, measuring the performance of, remuneration, changing/ redefining the sphere of activity, establishing which areas are commercially valuable, and evaluating the chances of success of the research. To answer the question who bears the risk, the contractual conditions will, in principle, be adhered to, unless the risk split is not in line with the functions performed (for example, the principal, as manager, does not have the expertise to manage the risks contractually allocated to it or the principal lacks sufficient equity to assume the financial risk contractually allocated to it), or the contractual conditions differ from the functions actually performed. The payment received by each company must be individually determined on the basis of the functions performed, taking into account the risks assumed and the assets employed. This will require attention to be paid to whether the principal is financially able to assume the risks and has the expertise to adequately manage these risks. The following examples will serve to illustrate the above.

**Examples**

*Example J*

A group has a head office in country X. The group produces and sells consumer products. In order to maintain and, where possible, improve its market position, research is continuously being carried out to improve existing products and develop new ones. The group has two R&D units that have been transferred to a separate company, which is resident in both country X (R&D X, as part of the head office) and in the Netherlands (R&D NL). The research programs for the group as a whole are prepared by R&D X, after the strategic decisions have been taken by the group management. R&D NL subsequently carries out part of the research program on the basis of separate contracts. R&D NL must submit the detailed project plans for the development of its part of the research program to R&D X. R&D X is responsible for approving the project plans and the accompanying budgets. Any suggestions R&D NL may have in respect of changes to the research program and/or the project plans already submitted, must also be submitted to R&D X. R&D NL provides regular progress reports to R&D X in respect of the research and the depletion of the budget. In the case of budget overruns, R&D NL must request additional financial resources from R&D X. Not all research activities are equally successful. Under the contractual terms agreed on between R&D X and R&D NL, all risks attached to the development undertaken by R&D NL are for the account and risk of R&D X. R&D X will own all legal and economic rights resulting from the research. R&D X has sufficient equity to assume the financial risks associated with the research. The payment R&D NL receives from company Y is calculated on the basis of the cost-plus method.

Conclusion: The functions performed by R&D NL are limited to the R&D activities. These activities are performed on behalf of R&D X that manages the activities (including control and decision-making). The risks attached to the R&D activities are for the account of R&D X. R&D X has the financial means and the professional expertise to assume and manage these risks. It is correct that the activities performed by R&D NL are regarded as contract research. Applying the cost-plus method leads in this case to an arm’s length payment.

*Example K*

A group has a head office in country X. The group produces and sells consumer products. To hold and, where possible, improve its market position, research is continuously being carried out to improve existing products and develop new ones. The R&D activities for product line A are performed in the Netherlands and have been transferred to a Dutch company (R&D NL). The European head office and the European sales activities have also been transferred to this Dutch company. R&D NL operates entirely independently, although strategic decisions are taken by the group's management.

Company Y is also a group member. Company Y is resident in country Y. Company Y has 2 employees, both with an administrative and financial background.

R&D NL and company Y have concluded an agreement for an indefinite period in respect of the R&D activities performed by R&D NL. Not all the research activities are equally successful. Under the contractual terms agreed on between company Y and R&D NL, all risks attached to the development undertaken by R&D NL are for the account and risk of company Y. Company Y will own all legal and economic rights resulting from the research. Company Y has sufficient equity to assume the financial risks associated with the research. The payment R&D NL receives from company Y is calculated on the basis of the cost-plus method.

Conclusion: The functions performed by R&D NL cover the entire range of R&D activities (from deciding which research to undertake to carrying out the research). Therefore, R&D NL independently manages the R&D activities. Under the contractual terms agreed, the risks related to the R&D activities are for the account of company Y. However, company Y does not have the necessary expertise to manage the risk. It is R&D NL that, in effect, manages the risk, so that the risk should also be allocated to R&D NL. Therefore, based on the actual situation, R&D NL does not carry out contract research. Consequently, using the cost-plus method to determine the payment R&D NL should receive will not lead to an arm’s length payment.

### 7. Contributions to a CCA (Cost contribution arrangement) (Chapter VII)

CCAs should be in line with the arm's length principle as outlined in the OECD Guidelines, in particular Chapter 8. On the basis of the arm's length principle, the payment must be related to the functions performed (taking into account the risks assumed and the assets employed). This means that the size of the payment received by the participants to a CCA must not effectively differ from the payment the particular businesses would have received had their collaboration not been subject to a CCA.

Chapter 8 of the OECD Guidelines states that each participant's proportionate share of the overall contributions to the CCA must be consistent with each participant's proportionate share of the overall expected benefits. In practice, this must be evaluated on a case-by-case basis. According to the Netherlands, the arm's length principle requires that each participant's share of the overall contributions to the CCA, as well as each participant's share of the overall expected benefits, must be determined on the basis of the fair market value. However, if it is plausible that the average proportionate value of the individual services contributed by the various participants to a CCA is roughly equal, it is permissible under the arm's length principle to use the cost price of the contributions to determine whether each participant's share of the overall expected benefits is proportionate to each participant's share of the contributions. Please refer to example P below. If the interested parties opt to allocate the expected benefits on the basis of the cost price of the contribution, they will need to substantiate this by providing proof that the average proportionate added value of each participant's contribution is the same.

Some countries will not accept a profit margin being charged, although they will accept a charge being made in respect of the equity needed to perform the activities. Both methods can have the same outcome. The choice as to which method to apply will be influenced by whether the charge would be acceptable in certain countries. For the purposes of Dutch taxation, the method chosen will be followed, provided the result is in accordance with the OECD Guidelines.

What follows are some examples of CCAs for R&D activities to clarify the above.[157]

**Examples**

*Example L*

Continent A houses the head office of company A, while continent B houses the head office of company B. Both companies manufacture and sell group products. Both have an R&D centre. The group decides to research the development of a new product. Market expectations for the product are good, but important research must be conducted before the product is ready for manufacture and sale. The product would do well in the markets on continents A and B.

Group companies A and B decide to conclude a Cost Contribution Arrangement in respect of the necessary research. A provides the research capacity and will make the first development results available, while B will provide the professional expertise, know-how, and researchers. A and B agree on a timeline indicating when they must jointly take decisions on the next stage of the project. There is a 1:1 ratio between the market value and the contributions from A and B. The overall expected value of the developed product is the same for both continents. A and B agree that each participant will bear their own costs. It was also agreed that A will hold the legal and economic ownership of the developed product as regards continent A and B will hold the legal and economic ownership of the

157. To avoid unnecessarily complicating matters, the examples do not take account of timing differences in respect of the individual contributions of the participants. Arm's length relationships would take account of such differences when determining the value of the contributions, in so far as significant, so that, in practice, attention must be paid to the determination of an arm's length payment if a CCA is concluded between associated parties.

developed product as regards continent B. The strategic project planning and management (including project monitoring and decision-making) is equally distributed.

Conclusion: The Cost Contribution Arrangement leads to an arm's length result. Both A and B can be regarded as a participant to the CCA because both participants receive a share of the rights to the developed product that corresponds to their contribution. Moreover, they can exploit or use this right as they see fit (para. 8.10 OECD Guidelines). Finally, the proportionate share of both participants in the contributions is the same as their proportionate share in the overall expected benefits (i.e. the right the participants receive).

*Example M*

Group company A is involved in the development, manufacture and sale of consumer products on continent A. Group company B carried out the initial research on the feasibility of developing a new product. The conclusion is that the development of the product will most likely be successful. Market expectations for the product are good. The product is also very well suited for the market on continents B and C. Group companies B and C are involved with the development, manufacture and sale of similar products for the markets on continents B and C.

Group companies A, B and C decide to conclude a Cost Contribution Arrangement for the research necessary to develop the new product. To ensure the development is successful, the following arrangements are made:

- Equal contributions by all: The preparation of a research programme and taking decisions as the project progresses in accordance with the stages identified in the research programme (strategic project planning and management of the project, including monitoring and decision-making).
- A's contribution: Results of the initial research. Developments costs incurred: EUR 1 million. Fair market value of the developed product: EUR 2 million.
- B's contribution: Development capacity (staff + fixed assets). The costs related to this development capacity are expected to be EUR 1.8 million. If this development capacity had been contracted from a third party on a contract research basis, it would have cost EUR 2 million (= fair market value).
- C's contribution: Liquidity of EUR 2 million for expected additional costs (purchase materials from third parties and contracting third parties).

The participants agree to carry the costs of their own contribution. The overall value of the developed product on continents A, B and C is expected to be the same, so that the value of the rights for all continents is also expected to be the same. The group companies agree that group companies A, B, and C will become the legal and economic owners of the developed product for continents A, B, and C respectively.

Conclusion: The Cost Contribution Arrangement leads to an arm's length result. A, B and C can be regarded as participants to the CCA because they will receive a share of the rights to the developed product that corresponds to their contribution. Moreover, they can exploit or use this right as they see fit (para. 8.10 OECD Guidelines). Finally, the participants' proportionate share of the contributions is the same as their proportionate share in the overall expected benefits (i.e. the right the participants receive).

*Example N*

Group company A, group company B and group company C are involved with the manufacture and sale of similar consumer products on continents A, B and C respectively. Group company A has an R&D centre. Group companies B and C employ a number of product specialists who also have knowledge of product development, but neither company has their own R&C centre. Group company A conducted the initial research on the development of a new product. Market expectations for the product on continents B and C are good, but important research must be conducted before the product is ready for manufacture and sale. The overall expected value of the developed product on continents B and C is expected to be the same. There does not appear to be a market for the product on continent A.

