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Transfer Pricing 2024

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Netherlands: Trends & Developments

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Trends and Developments

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Introduction

The Dutch transfer pricing landscape was impacted by various developments in 2023 and early 2024. Amongst others, these developments consist of clarifications around the transfer pricing mismatch legislation that was introduced in 2022 and case law addressing several transfer pricing topics. This article will furthermore address both European and broader international developments impacting the Dutch transfer pricing landscape, including the transfer pricing impact of Pillar Two, the proposal for an EU directive on transfer pricing, and Amount B.

Transfer Pricing Mismatch Legislation

As of 1 January 2022, the Netherlands has legislation in its Dutch Corporate Income Tax Act (CITA) that aims to eliminate double non-taxation through transfer pricing mismatches. The legislation requires Dutch taxpayers to ensure that intercompany transactions are priced at arm's length and correctly documented. Otherwise, this new legislation could potentially result in adverse Dutch corporate income tax (CIT) consequences.

The legislation includes three main elements:

- Article 8bb CITA allows no downward adjustment of the Dutch taxable profit without a corresponding upward adjustment;
- Article 8bc CITA allows no adjustment in the Dutch tax basis to the arm's length value for asset and liability transfers to the extent that no corresponding adjustment is taken into account in the transferor's profit tax base; and
- Article 8bd is applicable to contributions, distributions, and (de)mergers, pursuant to which the Dutch CIT base is at maximum (for assets) or at minimum (for liabilities) the value included in the transferor's tax base.

Also, the legislation contains a transitional rule that applies to asset transfers that took place between 1 July 2019 and 1 January 2022 and that would have been affected by the transfer pricing mismatch legislation, had the legislation been in force at the time. In that case, the transitional rule limits the depreciation amount to be taken into account by a Dutch taxpayer going forward (ie, from the financial years starting on or after 1 January 2022).

In practice, the (non-)applicability of Article 8bd CITA led to much uncertainty for taxpayers. On 24 January 2023, the Dutch State Secretary of Finance (the "State Secretary") issued a decree clarifying that capital contributions and distributions to a Dutch entity by an entity that is not subject to a profit tax are not affected by this provision, provided that the fair market value is included in the related civil law documentation and annual accounts. For certain situations and entities, the decree provides a comparable "fall-back" position to that envisioned in Articles 8bb and 8bc of the CITA, meaning that the contractually agreed or imposed price (even if not at arm's length) would be used for Dutch CIT purposes if there is no corresponding adjustment. The clarification by the State Secretary reduces uncertainties, especially concerning pension funds and other exempt entities.

In addition, two helpful knowledge group positions ("KG Positions") were published in June 2023. These KG Positions clarify the Dutch Tax Authorities' (DTA's) interpretation of the scope of the transfer pricing mismatch legislation in respect of contributions. The KG Positions were published as part of the DTA's recent policy to externally publish the views of its internal knowledge groups.

These KG Positions concern the contribution of impaired loan receivables against the issuance of shares. The DTA's knowledge group takes the position that these situations do not fall within the scope of Article 8bd of the CITA, even though there is a difference in value reported in the hands of the transferor and in the hands of the transferee. Both KG Positions confirm that there is no transfer of an asset within the meaning of Article 8bd of the CITA and that Dutch taxpayers therefore do not realise a taxable profit in relation to the debt release under the transfer pricing mismatch rules. The KG Positions provide a welcome clarification of the DTA's view on the scope of the rules, specifically in respect of contributions of an (impaired) receivable. Even though no general guidance is provided on the scope of Article 8bd of the CITA and the KG Positions in principle only apply to the specific cases at hand, the DTA's reasoning provides helpful arguments supporting the non-applicability of Article 8bd of the CITA in similar situations, such as for contributions involving entities that are disregarded for US tax purposes and tax-exempt entities. Nevertheless, the (non-)applicability of the transfer pricing mismatch rules remains peculiar, and specific situations might call for obtaining an advance tax ruling to provide the certainty taxpayers desire.

The Transfer Pricing Decree

On 1 July 2022, the State Secretary published the new Transfer Pricing Decree (the "TP Decree"), taking effect as of 2 July 2022. The TP Decree represents the views of the State Secretary (and, by extension, of the Dutch Ministry of Finance and DTA) on the interpretation of transfer pricing provisions, where taxpayers can still take deviating positions within the confines of Dutch legislation and case law. The TP Decree replaced the previous TP Decree from 2018, to be more aligned with the terminology of the 2022 OECD Transfer Pricing Guidelines (TPG). The main changes concerned the new guidance on financial transactions (ie, loans and guarantees) and the treatment of financial service companies (SCs).

