The road to acceptable conduit activities

Committee on Conduit companies

October 2021

Foreword

We are pleased to present below the report of the Committee on Conduit Companies. At the request of the House of Representatives, we, the Committee, have spent the past six months investigating the activities of conduit companies in the Netherlands, also sometimes referred to as letterbox companies. Our remit was by no means an easy one. There is no clear definition of a conduit company, which is not least because of the wide range of organisations that qualify as one. We came across a case where a German-French joint venture was set up with the holding company in the Netherlands to evade the issue of deciding whether the joint venture was to be governed by French or German law; that is how the well-established Dutch legal system came to be chosen. That is all well and good. However, things take a different turn when we find out that foreign profits are being channelled through the Netherlands to Bermuda, only to end up in the hands of an American company with a low tax rate. And unfortunately, Dutch letterbox companies are also used in long chains of vacant entities to conceal and eventually launder criminal proceeds. We also established that the Netherlands has for many years made itself an attractive option for organising conduit activities, and that the enormous ensuing flow of such activities will not automatically dry up again now that the tax regime is more on a par with countries comparable to ours.

We as a Committee have set out to develop a usable definition of a conduit entity, and have charted the extent of the conduit activities via the Netherlands as clearly as possible. We have also compared the relevant international tax systems to see where the Netherlands clearly differs from other countries and therefore attracts more conduit activities. We have also looked at what measures the Netherlands has already taken in recent years to combat the international abuse of tax systems, particularly regarding conduit activities, what we know of the effects these measures have had, and what additional measures are conceivable.

Our inquiry has resulted in a number of recommendations. As well as a call to gather more knowledge, they focus mainly on action at a European level, partly because the Dutch tax options are strongly embedded in the European legal system, but also because it would be of little benefit from the perspective of a fair international tax system if flows that are blocked in the Netherlands were subsequently to be channelled through another European country. The Committee believes that the flow of funds not related to economic activities in the Netherlands itself can be further restricted by reducing the country's fiscal attractiveness, increasing transaction costs, requiring more transparency, exchanging more information and strengthening supervision and enforcement.

We trust that we have thus been of service to the political decision-making process.

At this point, we as the Committee would like to take this opportunity to express our gratitude for the many pleasant discussions we have had the privilege of holding with a number of experts on this subject. We are also very grateful to the Dutch Central Bank (DNB), the Tax and Customs Administration, CBS and AMLC for their work to provide us with accurate figures. A special word of thanks is due to the secretariat of our Committee. Nadia Ganga, Bart van Raaij, Daan de Leeuw and Ben Tichelaar, always providing us with texts of the highest quality has hugely supported us in our work! Unfortunately, during the course of our activities we had to part company with Professor Unger as a member of our Committee. She stepped down prematurely because she found the Committee's focus to be overly tax-oriented and was not sufficiently confident that the Committee would adequately get to grips with the money laundering aspect of the remit, which is where her area of expertise lies. Given the limited time remaining for the Committee at the time, it was decided in consultation with the Ministry of Finance not to seek a replacement for Professor Unger. We have nevertheless endeavoured to do as much justice as possible to the money laundering aspects of the remit in our report.

As Chair of the Committee on Conduit Companies, I would like to sincerely thank the members of the Committee for our enjoyable time working together. We have held intensive, complex but always constructive talks to arrive at a shared end-product. Thank you!

All that now remains is for me to commend this report to you and to express the hope once again that it will serve the Dutch (and perhaps European) decision-making process concerning conduit companies.

Bernard ter Haar

Table of contents

Foreword 2

Summary 9

1 Introduction 15
- 1.1 Terms of Reference 15
- 1.2 Context 15
- 1.3 Research approach 18

2 What is a conduit company? 20
- 2.1 Introduction 20
- 2.2 Terms in legislation and regulations 20
- 2.3 Assessment on the basis of characteristics 22
- 2.4 Definition for statistical purposes 24

3 Dear flow in figures 27
- 3.1 Introduction 27
- 3.2 Number of conduit companies and balance sheet size 28
- 3.3 Income streams 29
- 3.4 Types of conduit companies 33
- 3.5 Importance for the Dutch economy 35

4 What is the role of taxation? 36
- 4.1 Introduction 36
- 4.2 Main tax elements for conduit companies 36
- 4.3 Measures taken and announced 49
- 4.4 Monitoring the effects of fiscal policy measures 55
- 4.5 International context 56

5 What is the role of non-tax factors? 59
- 5.1 Introduction 59
- 5.2 Business climate 59
- 5.3 Corporate law 61
- 5.4 Bilateral investment treaties 62

6 What is the link between tax avoidance and money laundering? 65
- 6.1 Introduction 65
- 6.2 Concurrence with tax avoidance 66
- 6.3 Measures taken and announced 70

7 Findings 75
- 7.1 Introduction 75
- 7.2 Fiscal measures 75
- 7.3 Non-fiscal measures 77
- 7.4 Money laundering 80

8 Recommendations 83
- 8.1 Introduction 83
- 8.2 Fiscal Recommendations 83
- 8.3 Non-fiscal policy options 85

Enclosures 88

Annex 1: External input 88
Annex 2: Composition of the committee 89
Annex 3: Country classification used 90
Annex 4: Examples of tax conduit structures 91