Group companies A, B and C decide to conclude a Cost Contribution Arrangement under the following terms:

- B and C will jointly prepare and equally contribute to a research programme for the development and follow-up development of the product. Each company will make the same capacity available for the management of the project (strategic project planning and management, including control and decision-making).
- A's contribution: Results of the initial research. Development costs incurred: EUR 1 million. Fair market value of the developed product: EUR 2 million.
- A's contribution: Development capacity (staff + fixed assets): A's R&D department works out the project plan, presents it to B and C and carries out the research. It provides regular progress reports to B and C. The costs related to this development capacity are expected to be EUR 1.8 million. The fair market value of the development capacity if contracted out is: EUR 2 million.
- B and C's contribution: Each pays A EUR 2 million as payment for the contribution made by A. In addition, B and C will each pay half of the additional costs paid to third parties (purchase of materials, contracting third parties) amounting to EUR 2 million.
- The participants will each pay the costs of their own contribution.
- B and C will hold the legal and economic ownership of the developed product on continents B and C respectively.

Conclusion: A is not a participant to the Cost Contribution Arrangement because there are no benefits to be gained for it from the developed product (*see* para. 8.10 OECD Guidelines). A, in effect, sells the product prototype to B and C and also performs contract research activities for B and C. B and C can both be regarded as participants to the CCA because they will receive a share of the rights to the developed product proportionate to their contribution (funds and management) and can exploit or use this right as they see fit (*see* para. 8.10 OECD Guidelines). The total fair market value of the development capacity and the product prototype made available by A is EUR 4 million. In exchange, A receives a monetary payment of EUR 4 million. Such a payment is at arm's length. The contribution of both the participants to the CCA (B and C) and the expected benefit (the rights acquired) are the same. Although the contract cannot be regarded as a CCA in respect of A, the contractual payment all participants receive is at arm's length.

*Example O*

Group company A is involved with the development, manufacture and sale of consumer products. Group company B employs two staff with a financial and administrative background. Group company A conducted the initial research on the development of a new product. Market expectations for the product are good on continents A and B, but important research must be conducted before the product is ready for manufacture and sale. The overall expected value of the developed product on continents A and B is expected to be the same. Group companies A and B decide to conclude a Cost Contribution Arrangement under the following terms:

- A's contribution: The product prototype and development capacity. Total costs: EUR 5 million. Total fair market value: EUR 10 million.
- B pays A EUR 5 million and 50% of the costs to the extent they exceed the projected EUR 5 million.
- A and B will hold the economic ownership to the developed product for continents A and B respectively.
- A will hold the legal ownership.

Further to the contract, it appears that A completely manages the project (including control and decision-making).

Conclusion: The functions performed by A cover the entire range of R&D activities (from deciding which research to undertake up to carrying out the research). A manages the R&D activity entirely independently. Under the terms of the contract, B will assume 50% of the risks attached to this R&D activity (B pays A EUR 5 million and 50% of the costs to the extent they exceed the projected costs and holds the economic ownership to the rights). However, B does not have the necessary functional expertise to manage its share of the risk associated with the R&D activity. The entire risk is in fact assumed by A, so that the entire risk should also be allocated to A.

The payment A receives must be in line with the functions it performs and the associated risks. On the basis of the payment agreed on with B, A wrongly only receives payment for its development activities in so far as they do not relate to the management of the project and the associated risk. This means that the conditions of the contract concluded by A and B are not at arm's length.

*Example P*

Group company A and group company B are involved with the development, manufacture and sale of similar consumer products on continents A and B respectively. A and B decide to jointly develop a new product. The research departments are similar, i.e. the quality of the departments (know-how and experience) and their cost structures are similar. The ratio of costs to contributions during all the development stages is equal. The expected value of the developed product on continent A and continent B respectively is also equal. A and B decide to conclude a Cost Contribution Arrangement under the following terms:

- A and B will jointly prepare and equally contribute to a research programme for the development and follow-up development of the product. Each company will make the same capacity available for the management of the project (strategic project planning and management, including control and decision-making).
- The participants will each pay the costs of their own contribution.
- A and B will hold the legal and economic ownership of the developed product on continents A and B respectively.

Conclusion: A and B can be regarded as participants to the CCA because they receive a share of the rights to the developed product that corresponds to their contribution. Moreover, they can exploit or use this right as they see fit (para. 8.10 OECD Guidelines).

Furthermore, the participants have convincingly demonstrated that the average relative added value of the services contributed are similar. A and B can use the cost price of their contributions when determining the ratio of their contributions to the overall expected benefits.

If the average relative added value of the services contributed by A and B had not been similar, for example, due to significant differences in the know-how and experience of their employees, then the cost price of the contributions cannot be used to determine the ratio of contributions to the overall expected benefits; instead, the fair market value of the contributions must be used.

The above examples are based on a stylized version of reality. In practice, it will be difficult to determine the exact fair market value of the contributions made by the participants to the CCA and the exact fair market value of the benefits derived from the CCA. With regard to whether the proportional allocation of the overall expected benefits derived from the CCA should be based on the costs related to the participants contributions, rather than the fair market value of these contributions, it will in practice also be difficult to establish whether the average relative added value of the contributions made by both participants are similar. In particular, when assessing CCAs the Dutch Tax and Customs Administration must take into account the fact that transfer pricing is not an exact science. This is regardless of the fact that taxpayers should be expected to convincingly demonstrate that independent parties in comparable circumstances would enter into a comparable agreement.

**8. Tangible/intangible fixed assets**

The criteria of the arm's length principle are not met if tangible/intangible fixed assets are transferred to a group company, while that group company does not add value to the particular assets because the necessary functionality is absent and therefore is not able to manage the risks associated with the tangible/intangible assets.

On the basis of the arm's length principle, it is assumed that associated enterprises aim to maximize their profits. A transaction involving tangible/intangible assets will generally only be entered into by unassociated parties if both parties can expect an increase in their own profit as a result thereof. For vendors and purchasers, this expectation can only become fact if this involves an expected increase in the joint profit. The expected increase in profit can only be achieved if the vendor, by whichever means possible, adds value. This is only possible if the vendor has the necessary functionality to be able to manage the relevant risks (the relevant functionality). If there is no expected increase in the joint profit, the offer made by a potential purchaser will be lower than the vendor's asking price. In that case, the transfer of the asset is not commercially viable and will not be effected partly due to the fact that there are transaction costs connected to the transfer. Therefore, such a transaction between associated enterprises does not meet the criteria of the arm's length principle.

Moreover, an arm's length assessment carried out from the perspective of both the vendor and purchaser must take note of whether there are other realistic and more attractive opportunities available to the vendor and/or purchaser. In the situation described above, it would not be realistic for the vendor and purchaser to enter into the transaction. After all, the overall operating profit jointly achieved by both parties is not higher than would be the case if the transfer had not taken place. Because the transfer involves additional costs (for example, for drafting the contracts) the joint operating result is expected to be lower than if the transfer had not taken place.

It is sometimes the case that the purchaser of a tangible/an intangible fixed asset is resident in a low-taxing jurisdiction. The sole fact that the purchaser is resident in a low-taxing jurisdiction will not lead to an increase in the joint profit if the purchaser does not have the relevant functionality. In situations where the functionality is retained by the vendor after the transfer, the purchaser will be completely dependent on the vendor for any growth in value and exploitation of the asset. Under arm's length conditions, the purchaser cannot expect any operating profit. Therefore, arm's length conditions will not allow it to profit from the low/lower tax rate.

Pursuant to the arm's length principle of Section 8b CITA, the disadvantages resulting from applying conditions that deviate from those applied by unassociated parties must be eliminated from the taxable profit of the Dutch vendor. This disadvantage is the difference in profit when compared to not transferring the asset.

The analysis of such cases is in line with example B "transfer of valuable intangibles to a shell company" of paragraph 9.190 et seq. of the OECD Guidelines.

In some situations, group companies hold the legal ownership of tangible/intangible fixed assets without these assets having been transferred to them in advance by other group companies. Where, in such situations, the legal owner does not have the relevant functionality, the Dutch Tax and Customs Administration will deal with these situations in accordance with the basic assumptions outlined in this paragraph. This will limit the remuneration received by the legal owner of the tangible/intangible fixed assets that does not perform the relevant functions in respect of the asset.

**9. Central purchasing within the group**

Paragraphs 9.154 through 9.160 of the OECD Guidelines provide an example of the implementation of a central purchasing function within a group. Commercial arguments in favour of centralizing purchasing activities are, for example, cost savings (integrating purchasing power and/or purchasing expertise), reducing operating capital and improving product quality. The intention is often also to locate the purchasing office close to the market that supplies the products.

The activities associated with purchasing can vary from performing support activities to performing purchasing activities that are part of the key functions of the group. Central to the functional analysis is the relative importance of the purchasing function within the overall value chain of the group. The next step is to determine which group members perform the various purchasing activities. Finally, the activities performed by the purchasing office can be analysed.

Few risks will be assumed if the activities performed by the purchasing office are routine. Such activities include:

- selecting potential suppliers;
- liaising locally with suppliers;
- carrying out quality control on the purchases; and
- providing transport and other logistics activities.

In practice, it appears that almost no price or inventory risks are run if such activities are performed by the purchasing office.

Sometimes the activities are more complex and the purchasing office is also involved with, for example, compiling the product range (which should be regarded as a separate function).

After the functional analysis has been carried out, an appropriate transfer pricing method must be selected to determine the arm's length remuneration for the activities performed by the purchasing office. This remuneration can vary from a routine payment (based on the own operating costs incurred or a fee based on the cost of the purchases) for the purchasing office performing routine tasks, to a profit split type of payment if the activities are regarded as a key function of the business.

It is generally accepted that the activities performed by local unassociated purchasing agents mostly consist of support activities. Their remuneration is generally based on the cost of the purchases. It is obvious that the payment percentage will increase as the responsibilities of the agent increase and will decrease as the purchasing volumes increase. In practice, it appears difficult to find reliable comparables that can be used to carry out a comparison based on a percentage of the cost of the purchases. In such situations, the Dutch Tax and Customs Administration will therefore generally apply a cost-plus method as test to assess the arm's length nature of the remuneration. This will, in principle, limit the cost base to the purchasing office's own operating costs, given the routine tasks performed by the purchasing office; the cost price of the purchases is not included.