Financial transactions

The updated section on financial transactions in the TP Decree has been aligned with the content of Chapter X of the TPG on financial transactions. This section emphasises, amongst other things, that it should first be determined whether a prima facie loan should be considered a loan for transfer pricing purposes. If adjusting the interest rate and/or other conditions of the loan transaction is not sufficient to make the transaction at arm's length, part of the loan may be reclassified to equity for transfer pricing purposes. The State Secretary believes that an arm's length interest charge should then be determined only for the remainder of the loan. However, a partial reclassification of a loan into equity, as now included in the TP Decree, contradicts the existing case law of the Dutch Supreme Court and it remains to be seen whether the view of the State Secretary will actually hold before court.

Financial service companies

The TP Decree further addresses the treatment of SCs. An SC is a company that predominantly (ie, more than 70%) receives and on-pays royalties, interest and lease payments within the group. The SC generally has limited risk either through the loan agreement or through a guarantee from the parent company. In the TP Decree, the State Secretary stresses that the arm's length remuneration of SCs must be aligned with the control over the credit risks and financial capacity to bear the potential negative consequences when such risks materialise.

On 12 February 2024, an independent working group of Dutch officials and external counsels (the "Working Group") published an extensive building blocks report containing policy recommendations to improve the Dutch tax system, amongst which is the recommended replacement of the current safe harbour rules for SCs. By virtue of the CITA, interest and royalties received and on-paid within the group by Dutch SCs are excluded from the Dutch taxable base if the SC does not incur real risk with respect to its conduit activities. This means, inter alia, that foreign withholding taxes are not creditable against Dutch CIT due. The CITA currently contains a safe harbour based on which SCs are deemed to incur a real risk if their equity equals at least (i) 1% of the outstanding loans or (ii) EUR2 million. The Working Group's policy recommendation suggests abolishing this safe harbour and replacing it with an open norm in line with the TP Decree. This would entail that a company must have sufficient control and financial capacity to manage its risks to (i) be allowed to credit withholding taxes, and (ii) account for the received and on-paid interest or royalties in its Dutch CIT base. It remains to be seen whether this recommendation will be followed by a new Dutch government and implemented in Dutch tax legislation.

Recent Relevant Dutch Case Law on Transfer Pricing

There has been an increase in litigation concerning transfer pricing in the Netherlands in the last few years. One of the recent Dutch court cases on transfer pricing addressed the use of implicit support for the purpose of determining a multinational entity's (MNE's) credit rating and the burden of proof in transfer pricing. The DTA disallowed a significant part of the deducted interest expenses and fully disallowed the deduction of commitment fees by a Dutch BV (private limited company), both in respect of certain intercompany loan facilities ("Facilities"). The interest rates for the Facilities were determined based on the credit rating of the BV, being the borrower under the Facilities. The DTA argued that the arm's length interest rates should have been lower due to the existence of implicit support from the parent company, which would enhance the BV's credit rating. The BV successfully challenged the claim of the DTA by providing statements from former bank employees, confirming that third-party lenders generally do not take into account implicit support when setting interest rates. In view of this case, it seems that the DTA cannot just assume the existence of implicit support without further substantiation.

The DTA also argued that the burden of proof had to shift to the taxpayer since the BV had not prepared contemporaneous transfer pricing documentation concerning the Facilities. Instead, the BV had prepared such documentation only after the DTA requested it to provide substantiation of the intercompany pricing. The court ruled that the DTA failed to prove that the BV's transfer pricing documentation contained errors that should have resulted in the conclusion that the BV had filed an incorrect CIT return. The fact that the BV prepared its transfer pricing documentation at a later stage (ie, only after the DTA's request) did not change this outcome.

In another case brought before the court, the DTA had relied, for its assessment, on internally prepared documents that were not necessarily prepared for tax purposes. Such documents included internal presentations, board minutes and external communication. The court considered that the content of these internal documents was relevant for assessing whether or not "something of value" had been transferred between affiliated entities, irrespective of how

such deemed transfer was contractually documented. In particular, these documents were used to substantiate that the taxpayer involved had been aware of an intercompany transfer of functions, assets and/or risks, as well as that such transfer involved material value for the parties involved.

