Letter of 20 September 2016 from the State Secretary for Finance, Eric Wiebes, to the House of Representatives on the tax climate

1. Background

It has always been attractive for businesses to locate in the Netherlands. Our infrastructure is good, our workforce is well educated and our tax climate is benign. These features are important to attract and maintain domestic and foreign investment and thereby create economic growth and jobs. But in the light of international developments, especially in the field of corporate tax, we need to develop a vision of our future tax climate so that we remain attractive to investors while at the same time upholding the principle that businesses should make a fair contribution to public services.

Against this background and in response to three parliamentary motions, the government announced it would present its vision of the tax climate on Budget Day. In the first motion, the Neppérus motion,[1] the House of Representatives asked the government to present a plan that would retain the Dutch tax climate's attractiveness in a responsible manner. The motion was submitted in the light of the OECD Action Plan on Base Erosion and Profit Shifting (BEPS). Following the European Commission's presentation of a proposal for a directive to combat tax avoidance, which has since been amended and adopted, the House approved a second motion, the Neppérus et al. motion.[2] It called on the government in more concrete terms to return the budgetary income generated by the directive to businesses as effectively and responsibly as possible so that it can be fully used to promote jobs and maintain a favourable tax climate. Finally, the House passed the Nijboer motion asking the government to prevent a race to the bottom in corporation tax rates.[3]

The government sets out its vision of the future tax climate in this letter. It proposes a strategy in which it vigorously continues its proactive approach to international tax avoidance while maintaining a favourable tax climate with a competitive corporation tax rate.

---

[1] Parliamentary Papers, House of Representatives, 2015/16, 34 302, no. 73.
[2] Parliamentary Papers, House of Representatives, 2015/16, 22 112, no. 2087.
[3] Parliamentary Papers, House of Representatives, 2015/16, 21 501-07, no. 1381.

2. A good and competitive business climate in the Netherlands

… is essential for investments and jobs …

A good business climate is one that encourages businesses to invest in the Netherlands. Investment creates economic growth and jobs. Both national and international businesses compare the business climate in different countries before taking investment decisions. The Netherlands has traditionally been relatively successful at attracting and retaining multinational groups that create real jobs in, for example, regional head offices, central purchasing and sales divisions and research centres. Where the decision to locate in a particular country is based chiefly on taxation, our main competitors in Europe are the United Kingdom, Ireland, Switzerland and Belgium.

Attracting and retaining multinationals is not a goal in itself. What they do here is more important. These businesses are pillars of our open economy and economic activity. Statistics Netherlands calculated in a recent report that multinationals account for over 50% of the added value created by all businesses in the Netherlands and over 80% of our international goods trade. It also found that 40% of people in employment in the Netherlands worked for multinationals. Foreign multinationals generate nearly a fifth of all our jobs, introduce new technologies and are a source of knowledge.[4] Small and medium-sized enterprises also benefit directly and indirectly from the presence of multinationals and regional headquarters, thanks to the transfer of knowledge and also, for example, the provision of goods and services.

... is about more than just taxes …

A business's decision to locate in a particular country is determined by a wide range of factors, including accessibility, educational standards, quality of life and government reliability. The Netherlands scores highly on many of these factors.[5] For example, the country is favourably located, its infrastructure is good and the workforce is well educated. The living environment in the Netherlands is also favourable, partly due to the high standard of public services and the government's reliability. Businesses also attach great value to the clarity of Dutch legislation.

---

[4] Statistics Netherlands, Internationalisation Monitor (third quarter, 2015). This report is also quoted in *Rapport werkgroep Fiscaliteit ten behoeve van de Studiegroep Duurzame groei*, July 2016, available (in Dutch) at https://www.rijksoverheid.nl/documenten/rapporten/2016/07/06/advies-studiegroep-duurzame-groei. Multinationals are defined here as businesses in the Netherlands that are controlled from abroad and Dutch businesses with foreign subsidiaries.

[5] See, for example, NFIA, Business Climate Monitor, October 2015.

… but taxes are important

The Dutch tax system has various strengths that contribute to the business climate. Thanks to our open economy, based on international trade, and the importance of foreign markets to Dutch businesses, the Dutch tax system has traditionally had an international focus. The corporation tax system, for instance, includes a participation exemption that prevents the double taxation of corporate profits. Important elements outside the corporation tax system include our extensive treaty network, the absence of withholding taxes on interest and royalties and our efficient dispute resolution procedures. The possibility of obtaining certainty in advance from the Tax and Customs Administration is a key pillar of the Dutch tax climate. Other important features are tax incentives to encourage innovation and the level of taxes on labour. The government reduced the tax burden on labour by €5 billion this year.