If, as a result of the centralization of the purchasing activities, the group obtains higher discounts than was previously the case due to an increase in purchasing volume, this additional benefit is, in principle, not attributable to the purchasing office. This benefit should be attributed to those group members whose joint purchasing volumes make it possible for the purchasing office to obtain such (additional) discounts. Attributing part of the discounts obtained to the purchasing office will be regarded as at arm's length only if and to the extent that the (additional) discounts obtained are due to specific know-how and expertise, such as that available at the purchasing office. I refer to the Supreme Court judgment dated 23 April 2004, no. 39 542.

**10. Guarantees for loan agreements**

There are various reasons for providing guarantees to group companies for loans granted in associated relationships. These guarantees should be assessed in accordance with the arm's length principle if they involve a group service.

The reasons that associated companies provide a guarantee to lenders include:

- the lender will not grant, or only grant minimal, financing if no guarantee is provided;
- the lender is prepared to grant the group company a loan, but under less favourable conditions than would apply had a guarantee been provided; and
- the lender wants to avoid the situation whereby the group company that has been granted the loan becomes financially less sound due to transactions carried out by the parent company.

If the group company is not able to independently − without a guarantee from associated companies − raise a loan on the capital market, the guarantee will, in principle, be provided in a shareholder capacity. This does not involve a chargeable group service. As such, the loan will no longer be a loan from a third party, but a loan from an associated guarantor.

If the lender calls in the guarantee from the guarantor, any write-down of the receivable from the associated group company by the guarantor will also be made in a shareholder capacity.

If the group company can be regarded as being able to independently raise a loan, then the extent to which it can demand, without an explicit guarantee from an associated company, conditions that are more favourable than a comparable independent company could demand, solely due to the fact that it is part of a group, must be evaluated. The more favourable loan conditions are obtained on the basis of an implicit guarantee. This implicit guarantee is based on the fact that the capital market assumes that the group will enable the particular group company to meet its obligations. If and in so far this is the case, it does not involve a chargeable group service (*see* para. 7.13 OECD Guidelines).

In all other cases where more favourable loan conditions are obtained due to the explicit guarantee of an associated company, and for which an independent third party would be willing to pay, a chargeable group service is present (the charge being the guarantee fee).

Important factors in determining the size of the guarantee fee are both the creditworthiness of the particular group company and the creditworthiness of the group as a whole.

The credit rating that companies forming part of a group receive from ratings agencies is, in principle, not only based on the relevant indicators of the independent company as such, but also on the relevant indicators of the group to which they belong and on their position within the group. This credit rating will hereinafter be referred to as a derived rating. There is a distinction between this derived rating and the stand-alone rating that the particular company would have had, had it not been part of the group. In the absence of an explicit guarantee, the capital market is willing to lend to the group company on the basis of the derived rating.

The capital market will want to make the interest rate dependent on the particular rating. In short, the following example sets out the difference between the interest rates charged:

- on the basis of the stand-alone rating: 6%;
- on the basis of the derived rating: between 4 and 6%;
- on the basis of the group rating: 4%.

In my opinion, if the guarantee involves a service, for tax purposes the fee charged (the guarantee fee) cannot, in principle, be higher than the difference between the interest rate based on the derived rating and the interest rate based on the group rating. That is the maximum benefit that the group company can realize from the explicit guarantee.

The derived rating will lie between the stand-alone rating of the group company and the group rating. The derived rating, and thereby the amount of the guarantee fee, will, in particular, depend on the degree to which the group company is of strategic interest for the group as a whole.

If this strategic interest is so important that any default by the group company in meeting its capital market obligations would lead to high costs for the group due to, for example, a lower group rating or damage to its reputation, then the derived rating will move toward the group rating. The interest rate that such a strategically important group company would independently be able to demand without an explicit guarantee lies in the region of the interest rate based on the group rating. If the group company is of only minor strategic interest to the group as a whole, then the derived rating will move towards to the interest rate based on the stand-alone rating of the group company.

The above is in line with the Supreme Court judgment rendered on 1 March 2013, no. 11/01985, in which the Court concluded that in the case of a guarantee provided under an umbrella credit facility, the acceptance by a company of joint and several liability for all the debts of the other company participating in the credit facility results from the corporate relationship between that company and the other companies. In that case, the companies' actions are governed by the group interest and they are therefore prepared to accept a liability that is higher than the liability arising from independently raising debt financing. A comparable joint and several liability will not often be encountered between unassociated parties and, furthermore, it will not be possible to determine an arm's length remuneration for the guarantees provided among the different associated parties.

**11. Internal insurance/reinsurance activities**

Within the group, there are group companies that formally act as the internal insurer/reinsurer. However, in some cases, these companies lack the activities that are characteristic of a professional insurer/reinsurer, such as product development, marketing and sales, screening of potential policyholders, asset/liability management and developing an independent reinsurance policy.

In addition, these companies do not "actively" diversify, i.e. outside the group, the risks run by the reinsurer in respect of the internal insurance/reinsurance activities; any diversification that takes place is "passive", i.e. within the group. I would like to explain in more detail two forms of insurance/reinsurance activities performed within a group.

In the case of "passive poolers", the group members effectively pool their risks with the internal insurer/reinsurer, without the internal insurer/reinsurer performing the activities typical of a professional reinsurer.

In those cases where insurance is offered as a by-product, the transfer of the insurance income realized to the internal insurer/reinsurer is not at arm's length.

In the cases described above, the internal insurer/reinsurer should only receive a limited remuneration, which takes account of its almost exclusive intermediary function.

*Passive poolers*

A passive pooler only insures group risks. This is mostly the own risk the group is prepared to assume or which is demanded by external insurers. As a rule, the passive pooler is an extension of the head office's Risk Management Department. It must insure all the members of the group and is generally prohibited from insuring the risks assumed by external parties. As such, it does not perform typical insurance activities and does not diversify outside the group. The passive pooler primarily performs an administrative and/or intermediary function, which only justifies a limited remuneration. The other benefits that this company gives rise to, such as the pooling benefit of being able to reduce the joint amount of equity cover, the benefits arising from having centralized negotiations with potential insurers/reinsurers and the benefits arising from the investment income the internal insurer/reinsurer earns with the premium income, belong to the group members who pool their resources in this way. This can be compared to a purchasing office for the group which performs routine purchasing activities (*see* para. 9 of this Decree).

*Insurance as by-product*

This refers to situations where the insurance is offered to customers (unassociated customers) by a group operating outside the insurance sector as a by-product of its products or services. For example, travel cancellation insurance or extended warranty insurance. In general, the customer's policy is provided in the name of a third (unassociated) insurer that falls under the oversight of the local supervisory authority. The premium is passed on to the internal reinsurer as a reinsurance premium after deduction of a fee for the third (unassociated) insurer. In practice, it is not the internal reinsurer that offers the insurance as a by-product, but the group member performing the main activity of the group. The group member uses its customer base to diversify; by doing so it knows how to realize insurance benefits for the group. The internal reinsurer does not, in effect, perform an insurance function and therefore, according to the arm's length principle, should not bear any insurance risk. Such a company only has a limited administrative function that justifies a limited remuneration.[158]

### 12. Financing transactions

a. The OECD Guidelines

According to the OECD Guidelines, the arm's length test for financing transactions comprises the following. Firstly, the conditions (including the price) under which the transaction was entered into are evaluated to see whether they are the same as the conditions that unassociated third parties would have agreed on for a comparable transaction entered into under comparable circumstances. If this is not the case, then the consequences must be adjusted (para. 1.6 OECD Guidelines). Where possible, it is preferable to do this by way of a price adjustment (interest). If it is not possible to make the loan arm's length by way of a price adjustment, then it should be considered whether changing the other conditions of the loan would make it an arm's length loan. This usually concerns a risk allocation not found between independent parties under comparable conditions. For example, mistakenly not demanding certain guarantees in respect of the repayment of the loan. If neither a price adjustment nor changes to the other conditions would make the transaction at arm's length, this can, in exceptional cases, result in disregarding/requalifying the loan, or a part thereof (para. 1.65 OECD Guidelines). By taking the above into account, an arm's length interest/interest expense can subsequently be determined for the remaining loan. The perspective of each of the parties involved is an important factor in the arm's length test.

b. The bilateral perspective

The unassociated lender wishes to limit its risks as much as possible, taking into account its functionality in the market and the related choices regarding the acceptance of risks. As a rule, its decision to grant a loan will be dependent on whether the unassociated borrower will be able to repay the loan with interest. It will therefore be more willing to grant a loan to an unassociated party whose creditworthiness, after the financial transaction has been entered into, does not fall below a certain level. Creditworthiness is usually expressed in a credit rating. Credit ratings falling between AAA to BBB-[159] reflect excellent to adequate creditworthiness; there is only a slight chance that an unassociated borrower will ultimately not be able to repay the loan with interest. In that case, the borrower is referred to as an "investment grade" borrower. Potential borrowers with a credit rating lower than BBB- are not regarded as investment grade borrowers because there is a very real chance that they will ultimately not be able to repay the loan with interest. The rating is determined on the basis of certain indicators, including interest cover[160]

158. Cf.: District Court, The Hague, 11 July 2011, AWB08/9105, LJN BR4966.
159. Standards & Poor ratings, Moody's uses, for example, Aaa to Bbb.
160. Operating profit divided by interest expense.

and the debt-to-equity ratio. Only in special situations is an unassociated lender prepared to accept a borrower with a credit rating lower than BBB-. An unassociated lender with a diversified loan portfolio will be more willing to grant a loan to such a company than an unassociated lender that only has one or a very limited number of outstanding loans. Based on the above, an associated lender that grants a loan to a borrowing group company with a poor credit rating (after the loan the credit rating is < BBB-) must convincingly demonstrate that the loan was entered into under arm's length conditions.