Amongst other things, recent Dutch case law again stresses the importance for taxpayers of having adequate and preferably contemporaneous transfer pricing documentation in place. However, based on recent case law, it may also be possible to meet the transfer pricing documentation requirements even if the documentation was not prepared contemporaneously, provided that the documentation is appropriate, non-contradictory, and sufficiently comprehensive to substantiate the arm's length nature of the transaction.

Further Dutch transfer pricing litigation is anticipated, including the appeal of some of the above-mentioned cases, in the coming period.

Dispute Resolution and Prevention

The number of tax audits has increased substantially over the last few years in the Netherlands. These tax audits often focus on financial transactions, business restructurings (ie, including the onshoring of intellectual property), and the general transfer pricing policies of MNEs. Also in view of the above-mentioned increase in litigation, alternative dispute resolution and prevention has become even more relevant.

To avoid discussions, taxpayers may consider entering into a (bilateral) advance pricing agreement (APA). In view of some of the developments already mentioned, a bilateral APA is generally preferred over a unilateral APA. Although there is no obligation for the competent authorities to reach an agreement on a bilateral APA, successful outcomes are in most cases reached by the Dutch competent authority.

Internationally, discussions with tax auditors may lead to a mutual agreement procedure (MAP). The increasing number of MAPs is expected to persist, as transfer pricing discussions arise more frequently and more MAPs are expected. MAPs remain an attractive cross-border mechanism to resolve double taxation that often results from a unilateral correction by a tax authority, where the Dutch competent authorities reach a resolution in most cases even without mandatory binding arbitration.

International Developments Impacting the Dutch Transfer Pricing Landscape

The proposal for an EU Directive on Transfer Pricing

On 12 September 2023, the European Commission released a legislative proposal for a Council Directive that integrates key TP principles into EU law (the "TP Proposal"). The TP Proposal seeks to harmonise TP norms within the EU through the incorporation of the arm's length principle into EU law and the clarification of the role and status of the TPG. To ensure a common application of the arm's length principle, the 2022 version of the TPG will be binding when applying the arm's length principle in EU member states. If adopted unanimously in the EU Council, member states must apply the provisions as of 1 January 2026.

The TP Proposal differs somewhat from current Dutch tax legislation and regulations. Examples of these differences include the following.

- The definition of "associated enterprises" under the TP Proposal includes permanent establishments and natural persons. This is a

broader definition than currently relied on by certain member states, including the Netherlands. The definition contains a quantitative threshold of 25%, whereas Dutch tax legislation is currently based on an open norm based on Article 9 of the OECD Model Tax Convention.
- According to the TP Proposal, the arm's length range must be determined using the interquartile range. If a result falls outside the interquartile range, tax authorities must make an adjustment to the median. This rule is more stringent than current Dutch tax law, where the use of the interquartile range is not imposed and there is no obligation to adjust to the median.
- The TP Proposal requires taxpayers to have sufficient transfer pricing documentation available. The European Commission will further specify the documentation requirements at a later stage, but documentation comparable to a Local File may be required. Since the TP Proposal does not contain a revenue threshold, these documentation requirements could result in an additional compliance burden for taxpayers that currently do not fall within the scope of the Local File obligations.

The State Secretary informed the Dutch Parliament that the Netherlands would prefer the TP Proposal to be, as much as possible, in line with the TPG. Divergence from the TPG can lead to the arm's length principle being applied differently within the EU compared to outside it. In addition, the State Secretary stated that the TP Proposal seems to hold member states responsible for ensuring that transactions are in line with the arm's length principle. Instead, the Netherlands would prefer the TP Proposal to mandate that taxpayers themselves have the primary responsibility to ensure that cross-border transactions are entered into in accordance with the arm's length principle. In view of these Dutch reservations and those of other member states, it remains to be seen whether the TP Proposal will be implemented in its current form.

Transfer pricing aspects of Pillar Two

The Dutch domestic Pillar Two legislation has entered into force as of 1 January 2024. Pillar Two introduces the Global Anti-Base Erosion (GloBE) Rules, which seek to enforce a global minimum CIT at an effective rate of 15%, calculated on a jurisdiction-by-jurisdiction basis. Pillar Two applies to MNEs meeting the consolidated group revenue requirement of EUR750 million per year.