3. International developments

The fight against tax avoidance …

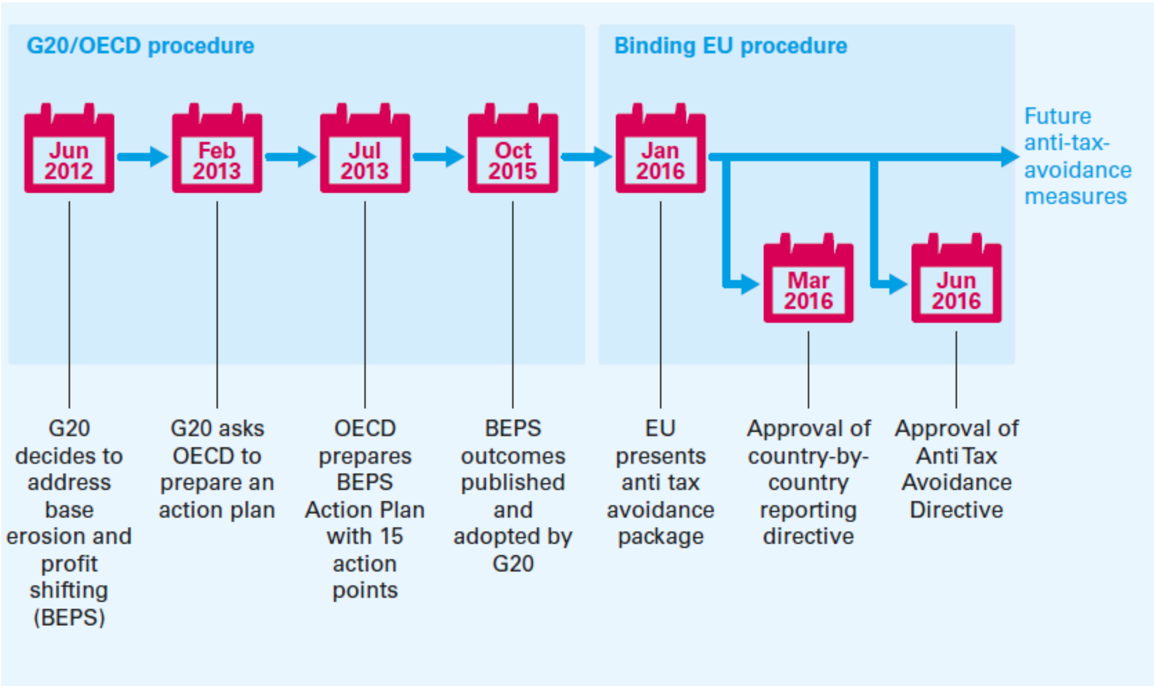
Multinationals are not only a source of investments and jobs. Our tax regime's international focus and the differences between national tax systems also have a downside. Businesses are tempted to use the Dutch system and treaty network for unintended purposes. Artificial structures are used to erode the tax bases of other countries and so avoid foreign taxes. In some cases businesses erode our tax base by exploiting differences between tax systems, for example concerning the deduction of interest. Both these practices are undesirable and are encountering growing public resistance. The Netherlands has therefore consistently and unreservedly committed itself to the OECD's BEPS project.

The final BEPS reports were released by the OECD and endorsed by the G20 towards the end of 2015. The Netherlands will follow them up in a variety of ways. For example, it will adopt the new minimum standard on treaty abuse agreed in the BEPS project so that it is less attractive to use Dutch shell companies in international structures. It transposed the BEPS agreements on country-by-country reporting into national law even before it assumed the Presidency of the Council of the European Union, and it successfully incorporated country-by-country reporting into an EU directive during the Presidency. The Anti Tax Avoidance Directive (ATAD) was adopted later in the Presidency, in June 2016.[6] These measures will gradually harmonise the corporate tax bases of different countries, for example by introducing a generic limit on the deductibility of interest in the form of an

[6] Council Directive (EU) 2016/1164 of 12 July 2016 laying down rules against tax avoidance practices that directly affect the functioning of the internal market.

earnings stripping measure. This welcome step will simultaneously and uniformly tackle several forms of tax avoidance in all EU member states while protecting the tax base. To guarantee a level playing field, the European Commission will ensure state aid rules are respected, for example in agreements in which tax authorities provide individual businesses with certainty in advance.

Figure 1: Timeline with steps to combat tax avoidance



… makes the corporation tax rate more important

In anticipation of a future in which tax planning is no longer the overriding factor in business location decisions, other countries with attractive tax climates are lowering their tax rates. The corporate tax rates in the United Kingdom, Ireland and Switzerland are already less than 20%, or will be soon. Belgium recently announced it would introduce a lower, uniform rate of 20%. The top rates in Denmark, Finland and Sweden are now lower than in the Netherlands. Tax competition is shifting from tax base to tax rate. This means we will have to rethink our tax climate and offer a long-term vision to avoid missing out on real economic activities with real jobs. Without further measures, the Netherlands' top corporation tax rate of 25% will deter multinationals from investing here. Our business climate, including the tax climate, is attractive, but we have to take action if it is to remain so in the future.