The unassociated borrower will strive to ensure that the financing of its business activities takes place as efficiently as possible, so that the cost of capital is kept as low as possible.[161] The debt-to-equity ratio is an important factor in the cost of capital and whether this cost will be significant or slight. On the one hand, it is advantageous to finance a certain part of the business activities with debt. One of the reasons being that because the interest payment is, in principle, tax deductible, this will increase the return on the invested capital. On the other hand, the additional costs connected with raising debt financing above a certain amount are so high that this negatively impacts the cost of capital and decreases the return on the invested capital.

The amount of the costs of borrowed capital is largely dependent on the creditworthiness of the borrower. An unassociated borrower will generally not enter into a loan transaction which would see its credit rating fall under investment grade/BBB-. Such a credit rating makes raising debt financing either impossible or makes the cost of financing this debt excessive. In addition, there would be no buffer to deal with calamities and a very high risk of bankruptcy.

In light of the above, in those cases where an associated financing transaction results in a debt-to-equity ratio and interest expenses that, after the financing transaction has been entered into, result in a poor credit rating for the borrowing group company (a rating < BBB-), that company will have to convincingly demonstrate that the loan was agreed on under arm's length conditions.

c. Dutch case law

On 25 November 2011, the Supreme Court rendered judgment in a case (no. 08/05323) concerning an associated loan. At issue was whether such a loan could be written down in domestic situations. According to the Supreme Court, if the interest on a loan between associated parties is not determined in accordance with the arm's length principle, the calculation of the profit for tax purposes must nevertheless be based on interest that is at arm's length. The basic assumption for the determination of that interest has been described above.

The Supreme Court further concluded that should the required adjustment result in a profit-sharing payment, this would undermine that agreed on by the parties. According to the Supreme Court, if it is not possible to agree on an interest rate that an independent third party would be willing to accept if it were to grant a similar loan to the borrowing group company under the same conditions and in the same circumstances, then the lending group company assumes a bad debt risk on its loan that a third party would not have accepted. In that case − special circumstances excepted − it must be assumed that the lending group company accepted this risk with the objective of serving the interests of the associated company in a shareholder or sister/subsidiary capacity. The Supreme Court regards this as a non-business motivated loan. Any write-down loss on such a loan cannot be deducted from the lender's taxable profit.

161. The professional literature also refers to this as the weighted cost of capital (Wacc).

An arm’s length interest must subsequently be determined for the non-business motivated loan. The Supreme Court has developed a rule of thumb for this. The interest rate on a non-business motivated loan should be set at the interest rate that the borrowing group company would have had to pay had it borrowed from a third party under the same conditions and in the same circumstances and with the lending company acting as guarantor. In that case, the interest would be deductible at the borrowing group company and taxable at the lending group company. The difference between the interest actually charged and the interest rate decided on based on the credit rating of the lending group company is attributable to the capital account.

The assessment of the loan − whether or not it is at arm’s length − can take place at the time it is granted or during the term of the loan. This assessment must be made from the perspective of the lending and borrowing parties. With reference to that stated above in respect of the perspective of the parties involved, the approach adopted by the Supreme Court in the above judgment also requires an associated lender that grants a loan to a borrowing group company with a poor credit rating (after the loan has been entered into the rating is < BBB-) to prove that this does not involve a “non-business motivated loan”. In my view, this also applies to the borrower that sees its credit rating fall below BBB- as a result of the associated financing transaction.

According to the Supreme Court, the amount of interest on a “non-business motivated loan” − a loan with a non-arm’s length bad debt risk − must be determined on the basis of the credit rating of the lending group company. However, in its judgment the Court did not explain how to deal with the relationship between the credit rating of the lending group company and the credit rating of the borrowing company.

If the lender’s credit rating is higher than that of the borrower, then the interest that would be charged to the lending group company will be regarded as the appropriate arm’s length interest.

The deemed guarantee will have no impact where the credit rating of the lending group company is no different from that of the borrowing group company. In that case, I consider that only the risk-free interest on the loan should be taken into account.

The end result should be interest income/an interest expense that meets the arm's length conditions of Section 8b CITA.

**13. Subsidies, tax incentives and limited deductible costs**

A question that regularly arises in practice regarding, in particular, situations in which a cost-related payment is used to determine the arm’s length price, is whether subsidies and tax benefits can be deducted from the cost base. With regard to the Dutch situation, the basic assumption is that subsidies can be deducted from the cost base if there is a direct relationship between the subsidy and the supply of the product or service and the particular benefit given in the form of a cost discount or a cost allowance. For example, a subsidy for the use of more expensive but environmentally friendly raw materials, a cash-back payment for the purchase of energy-efficient business assets, but also a contribution pursuant to the regional investment aid scheme (*investeringspremieregeling*; IPR). In contrast, additional taxes, for example, on the use of raw materials that are hazardous to the environment, will increase the cost base. The remittance reductions referred to in Section 3 of the Wages and Salaries Tax and National Insurance Contributions Reduced Remittances Act reduce payroll costs and lower the cost base for the calculation of the profit margin.

Subsidies and tax benefits allocated to the entity that have no direct causal relationship with the cost-plus activities cannot be deducted from the tax base. To the extent that they form part of the taxable profit, they are separately recorded in the income statement.

If the tax relief involves deductions to the taxable profit, such as, for example, the investment deduction, they will not be able to be deducted from the tax base. This requires that the profit must first be calculated on the basis of the cost-plus method, after which the relief is separately deducted from the taxable profit.

Tax law has limited the deductibility of certain cost categories, for example the costs referred to in Section 3.14 Personal Income Tax Act 2001, the cost of depreciating buildings as referred to in Section 3.30a Personal Income Tax Act 2001 and the costs referred to in Section 10(1)(j) CITA. The costs do form part of the tax base for the calculation of the cost-plus markup. The cost deduction limitation is realized by adding the non-deductible part of the costs to the profit when determining the taxable profit.

### 14. The documentation obligation

Section 8b(3) CITA contains the transfer pricing documentation obligation. The documentation must consist of a description of the five comparability factors of associated transactions listed in Chapter I of the OECD Guidelines, a substantiation of the transfer pricing method applied and a substantiation of the conditions, including the price, under which the transaction was entered into. When codifying the documentation obligation, a conscious choice was made not to include an exhaustive list of documents to substantiate the arm's length nature of the transactions. To that extent, one could speak of an "open standard".

The principle of proportionality is an important factor in evaluating the extent to which the documentation is adequate. The basic assumption is that the additional administrative costs arising from Section 8b(3) CITA must be kept to a minimum.

I realize that the open standard can give rise to uncertainty by taxpayers regarding whether the Dutch Tax and Customs Administration will regard the available documentation as adequate. The competent tax inspector may therefore be requested to provide certainty on the whether the documentation obligation of Section 8b(3) CITA (*see also* the Decree of 11 August 2004, no. DGB2004/1339M) has been met.

On 27 June 2006, the Council of the European Union approved the Code of Conduct on transfer pricing documentation for associated enterprises in the European Union (EU TPD).[162]

One of the reasons underlying such a code of conduct was the wish to introduce a uniform documentation obligation for the European Union. As this is also in line with the basic assumptions held by the Netherlands with regard to the documentation obligation, taxpayers have the option of applying the EU Transfer Pricing Documentation Code of Conduct in order to meet their documentation obligation. The application of the principle of proportionality as described above also applies to the EU Transfer Pricing Documentation Code of Conduct, in so far as this relates to documentation in respect of the Dutch tax conditions listed in Section 8b(3) CITA.

### 15. Early consultation on possible double taxation

162. Resolution of the Council and of the representatives of the governments of the Member States, meeting within the Council, of 27 June 2006 on a code of conduct on transfer pricing documentation for associated enterprises in the European Union (EU TPD), (2006/C 176/01).

Double taxation resulting from transfer pricing adjustments is to be avoided. Tax treaties and the EU Arbitration Convention provide for assistance to be given to taxpayers who are being taxed in violation of the provision of a treaty. This assistance is provided by the Directorate for International Fiscal Affairs of the Ministry of Finance, which is the competent authority in such matters. The basis assumption is that double taxation must be eliminated as quickly and efficiently as possible. It is the intention of the Netherlands to have negotiations with treaty partners start as early as possible. This has been set out in more detail in the Decree of 29 September 2008, no. IFZ2008/ 248M, *Government Gazette* (Staatscourant) no. 188.

We know from experience that in a number of cases eliminating double taxation is simply a matter of exchanging the facts and circumstances of the particular case during the negotiation process. In those cases where a taxpayer expects to be faced with double taxation arising from transfer pricing and resulting from the position taken by the tax authorities in a country with which the Netherlands can exchange information, the Dutch Tax and Customs Administration is prepared to use the exchange of information or joint audits as ways to avoid double taxation at the earliest possible stage. A taxpayer can file such a request with the Dutch tax inspector.

There must be a realistic chance that the position taken by the foreign tax authorities will lead to a transfer pricing adjustment; this must be substantiated in the taxpayer's request. Whether exchanging information or conducting joint audits will be successful in avoiding any double taxation will depend on legal considerations and the willingness of other countries to participate.

**16. Effective date**

This Decree will take effect the day after the publication date of the Government Gazette (Staatscourant) in which it is published.

**17. Withdrawal old Decrees**

This Decree replaces the Decrees of the Deputy Minister of Finance dated 30 March 2001, no. IFZ 2001/295M and 21 August 2004, no. IFZ 2004/680M.

This Decree will be published in the Government Gazette (Staatscourant).