Pillar Two includes a specific provision on arm's length pricing that applies to in-scope MNE groups. This transfer pricing provision stipulates that transactions should be valued at arm's length prices, including transactions between non-Dutch entities and between a permanent establishment and the head office. Furthermore, the Pillar Two legislation contains specific provisions prescribing when adjustments in accordance with the arm's length principle can be booked and to exclude them if they result in double non-taxation. Where possible, making year-end adjustments not accounted for in previous consolidated annual financial statements, as well as other adjustments in later years, should be avoided. Adjustments that may take place in a later year might have an adverse Pillar Two effect due to the transaction not being correctly priced in the year of the review.

Where the Dutch transfer pricing mismatch legislation already places emphasis on consistent pricing within the group, this has become even more relevant now that Pillar Two has entered into force. The Pillar Two legislation requires taxpayers to ensure alignment between financials

and tax accounts in accordance with the arm's length principle. However, specific local transfer pricing rules (eg, the transfer pricing mismatch rules or the "non-businesslike loan" case law in the Netherlands) may make such alignment difficult. It remains to be seen whether the proposed TP Proposal can provide the desired harmonisation within the EU in this respect.

Pillar One – Amounts A & B

Pillar One's Amount A seeks to create a new taxing right for market jurisdictions, independent of the physical presence requirement and determined using a formulaic approach. Although a final agreement was nearly reached, the Multilateral Convention (MLC) text released on 11 October 2023 is not open for signatures yet. The Dutch State Secretary informed the Dutch Parliament that, even though the Netherlands remains in favour of an international agreement on Pillar One by means of an MLC, alternatives should be considered if a global agreement becomes less feasible. In this regard, the Netherlands would then prefer a European solution over a unilateral digital services tax.

On 19 February 2024, the OECD Inclusive Framework (IF) published the Pillar One Amount B Report. This Report provides guidance on an optional application of a simplified and streamlined approach ("S&S Approach") to baseline marketing and distribution activities. The S&S Approach provides a pricing framework that includes a three-step process to determine a return on sales for in-scope distributors. No minimum revenue threshold is applicable for the S&S Approach. Jurisdictions can choose to apply the S&S Approach for fiscal years beginning on or after 1 January 2025. The Report has been incorporated in the TPG as an Annex to Chapter IV. It remains to be seen how the S&S Approach will be further implemented in Dutch tax law and regulation. This could be effected through an update of the current TP Decree if the S&S Approach would be optional, whereas a mandatory application would require a change of law.

BEFIT

On 12 September 2023, the European Commission proposed a Council Directive on Business in Europe: Framework for Income Taxation (the "BEFIT Proposal"). The BEFIT Proposal contains a common CIT framework for groups active in the EU. If adopted within the timeframe envisaged by the Commission, member states must implement the BEFIT proposal by 1 January 2028 and apply its provisions as of 1 July 2028.

The BEFIT Proposal stipulates that in the first seven fiscal years following its implementation, transactions between entities that are subject to the BEFIT rules (ie, intra-BEFIT group transactions) are considered at arm's length if they are considered to be in "a low-risk zone". The "low-risk zone" would cover the expense incurred/income earned by a BEFIT group member from an intra-BEFIT group transaction that increases by less than 10% compared to the average amount of the income or expense in the previous three fiscal years. If this threshold is exceeded, the transaction is presumed not to be consistent with the arm's length principle, unless the BEFIT group member can provide evidence that the relevant intra-BEFIT group transaction was priced at arm's length.

The State Secretary informed the Dutch Parliament that the Netherlands expects BEFIT to increase compliance costs for tax authorities as well as for taxpayers, which would undermine BEFIT's goal of decreasing the administrative burden for tax authorities and taxpayers. As BEFIT will have a major administrative impact

for MNEs with a European footprint, it remains highly uncertain if, and when, member states will reach an agreement on its adoption.

Concluding Remarks

There have been many important transfer pricing developments in the Netherlands in 2023 and early 2024. The transfer pricing mismatch rules remain an attention point for Dutch taxpayers, where the published DTA's views on the scope of the rules provide welcome clarification. In addition, the introduction of Pillar Two, as of 2024, has made consistent pricing within the group and avoiding adjustments in later years even more important. Further, developments in recent Dutch case law increasingly require taxpayers to have comprehensive and, preferably, contemporaneous transfer pricing documentation. Taxpayers are, furthermore, recommended to closely monitor the various European and broader international developments affecting the Dutch transfer pricing landscape, including developments around the TP Proposal and the implementation of the S&S approach (ie, formerly known as Pillar One's Amount B).

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