4. The best of both worlds

International developments call for a proactive response from the Netherlands ...

Tax planning structures that have influenced business location decisions here and elsewhere are losing their credibility and therefore their attraction in the acquisition of companies. This is leading to uncertainty, which is bad for the business climate. We need to act simultaneously on two fronts: (1) we must vigorously continue the Netherlands' proactive approach to tax avoidance and act as an international leader in this field; and (2) we must lower the corporation tax rate to a competitive level. In concrete terms, the more successful we are at combating tax avoidance, the more we can reduce corporation tax rates. The government will use this strategy to implement the Neppérus motion.

... with active anti-tax-avoidance measures ...

The OECD agreement and the subsequent ATAD clearly show which international tax structures should be consigned to the past. Without isolating itself, the Netherlands can actively combat those structures in a practical and legally certain manner, and provide an acceptable transition period if necessary. The government's tax avoidance strategy makes a clear distinction between real activities and artificial structures.[7] It is opting for a proactive international approach and vigorously implementing ATAD. It aims to submit a bill for consultation in the second half of 2017. Tackling tax evasion (fraud) is and will remain a priority of government policy. The Panama Papers underlined the need to combat it. The government intends to present proposals in this area later this year. If they receive sufficient support from the House, they will then be fleshed out and enacted.

... and a phased route to competitive corporation tax rates

As tax planning opportunities are restricted, the importance of the statutory corporation tax rate increases, alongside the Netherlands' traditional – tax and non-tax – strengths. An attractive statutory tax rate is a significant – and sometimes decisive – factor when national and international businesses decide to shortlist a particular country. Corporation tax is therefore an important factor when businesses decide where to locate. If the tax rate is high and non-tax factors are comparable, businesses will tend to locate in another country. Corporation tax rates must therefore be competitive.

The government wants the Netherlands to retain competitive tax rates but does not wish to take part in an undesirable race to the bottom. The Netherlands does not wish to limit other countries' freedom to set their own rates, but it is in every country's interests to prevent such a race. Given the standard of our public services, we cannot afford to act as discounters. Furthermore, corporation tax rates should be proportionate to personal income tax rates.

[7] Parliamentary Papers, House of Representatives, 2015/16, 34 306, no. 6, p. 2 (Amendment of the Parent-Subsidiary Directive (Implementation) Act 2015).

Multinationals must pay their fair share. The cost of lower corporation tax rates must not be borne by private taxpayers; their tax burden must not be increased. The government will thus implement the Nijboer motion, which called on it to avoid a race to the bottom in corporation tax rates.

It goes without saying that appropriate compensation must be found for any rate reduction, for example in the form of a wider tax base and greater harmonisation. A report issued by the Sustainable Growth Study Group presents measures that could offer compensation and allow for a raft of political decisions to lower the top rate.[8] Part of any future tax burden reduction could also be used to lower the corporation tax rate. Decisions on this matter will have to be made in the broader context of negotiating a coalition agreement.

This combined strategy means the Netherlands will retain an attractive tax climate but one where aggressive international tax planning arrangements are replaced with a more sustainable arsenal of tax instruments. Aggressive tax behaviour will be made impossible or quickly addressed and, thanks to a competitive corporation tax rate, the Netherlands will remain in all respects an attractive location for new investments, resulting in the creation of new and lasting jobs.

5. The future beckons

We are now taking the first steps ...

More has been done to combat international tax avoidance in the last two years than in the decade before. The Netherlands used its EU Presidency to reshape its profile on this issue. An extensive package of EU rules to combat tax avoidance has been agreed and bills have been submitted to the House that, from next year, will implement the directive on the automatic exchange of information on tax rulings and bring the innovation box into line with the internationally agreed standard. The rules on trust offices will also be tightened up.[9] Implementation of ATAD is planned for the near future.

In addition, the first step regarding the corporation tax rate will be taken to ensure, in a responsible fashion, that the Dutch tax climate remains attractive in the long term. In the 2017 Tax Plan, the first corporation tax band (the 20% band) will be raised in steps from

[8] *Kiezen voor duurzame groei*, report of the Sustainable Growth Study Group, July 2016 and *Rapport werkgroep Fiscaliteit ten behoeve van de Studiegroep Duurzame groei*, July 2016, available (in Dutch) at: https://www.rijksoverheid.nl/documenten/rapporten/2016/07/06/advies-studiegroep-duurzame-groei.

[9] The aim is for the tighter rules on trusts to come into effect before the end of 2018.

€200,000 to €250,000 in 2018, €300,000 in 2020 and €350,000 in 2021. This will also benefit SMEs.

... and will take further steps on a firmer basis

Opting for both a proactive approach to international tax avoidance and a reduction in the corporation tax rate represents a new tax strategy for the years ahead.