The Hague, 14 November 2013

Deputy Minister of Finance

F.H.H. Weekers

**2. Unofficial translation of FSC Decrees**

**Service Entities and advance certainty. Entities with financial service activities within a group of companies without real economic presence in the Netherlands; no advance certainty, providing of information and limitation of a crediting withholding tax.**

*Decree DGB 2014/ 3101*

*Directorate-General for the tax authorities, Cluster taxation*

The State Secretary of Finance has decided as follows:

This decree replaces the decree of 11 August 2004, IFZ2004/126M. This decree updates the preceding decree.

**Entities providing intra-group financial services**

For the application of this decree the following definitions apply:

- *Entities providing intra-group financial services (hereinafter referred to as:* service entities) resident taxpayers as referred to in Article 3a, paragraph 1, of the regulations of the International Assistance for the Levying of Taxes Act;
- *A group of companies*: the taxpayer together with affiliated entities, as referred to in Article 10a, paragraph 4 in conjunction with paragraph 6 of the Corporate Income Tax Act 1969 ("*CITA 1969*"), and related natural persons, as referred to in Article 10a, paragraph 5 of the CITA 1969.

**No advance certainty**

The providing of advance certainty on the tax implications of the contemplated transactions by the service entity is to be construed that advance certainty is solely to be furnished on the application of the present decree in combination with the at arm's length remuneration for the activities of the service entity. For advance certainty on the at arm's length remuneration or the method of determining such remuneration, reference is made to decree DGB 2014/ 3098.

A service entity is not granted advance certainty on the tax implications of all contemplated transactions if:

a. the service entity does not meet one or more conditions with regard to substance in the Netherlands as mentioned in the attachment to this decree; or

b. the functions performed by the service entity with regard to these transactions, on balance, do not involve real risks (*see* paragraph 6 below).

**Provision of information**

In case of advance certainty in the form of an APA, information concerning this APA will be spontaneously exchanged with the tax authorities of the country or countries involved if the group of companies to which the service entity belongs does not engage in more activities in the Netherlands than those as specified in the attachment to this decree and if there are no minimum substance requirements for substance in the Netherlands or if there are no concrete plans to expand the substance in the Netherlands.

Part of the advance tax ruling is the statement of the taxpayer that he will not rely on one of the clauses in article 14, paragraph 2, sub e, of the International Assistance for the Levying of Taxes Act, in respect of the levying of taxes (commercial, industrial or professional confidentiality) regarding the information included in the advance tax ruling. Possible disputes between the tax authorities and the applicant regarding this matter will be prevented this way.

**Credit of foreign withholding tax**

With regard to transactions as mentioned in paragraph 2, sub b, no credit of foreign withholding tax shall be granted because the financial service entity in fact acts as an intermediary and the received flows of money as a consequence thereof do not belong to the Dutch corporate tax base of that entity.

### Good faith owed towards treaty partners

In the cases mentioned in paragraph 2, sub a and b, no advance certainty is provided because the therein mentioned elements indicate that advance certainty will be in conflict with good faith which is owed towards treaty partners. Besides the elements specifically described in subparagraphs a and b, requests for the provision of advance certainty should be assessed more generally on the basis of the tax administrative decree [*Besluit Fiscaal Bestuursrecht*].

### Running of real risks

The risks that could follow from the transactions mainly consist of credit risks (bad debt and currency risks), market risks and operational risks. Solely running operational risks shall generally not lead to presence of real risks within the meaning of this decree. The extent to which a service entity runs risk is reflected, in particular, in the possibility that the service entity could be affected in its equity held over its assets. Therefore, decisive for the answer to the question whether and to what extent the service entity runs real risks is whether and to what extent the service entity runs one or more of the aforementioned risks and if the service entity holds sufficient equity to bear these risks.

A service entity whose activities consist of the receiving and paying of interest is deemed to run real risks if the equity required to bear the risks is at least equal to 1% of the loan amount or an amount of EUR 2 million. If therefore an equity is held of 1% of the loan amount, or EUR 2 million if that is a lower amount, the service entity is deemed to run real risks, provided that an applicant demonstrates that the realistic possibility exists that this equity would be affected, in case the risks connected to the transactions should manifest themselves.

*Example 1*

The sole activity of a service entity consists of the provision of a loan amounting to EUR 100 million to related party X. The equity of the service entity amounts to EUR 1.5 million. In addition, the service entity has borrowed an amount of EUR 98.5 million from related party Y to finance the loan. Service entity's parent company (M) has issued a guarantee that the entire debt to Y will be repaid by it should the service entity not fulfil its payment obligations. If the credit risk (bad debt risk) should manifest itself (X cannot fulfil its payment obligations), service entity's equity would be affected at first. Only to the extent that service entity's equity is not sufficient to fulfil its payment obligations, the guarantee given by M will be invoked. As the service entity holds an equity in excess of 1% of the loan amount and besides the realistic possibility exists that the equity will be affected if the risks manifest themselves (in this case bad debt risk), the service entity runs real risks.

*Example 2*

The sole activity of a service entity consists of the provision of a loan amounting to EUR 400 million to related party X. The equity of the service entity amounts to EUR 3 million. In addition, the service entity has borrowed an amount of EUR 397 million from related party Y to finance the loan. Service entity's parent company (M) has issued a guarantee that the entire debt of X will be repaid by it should X not fulfil its payment obligations. If the bad debt risk that the service entity runs towards X should manifest itself (X cannot fulfil its payment obligations), the service entity could rely on M for the repayment of the debt. Although the service entity holds an equity in excess of EUR 2 million, no realistic possibility is present that this equity will be affected should X not fulfil its payment obligations. Therefore, the service entity does not run real risks.

The amount of EUR 2 million applies per company. If a company provides multiple loans, a pro rata part should be held with regard to each of the loans. Per loan an equity equal to the lower of the following amounts should be held:

a. 1% of the (separate) loan, or

b. a pro rata part of EUR 2 million with respect to the total amount of loans.

This is explained with the example below.

*Example 3*

The sole activity of a service entity consists of the provision of two loans: a loan amounting to EUR 200 million (loan 1) and a loan amounting to EUR 300 million (loan 2). The service entity's equity amounts to EUR 2 million. The risk with regard to loan 1 is limited to EUR 500,000, due to a guarantee issued by its parent company (M). As the risk with regard to loan 1 is limited to EUR 500,000, while this risk should at least be equal to the lower amount of (a) 1% of EUR 200 million or EUR 2 million and (b) 200/500 x 2 million or EUR 800.000, insufficient equity is held with respect to loan 1. Therefore, the service entity does not run real risk with respect to loan 1.

**Competence**

For information on the competence with regard to service entities within the meaning of this decree, reference is made to decree DGB2014/296M.

**Entry into force**

This decree enters into force the day after the date of issuance of the Government Gazette in which it is published.

**Withdrawal of the old decrees**

This decree replaces the decree of 11 August 2004, IFZ2004/ 126M, which hereby will be withdrawn.

The state secretary of Finance,

on his behalf,

T.W.M. Poolen,

Member of the management team of the tax authorities

**Attachment**

*List of minimum requirements as mentioned in paragraph 2, sub a, of this decree*

- At least half of the total number of statutory board members and board members with power of decision resides or is actually established in the Netherlands.
- Board members residing or established in the Netherlands have the required professional knowledge to properly perform their duties. The duties include at least the decision-making on transactions to be entered into by the entity – on the basis of the own responsibility of the entity and within the ordinary course of the group involvement – and ensure a proper handling of the transactions entered into.

- The entity has qualified employees for proper implementation and registration of the transactions to be entered into by the entity.
- The management decisions are taken in the Netherlands.
- The most important bank accounts of the legal entity are held in the Netherlands.
- The bookkeeping is performed in the Netherlands.
- The entity has – in any case until the moment of assessment – filed all tax returns properly. This could include corporate income tax, wage tax, value added tax and so forth.
- The business address of the entity is in the Netherlands. The entity is – to the best of the company's knowledge – not considered a resident for tax purposes in another country.
- The legal entity has an appropriate equity with regard to the functions performed by the legal entity (taking account of the assets used and the risks run).

For the interpretation of these requirements, chapter III of decree DGB 2014/ 3102 equally applies.

**3. Unofficial translation of FSC Decrees**

**Question and answer decree Service Entities. Questions and answers regarding the decree Service Entities and advance certainty (DGB 2014/3101), and the decree Treatment of requests on advance certainty in the form of an Advance Tax Ruling (ATR) (DGB 2014/3099).**

*Decree DGB 2014/3102*

*Directorate-General of the tax authorities, cluster taxation*

The State Secretary of Finance has decided as follows.

This decree replaces the decree of 11 August 2004, No. IFZ2004/127M. In this decree, the preceding decree is updated.

In daily practice, questions have arisen on the application of decrees No. DGB 2014/3101 and No. DGB 2014/3099. More clarity about this application is given below in the questions and answers format.

**I. General**

**1. How should the phrase "de jure or de facto directly or indirectly" in article 3a, paragraph 1, of the regulations of the International Assistance Levying of Taxes Act (hereafter: "Regulations") be construed?**

*Answer:* The phrase "de jure or de facto directly or indirectly" should be construed on a similar manner as in article 10a of the Corporate Income Tax 1969 ("CITA 1969"). This means, for example, that a company taking out a loan with an unrelated party under a guarantee of a related company, whereby the company could not have taken out the loan on a stand-alone basis, the loan "de jure or de facto directly or indirectly" is taken out from the related company.

**2. If the company in the answer on question 1 above (partially) (re)lends the funds obtained to the group company/guarantor, could it be provided with advance certainty on the tax consequences related to the proposed transactions?**

*Answer:* If the conditions of the decrees are met, advance certainty can be obtained.

**3. How should it be determined whether the activities "mainly" consist of receiving and the (on-)payment of interest and/or royalties within the group of companies, as referred to in article 3a, paragraph 1 of the Regulations?**

*Answer:* Connection can be sought with the way of determining whether activities "largely" consist of directly or indirectly financing affiliated companies as referred to in article 10a, paragraph 4, CITA 1969. Hereto, factors such as types of assets and liabilities on the balance, turnover, activities from which the profits are derived, time spent by employees et cetera play a role. With article 3a, paragraph 1 of the Regulations it is not intended to expand the scope of the term service entities, as was provided for in decree No. IFZ 2004/126M, except for the expansion of this term with receiving and paying of rent and lease instalments.

It must be noted that a company performing so-called "cash pool" activities could be subject to decree No. DGB 2014/3101. Considering the diversity of situations wherein "cash pool" activities are performed, no general statement could be made at this moment. Whether a company performing "cash pool" activities is subject to decree No. DGB 2014/3101 has to be determined on the basis of the facts and circumstances.

**4. How should it be determined whether there are sufficient operational activities in the Netherlands?**

*Answer:* This should be determined based on the facts and circumstances. The following matters could play a role here: the number of employees, the operational cost level, the presence of an own space of the group to perform its operational activities, etc.

**5. How should decree No. DGB 2014/3101 be tested with regard to an entity included in a fiscal unity for the CITA 1969?**

*Answer:* The test of the "mainly" criterion as set forth in article 3a, paragraph 1, of the Regulations should be applied at the level of the fiscal unity.

For the real risk requirement it is decisive to what extent risks are assumed and whether sufficient equity is held to bear these risks. At the moment of drafting of article 8c CITA 1969 it was stated that it is decisive how much equity is maintained at the level of the fiscal unity. The same applies for the application of decree DGB 2014/3101.

The subsidiary which is included in a fiscal unity remains the debtor of the loans under civil law. Hence, the substance requirements as included in the annex to the decree should be tested on the level of the entity, except for the so-called appropriate amount of equity requirement. Due to the relation with the real risk requirement the appropriate amount of equity requirement could be tested on the level of the fiscal unity (whereby of course applies that this equity could possibly be claimed, if the risks materialize).

Article 8b CITA 1969 should be applied separately on each entity. Consequently, for each entity the remuneration should be determined based on the functions performed by that entity with due regard of the risks incurred and the assets used.

**6. Is it possible to obtain advance certainty on the application of the requirements of decree DGB 2014/3101 without requesting advance certainty on the remuneration?**

*Answer:* The provision of advance certainty is based on [the decree] of 4 April 2011, No. BLKB2011/265M. Based on that decree a definite answer is given about the tax consequences related to acts of the taxpayer. In the case of a service entity this includes both the application of the requirements of the present decree and the arm's length remuneration of the company and the ability to credit possible withholding taxes. Therefore, in the modified decree it is explicitly included that the provision of advance certainty on the application of the requirements of the present decree takes place exclusively in combination with advance certainty regarding the arm's length remuneration and the ability to credit possible withholding taxes.

**7. Could advance certainty be obtained on the application of article 8c CITA 1969 without requesting advance certainty on the remuneration?**

*Answer:* Decree DGB 2014/3101 states in which cases a service entity is not able to obtain advance certainty on the tax consequences of its proposed transactions. As noted in the answer on question 6 above, for a service entity this includes both the application of the requirements of that decree and the arm's length remuneration of the company and the ability to credit possible withholding taxes. Therefore, a service entity is only provided with advance certainty on the application of article 8c CITA 1969 in case the remuneration forms part of the request for advance certainty.

**II. Withholding tax**

**8. How does the crediting of withholding tax take place?**

*Answer:* Withholding tax credit takes place under the conditions of the applicable tax treaty or the Double Taxation Avoidance Decree 2001. If article 8c CITA 1969 and/or paragraph 4 of decree DGB 2014/3101 apply(ies), no crediting can take place.

**III (a). Substance – board members**

**9. Is the requirement that at least half of the total number of statutory and authorized board members resides in the Netherlands or is actually established in the Netherlands met if half of the statutory board exists of A-members (the directors are resident/established abroad), the other half of B-members (directors are resident/established in the Netherlands) and valid decisions can only be taken with the approval of at least one A-member whereas the approval of at least one B-member is not always required?**

*Answer:* In such a case, the requirement is not met. The requirement must be explained substantive, which means that the director(s) resident/established in the Netherlands has/have at least the same decision-making power as the director(s) resident/established abroad. The place of residence or establishment of a director should be determined according to article 4 of the State Taxes Act.

**10. Do the board members resident/established in the Netherlands have the required professional knowledge to carry out their tasks properly if they are only qualified to look after the daily, local, mostly administrative burden of the entity?**

*Answer:* No, the responsibility and therefore the required professional knowledge of the board members must reach further than daily, local, mostly administrative burden of the entity. The board members must be able to exercise the tasks assigned to them properly. They must take accountability – on the basis of the responsibility of the entity and within the framework of the normal intra-group involvement – for the decision-making with respect to the transactions and (the decision-making with respect to) the good settlement of these transactions.

For example, the responsibility of the board is that it must see on the legal settlement of the transactions, managing the loans and the involved risks, and the construction of transactions. For this task they must have sufficiently professional knowledge.

The board members may choose to hire staff to implement the activities or outsource these activities to external parties. However, the decision-making power with respect to this choice, as well as the monitoring of the application of the activities, must be performed by the board.

**11. As regards the supervisory board members, how is the requirement that at least half of the statutory and authorized board members reside or are actually established in the Netherlands dealt with?**

*Answer:* The decrees only make reference to board members. The board does not include supervisory board members. Therefore, supervisory board members are not taken into account. Non-executive directors are also not taken into account.

**12. Is the requirement that board decisions must be made in the Netherlands met if, with some regularity, the board holds a meeting in the Netherlands where the presented decisions are formally adopted by the present board members?**

*Answer:* It is not sufficient that the presented decisions have already been made abroad and are only formally ratified in the Netherlands. The board meetings must be held regularly and physically in the Netherlands and during these meetings the (important) board resolutions must be taken. However, it is possible that some preparatory operations to the board decisions take place outside the Netherlands. The board must commission these preparatory operations and must be involved with their control and appraisal.

**III (b). Substance – main bank account in the Netherlands**

**13. What is meant by the requirement that the most important bank accounts of the service entity must be held in the Netherlands?**

*Answer:* This criterion must be interpreted in a way that both the entitlement and the decision-making power with respect to the most important bank accounts rests with the Dutch entity. The bank account may be held with a bank established in the Netherlands or a bank established abroad.

**III (c). Substance – bookkeeping in the Netherlands**

**14. It is required that the bookkeeping is conducted in the Netherlands. In practice, frequent communication takes place between the head office of the group and local management at the preparation of the financial account. Which requirements have to be met in order to consider the bookkeeping to be conducted in the Netherlands?**

*Answer:* The accountancy and the administrative actions for that must be physically performed in the Netherlands. Whether or not the accountancy is considered to be conducted in the Netherlands is dependent on facts and circumstances. For example, it is not sufficient that the transactions are administered throughout the year by the foreign head office and that the financial accounts are prepared in the Netherlands once a year. If an entity belongs to a group of companies which has its bookkeeping centralized outside of the Netherlands, the entity is considered to have met the bookkeeping requirement if the group of companies has sufficient operational activities in the Netherlands.

**III (d). Substance - dual resident**

**15. It is required that the service entity is established in the Netherlands and that the service entity, to the best knowledge of the company, is not also considered tax resident in another country. Does this means that an entity incorporated under foreign law does not qualify for obtaining certainty in advance?**

*Answer:* The requirement aims to exclude dual resident entities of obtaining certainty in advance, unless it is considered by both treaty parties as a resident of the Netherlands for treaty purposes. The requirement applies regardless under which foreign law the entity is incorporated. In case there is no tax treaty, it has to be proven conclusively that the entity is established in the Netherlands.

**III (e). Substance - appropriate equity**

**16. How is the appropriate equity determined?**

*Answer:* The amount of equity appropriate for the activities and risks is dependent on facts and circumstances. Although a service entity performs activities within its group, and a banking institution grants services to third parties, the Basel capital agreement may be applied analogous in case of loans. The Basel capital agreement assumes risk-weighted assets; by means of a risk weighting, minimum equity requirements are linked to certain assets. Analogous application of the Basel capital agreement is an example of a possible method for the determination of the amount of appropriate equity; however, other methods for determining appropriate equity are also conceivable.

**17. It is required that the service entity holds at least an appropriate amount of equity considering the functions performed by the entity (taking into account the assets used and the risks incurred). Is this a different requirement than the requirement to hold an amount of equity being 1% of the loan amount or an amount of EUR 2 million, on the basis of paragraph 6 of decree DGB 2014/3101?**

*Answer:* Yes, the minimum amount of equity requirement as meant in paragraph 6 of decree DGB 2014/3101 and the appropriate amount of equity requirement as contained in the annex to that decree are two different requirements. Whether the equity is “appropriate” should be related to the overall activities of the service entity and the risks incurred. Two illustrative examples follow.

*Example 1*

A service entity (SE) has provided a loan of EUR 200 million and holds an equity of EUR 2 million. No guarantees are provided in respect of the loan. SE runs such risks in respect of this transaction that based on an analogous application of the Basel Capital Accord – that is a possible method for determining the appropriate amount of equity – the appropriate amount of equity can be determined at, for example, 4% of the loan granted, or EUR 8 million. The appropriate amount of equity requirement as specified in the annex of the decree is not met and therefore no advance certainty is provided.

*Example 2*

A service entity (SE) holds an equity of EUR 2 million, which is fully invested in Dutch sovereign bonds. Furthermore, SE has provided a loan of EUR 200 million, which is fully funded through an intercompany loan. The risk that SE runs in respect of the loans is limited to EUR 2 million due to guarantees of a group company. Based on the Basel Capital Accord, a loan granted to the government of an OECD country (e.g. the Netherlands) has a weighted risk value of 0 (no risks are run). Based on the risk profile, it is not required to hold equity against the Dutch sovereign bonds. The appropriate amount of equity requirement as meant in the annex of the decree is met, as the equity amounting to EUR 2 million is available to bear the loan-related risk. Therefore, advance certainty can be provided.

### IV. Running real risks

**18. Is the test whether sufficient equity is held within the context of running real risks a non-recurring test at the moment of entering into the transaction or is it a continuous/annual test? And for the appropriate amount of equity requirement as included in the annex to decree DGB 2014/3101?**

*Answer:* In principle, it is a continuous test. However, if the equity is affected because the real incurred risks have materialized, the advance certainty continues to apply. Even if after entering into the transactions, for example as a result of a revaluation, it appears that insufficient equity was available at the aforementioned moment and yet the equity is complemented, the advance certainty continues to apply. If the taxpayer has reduced its equity, for example by repayment of equity, the advance certainty will terminate if sufficient equity is no longer available. The same applies with respect to the appropriate amount of equity referred to in the annex of the decree (substance). If the volume of the transaction is reduced (for example, regarding a loan, by paying off a portion of the principal amount) and/or the related risks incurred are reduced, the equity held may be reduced accordingly while the advance certainty will not terminate, provided that the remaining transactions and risks incurred continue to meet the requirements of the decree.

It should be noted that there must be a realistic possibility that the equity amount that is held in connection with the transactions to which this decree applies is affected if the related risks materialize.

**19. Could the minimum equity to be held of 1% of the loan amount or an amount of EUR 2 million be applied on a similar manner in situations which are a matter of receiving and (on)payment of royalties, rent or lease instalments instead of interest?**

*Answer:* Given the diversity in appearances of situations in which royalties, rent or lease instalments are concerned, this cannot be applied mutatis mutandis. In those situations, the minimum equity to be maintained should always be determined based on the specific circumstances of the case.

Taking into account the above, the equity amount that is held to bear the risks could, however, as rule of thumb, be an amount of at least 50% of the annual royalties, rent or lease instalments to be received, or an amount of EUR 2 million. At least half of the risks run should be composed of market risk.

**20. Are real risks run within the meaning of paragraph 6 of decree DGB 2014/3101 if a loan is granted in two divisions, i.e. specifically in a risk-part and a risk-free part, in the sense that the loan granted is back-to-back for the risk-free part with a pro rata part of the funds borrowed?**

*Answer:* If a loan is granted in two parts, both parts should be assessed separately. With regard to the part of the loan for which no risk is run (which is provided back-to-back) no real risks are run and no advance certainty can be given.

**21. Are real risks run within the meaning of paragraph 6 of decree DGB 2014/3101 if the risk with respect to the loan granted is divided between the service entity and a group company?**

*Answer:* Division of the risk is possible if the service entity continues to run real risks and it is realistically possible that the equity held is affected by materialization of the risks within the meaning of the decree.

This is by all means the case if the risk, when that risk materialises, is run in the first place by the service entity or simultaneously, on a pro rata basis, on behalf of the service entity and the group company.

**22. Are real risks run within the meaning of paragraph 6 of decree DGB 2014/3101 if, in the situation of example 1 of that paragraph, the credit risk (default risk) that the service entity runs would become apparent (X cannot comply with its payment obligations) as a result of which the equity of the service entity is affected but whereby the service entity, as a consequence of an internal guarantee of M (to the service entity), results in a claim on M amounting to EUR 1.5 million?**

*Answer:* No, although DVL holds an equity of more than EUR 2 million, in principle no realistic possibility exists that this equity is affected if X cannot meet its payment obligations. Therefore, SE does not run real risks.

**23. Are real risks run within the meaning of paragraph 6 of decree DGB 2014/3101 if, in the situation of example 1 of that paragraph, M issues a full guarantee with respect to Y and the guarantee commences immediately at the time the credit risk (default risk) that the service entity runs would materialize, yet whereby the service entity (internally) gets a debt to M amounting to its amount of equity at the moment the risk would materialize?**

*Answer:* Yes, if the credit risk (default risk) that SE runs materializes (X cannot meet its payment obligations), the equity of DVL will actually be affected and therefore real risks are run.

**24. Is the risk requirement of article 8c CITA 1969 identical to the real risk requirement as stated in paragraphs 4 and 6 of decree DGB 2014/3101?**

*Answer:* No, article 8c CITA 1969 applies per taxpayer, while the test is assessed at the level of the transaction based on decree DGB 2014/3101. As for the decree this means that when an entity provides several loans, in respect of each of the loans a proportionate amount of the risk should be run. Per loan, a risk should be run equal to the lower of the following amounts:

a. 1% of the (individual) loan, or

b. a proportionate share of EUR 2 million compared to the total amount of loans.

This is explicitly included in paragraph 6 of the decree and illustrated with an example.

**25. Does the real risk requirement as mentioned in paragraph 6 of decree DGB 2014/3101 (i.e. at the level of the transaction) also apply regarding new loans if loans are taken out subsequently?**

*Answer:* Yes, the real risk requirement also applies in that situation. However, in that case it is allowed to expand granted guarantees on existing loans with regard to the allocation of equity to the new loan. An illustrative example: A service entity (SE) has provided a loan of EUR 400 million (loan 1) to a group company. In respect of this loan equity is maintained to the amount of EUR 2 million. SE will provide a new loan of EUR 100 million (loan 2). Regarding loan 2, SE should hold equity that corresponds to an equity of EUR 400,000 (lowest of (a) 1% of EUR 100 million, being EUR 1 million and (b) 100/500 x EUR 2 million, being EUR 400,000). If in respect of loan 2 no real risks are run, no advance certainty will be given. SE can obtain advance certainty regarding loan 2 if SE regarding loan 2 runs enough risk, where the guarantee on loan 1 might be expanded with EUR 400,000 with preservation of the advance certainty regarding loan 1. On balance, an equity of EUR 2 million is sufficient regarding loans 1 and 2 together.

In this context it is also noted that if as a result of entering into subsequent loans a situation arises wherein there is no(t) (longer) a matter of sufficient equity as meant in the annex to the decree, which means that the substance requirements are no (longer) met and the company as a whole is not eligible for advance certainty. To the extent that advance certainty has been given, it will terminate.

### V. Substantiation of the remuneration

**26. Is it possible to determine the remuneration of a service entity on the basis of the cost-plus method?**

*Answer:* The basis for the assessment of the applicable transfer pricing is formed by the framework of article 8b CITA 1969, the Transfer Pricing Decree (Decree of 14 November, No. IFZ2013/184M), the APA Decree (DGB 2014/3098), together with the Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations that were published by the OECD in 1995 and which were amended in 2010 (OECD Guidelines).

Regarding the choice of a particular transfer pricing method the Transfer Pricing Decree stipulates:

"In accordance with Paragraph 4.9 of the OECD Guidelines, whenever the Netherlands' tax administration undertakes a transfer pricing audit, it should start from the perspective of the method adopted by the taxpayer at the time of the transaction. This complies with Paragraph 1.68 of the OECD Guidelines. The implication is that taxpayers are in principle free to choose a transfer pricing method, provided that the method adopted leads to an arm's length outcome for the transaction in question. In certain situations, however, some methods will generate better results than others. Although taxpayers may be expected to base their choice of a transfer pricing method on the reliability of the method for the particular situation, taxpayers are definitely not expected to weigh up the advantages and disadvantages of all of the various methods and then explain why the method that was ultimately adopted generates the best results in the prevailing conditions (i.e. the best method rule). Certain situations are also suited for a combination of methods. At the same time, taxpayers are not obliged to use more than one method. The only obligation resting on the taxpayer is to explain why the decision was taken to adopt the particular method that was adopted."

Regarding financial services, the Transfer Pricing Decree stipulates:

"Financial services exist in a vast variety of forms. Here too, an arm's length price should be calculated on a case-by-case basis, based on the functions performed and on a comparison with transactions between third parties. If the functions of a financial service entity consist primarily in supplying loans, the functions performed by the company in question are basically comparable with the functions performed by independent financial institutions operating under the supervision of the Netherlands' Central Bank (De Nederlandsche Bank). The application of the arm's length principle implies that the arm's length price for the functions performed should be based on the fees charged by these institutions for comparable services. (…)

Independent financial service providers calculate the charges for their loans by adding a number of markups or surcharges to the basic cost of funding, i.e. a surcharge to take account of solvency requirements, a surcharge to take account of the credit risk, a handling fee and a markup for any foreign exchange risk that may be involved. The credit risk should be calculated on the basis of the contractual terms of the loan and the results of the risk analysis described above. The contractual terms of the loan also affect the degree of foreign exchange risk. Independent financial service providers always link the size of the fee charged to either the amount of money borrowed or the market value of assets held under management."

Based on the APA Decree, inter alia, the following information should be provided:

> "6. The APA request
>
> Depending on the facts and circumstances of each case, the taxpayer will have to submit the following information to the tax administration:
>
> (…)
>
> (d) information regarding the worldwide organizational structure (including information on the beneficial owners of the applicant's capital), history, financial data, products and functions, including the assets (tangible and intangible) and risks of and by any of the associated enterprises involved;
>
> (e) a description of the proposed transfer pricing methodology, including a comparability analysis (*which includes comparable data from unrelated market parties and possible adjustments*)."

Although the choice of a particular transfer pricing system is free, the reliability of a method in the present situation should be taken into account when selecting a particular method. In addition, the application of the method should lead to an arm's length outcome.

The remuneration is always related to the managed assets or borrowed funds by independent financial service providers. An APA request should be supported with comparable figures of independent market parties.

The level of costs will, in general, not be a reliable profit indicator for financial services (e.g. by choosing for the transactional net margin method, TNMM) and therefore the cost-plus method will generally not lead to a reliable outcome.

**27. Which method of substantiation of the remuneration could be accepted?**

*Answer:* The choice of a particular transfer pricing method is free, provided that it is in accordance with article 8b CITA 1969, the Transfer Pricing Decree (Decision of 14 November, No. IFZ2013/184M) and the decree no. DGB 2014/3098, together with the Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations which were published by the OECD in 1995, and which were amended in 2010 (OECD Guidelines). An example of a substantiation which is in accordance with these principles is described below. The taxpayer is free to choose a different method of substantiation, as long as it meets the aforementioned principles.

The remuneration for a financial service entity is split into two components: (i) a remuneration for the risk incurred with the disposed equity or a remuneration for the equity "at risk" and (ii) a remuneration for the activities concerning the in- and on-lending of funds (handling fee). Both remunerations are realized by an interest margin, namely the difference between the interest on the loan granted and the interest on the funds borrowed. This margin should be used to cover the costs. Sometimes, the executive activities are outsourced to a third party or a related company; these costs should also be covered by the remuneration, after which a reasonable remuneration should remain.

If the equity is actually used to provide the loan, the service entity's profit consists of the margin between the received interest on the loan granted and the paid interest on the funds borrowed. If the equity is only put “at risk”, the profit of SE consists, apart from the surplus of the received interest on the loan granted and the paid interest on the funds borrowed, of the yield on assets invested in with the concerned equity (e.g. bank interest or dividend).

Two situations should be recognized: (i) the service entity attracts funds from the market and lends these funds on to a related entity, whereby an entity related to the service entity issues a guarantee to the market, and (ii) the service entity borrows funds from a related entity and on-lends these funds to one or more related entities.

In situation (i) the interest on the funds borrowed is paid to third parties. The level of the interest is by definition at arm's length. In principle, the interest is determined by the rating of the entire group (or the group of which the entity forms part) and not by the rating of the service entity as a separate entity. This interest should be raised by an interest margin consisting of a compensation for risks and a handling fee.

The equity of the service entity can be considered economically equivalent with a subordinated loan as for the function of the equity and the risks incurred. The compensation for the risks that the service entity runs regarding the equity can be based on a rise in base points that banks actually use in making loans subordinated (volume, maturity, currency et cetera should be comparable).

The compensation for the risk is the yield between the interest on “secured loans” (RS) and subordinated loans (RA). A secured loan is defined as a loan whereby priority for the creditor arises through collateralization or by non-subordination of the loan. Subordinated loans can be put just above equity and have a comparable risk profile. The reimbursement in euro is determined based on the equity (EV) and subsequently related to the principal amount of the loan granted (LUG) and consequently expressed in base points (RV):

$$RV = \frac{((RA - RS) \times EV) / LUG}{100}$$

As the volume rises, RV will drop.

The foundation of an arm's length handling fee should be based on a comparison of transactions between independent third parties. Information about reimbursements that third parties use can be found in commercial databanks and banks involved in similar transactions. Information can be found regarding the reimbursements for “loan management”. Reference can be found by looking at the reimbursements that bank syndicates and other financial institutions charge for attracting funds from the market for the benefit of third parties.

Legally and factually, the note holders provide loans to an independent third party. The syndicate receives a joint reimbursement expressed in base points for attracting funds from the market. This reimbursement will be divided between the members of the syndicate. It should be examined whether these reimbursements vary based on rating and volume.

The reimbursements are usually charged in base points on behalf of the entire syndicate. The reimbursement is charged for the whole amount of activities that are carried out regarding the transaction. It is this reimbursement for the activities as such that can be used as comparative material.

By comparing the transaction by the syndicate and the transaction by the service entity the conclusion can be drawn that the whole amount of activities regarding the transaction will not only be carried out by the service entity. The service entity will usually carry out such a function jointly with the treasury department of the concern it is part of. If this is the case, the reimbursement can be divided between the service entity and the group entity to which the treasury department belongs, e.g. based on hours worked or full-time units. The assessed amount of base points constitutes the handling fee (HF).

The interest on the loan granted (RLUG) consists of the interest on the funds borrowed (RLOG), increased by the risk compensation and the handling fee: RLUG = RLOG + RV +HF.

In situation (ii) as mentioned before, the service entity borrows from a related entity and on-lends to one or more related entities. The interest of the loan granted can be assessed in the way as explained regarding situation (i). However, the interest on the funds borrowed is not given. The interest on the funds borrowed should be assessed based on the arm's length principle. Therefore, the rating of the service entity and its debtors should be determined in the first place. This can be done based on internal risk models of a bank (if a bank is involved with the counselling or the service entity is part of a bank) or based on publicly available simulation models.

**28. Could a proposal of an independent party form the basis of a comparability analysis?**

*Answer:* The OECD Guidelines (paras. 1.11, 1.12, 1.13) mention the comparisons of transactions between related companies with transactions between independent companies. Actual transactions agreed with a third party or between two third parties are the basis for the comparison. The use of the word "transaction" implies that there is a binding agreement between the parties. A proposal is not binding for at least one of the parties. The conditions mentioned in the proposal are open to negotiations from the perspective of the party to whom the proposal is given. To put it briefly, a proposal is not decisive about actual agreed conditions between parties and therefore cannot be the basis of a comparability analysis. However, if a proposal is made, the possibility should not be dismissed that the proposal is based on actual transactions. The taxpayer might be able to obtain information about these actual transactions and use this information as base for the comparability analysis. In such a case, the proposal itself is not the basis of the comparability analysis, but the proposal might provide the taxpayer with a clue in his search for information about actual transactions. It is the taxpayer's duty to reason that the actual transactions agreed upon are comparable with the contemplated transactions.

## VI. Entry into force

This decree enters into force on the day after the date of publication of the Government Gazette in which this decree is published.

## VII. Withdrawal of the old decrees

This decree replaces the decree of 11 August 2004, no. IFZ2004/127M, which is hereby withdrawn.

## 4. Unofficial translation APA Decree

Decree of 12 June 2014, no. DGB 2014/3098: Procedure for Dealing with Requests for Advance Certainty for Transfer Pricing in Cross-Border Transactions (Advance Pricing Agreements)

**[*to be included*]**

## 5. Unofficial translation ATR Decree

Decree of 12 June 2014, no. DGB 2014/3099: Treatment of Requests for Advance Certainty in the Form of Advance Tax Rulings (ATR)

**[*to be included*]**

### 6. PE Decree

Decree of 15 January 2011, no. IFZ 2010/457M. Decree on the attribution of profit to permanent establishments.

**[*to be included*]**

### 7. Decree on Fiscal Policy

Decree of 7 January 2015, no. BLKB2015/62M. Decree on Fiscal Policy (paragraphs 3 and 4) (in Dutch).

### 3. Vooroverleg

Een rechtsvraag kan ook opkomen bij vooroverleg. Vooroverleg is een overleg tussen de inspecteur enerzijds en de belanghebbende of zijn vertegenwoordiger anderzijds, dat leidt tot een standpuntbepaling van de inspecteur over de wijze waarop het recht in een specifiek geval moet worden toegepast. Een standpuntbepaling is uiteraard pas mogelijk als uit het verzoek de feiten, de rechtsregels en de conclusie duidelijk blijken. De inspecteur loopt met het vooroverleg vooruit op de heffing of de uitvoering van andere aan de inspecteur opgedragen taken. Het specifieke geval kan zowel al verrichte als voorgenomen (rechts)handelingen betreffen.

Het verzoek moet een duidelijke omschrijving van de casus bevatten, waarover een standpunt wordt gevraagd, inclusief alle relevante feiten en omstandigheden en, indien betrekking hebbend op de toepassing van het recht, een helder(e) standpunt/zienswijze/conclusie bevatten over de fiscale consequenties van de voorgelegde casus.

### 4. Fiscale grensverkenning en strijd met goede trouw

1. Als sprake is van fiscale grensverkenning of als er sprake is van strijd met de goede trouw, zet de inspecteur het vooroverleg niet voort en neemt hij ook geen inhoudelijk standpunt in.

- a. Van fiscale grensverkenning is sprake als de inspecteur in het vooroverleg een standpunt inneemt, de vragensteller zich hier niet in kan vinden en vervolgens probeert de casus, door telkens (kleine) wijzigingen aan te brengen, fiscaal net aanvaardbaar te presenteren.
- b. Strijd met de goede trouw die jegens verdragspartners en/of in internationaal verband verschuldigd is, doet zich voor als de inspecteur vermoedt dat het belang van een verdragspartner of een ander internationaal belang wordt geschaad. Van het laatste is onder andere sprake als de inspecteur betrokkenheid vermoedt bij witwassen, steekpenningen, ernstige vermogensdelicten of terrorismefinanciering, tenzij het tegendeel blijkt.
- c. Als bij vooroverleg over (een) voorgenomen (rechts)handeling(en) de inspecteur van mening is dat:
  - a. belastingbesparing de enige dan wel de doorslaggevende beweegreden voor het verrichten van die handeling(en) is en

b. de handeling(en) voor de belanghebbende buiten het beoogde fiscale voordeel geen reële, praktische betekenis heeft (hebben) en voorts

c. doel en strekking van de wet of een verdrag zouden worden miskend als de door de belanghebbende verlangde rechtstoepassing zou worden gevolgd, dan neemt de inspecteur een afwijzend standpunt in.

2. Zo nodig voegt de inspecteur hieraan toe dat hij dit standpunt te gelegener tijd zal formaliseren, bijvoorbeeld bij het vaststellen van een belastingaanslag. De belanghebbende kan daarna gebruik maken van de gebruikelijke rechtsmiddelen.

## 20.3. Internal instructions and guidance for tax authorities relating to transfer pricing and transfer pricing audits

Not applicable.