List of Abbreviations

AML	Anti-Money Laundering
AMLC	Anti Money Laundering Centre
AMLD	Anti-Money Laundering Directive
APA	Advance Pricing Agreement
ATR	Advance Tax Ruling
BIT	Bilateral Investment Treaty
GDP	Gross Domestic Product
BEPS	Base Erosion and Profit Shifting
GNI	Gross National Income
BV	Besloten vennootschap (private limited company)
BW	Burgerlijk Wetboek (Dutch Civil Code)
CBS	Statistics Netherlands
CFC	Controlled Foreign Company
CFT	Countering Financing of Terrorism
CV	Commanditaire vennootschap (limited partnership)
FDI	Foreign Direct Investment
DNB	De Nederlandsche Bank (Dutch Central Bank)
DVL	Dienstverleningslichaam (Service Providing Body)
EU	European Union
FATF	Financial Action Task Force
FEC	Financial Expertise Centre
FIOD	Fiscale Inlichtingen- en Opsporingsdienst (Fiscal Intelligence and Investigation Service)
FIU	Financial Intelligence Unit
GAAR	General Anti-Abuse Rule
ECJ	European Court of Justice
HTJ	High tax jurisdiction
IBFD	International Bureau for Fiscal Documentation
IMF	International Monetary Fund
LTJ	Low tax jurisdiction
NFIA	Netherlands Foreign Investment Agency
NGO	Non-governmental organisation
NRA	National Risk Assessment
NV	Naamloze vennootschap (public limited company)
OECD	Organisation for Economic Co-operation and Development
PPT	Principal Purpose Test
PSD	Parent Subsidiary Directive
PwC	PriceWaterhouseCoopers

SPE	Special Purpose Entity
TIEA	Tax Information Exchange Agreement
UK	United Kingdom of Great Britain and Northern Ireland
PE	Permanent establishment
Vpb	Vennootschapsbelasting (Corporate Income Tax)
US	United States of America
UB WIB	Implementing decision on The International Assistance (Levying of Taxes) Act
UBO	Ultimate Beneficial Owner
Wet DB 1965	Wet op de dividendbelasting 1965 (Dividend Tax Act 1965)
Wet Vpb 1969	Wet op de vennootschapsbelasting 1969 (Corporate Income Tax Act 1969)
WIB	Wet op internationale bijstandsverlening bij de heffing van belastingen (The International Assistance (Levying of Taxes) Act)
Wtt 2018	Wet toezicht trustkantoren 2018 (Trust offices (Supervision) Act
Wwft	Wet ter voorkoming van witwassen en financieren van terrorisme (Money Laundering and Terrorist Financing (Prevention) Act

Overview of figures and tables

Figure 1: Incoming (left) and outgoing (right) FDI- 2019	16
Figure 2: Development of Dutch FDI position as share of total global FDI	18
Figure 3: Share of sector S.127 in total FDI assets (left) and liabilities (right)	26
Figure 4: Number of entities (left) and balance sheet size in billions of euros (right) by subsector	29
Figure 5: Balance sheet size by geography in billions of euros (average 2015-2019)	29
Figure 6: Incoming and outgoing income flows S.127 in billions of euros	30
Figure 7: Distribution of total income by entities and clusters - average 2015-2019	31
Figure 8: Geographical distribution of income flows S.127, average 2015-2019, in billions of euros	32
Figure 9: Percentage of total NL outgoing income flows by country of outflow and home country (average in the period 2015-2019)	34
Figure 10: Type of conduit company as a percentage of total	34
Figure 11: Number of tax treaties per country in 2020	37
Figure 12: Share of tax treaties with a zero withholding tax rate	38
Figure 13: Country comparison of withholding tax rates on dividends, interest and royalties	47
Figure 14: Comparison World Bank governance indicator Netherlands, EU and OECD - 2020	60
Figure 15: Number of S127 entities by type of representation	61
Table 1: Overview of adopted and announced tax measures	17
Table 2: Characteristics of SPEs and other captives	25
Table 3: Distribution by type based on average balance sheet size 2015-2019	33
Table 4: Country comparison of conditions of tax residence and certificate of tax residence	41
Table 5: Country comparison participation exemption	45
Table 6: Comparison of ruling practice between countries	49
Annex Table 8: Number of countries by country group and breakdown OFC's, LTJs and emerging markets	90
Sample structure 1	39
Sample structure 2	43
Sample structure 3	46
Annex example structure 1	91
Annex example structure 2	92
Annex example structure 3	93
Annex example structure 4	94
Annex example structure 5	95
Annex example structure 6	96
Annex example structure 7	97
Annex example structure 8	98

Summary

Introduction

In principle, multinational companies are free to arrange their internal organisation as they see fit and spread it over various jurisdictions. This freedom also allows multinationals to take advantage of the legal benefits of countries where they have (practically) no economic activities or to evade the laws and regulations of countries where they do.

This may relate to tax rules (to reduce the tax burden) but also civil law rules (such as rules on corporate governance or debt restructuring) or access to a bilateral investment treaty. There may also be other reasons for channelling financial flows through foreign entities, such as laundering criminally acquired assets.

Whether and to what extent the Dutch legal system is a desirable or undesirable facilitator in this respect has become the subject of increasing national and international attention. Against this background, the committee was asked to "investigate all aspects of the phenomenon of conduit companies and to advise on policy options as a result of this investigation."[1] Fifteen more specific questions were put to the committee as part of this remit. This report contains the results of that investigation and advice on the policy options.

In its approach, the committee was aware of the measures already taken in this field and has approached the issue not only from a national, but especially from an international perspective. In that perspective, the Netherlands is an outsider, with historically originated, exceptionally large conduit activities. But it is also recognised that the Netherlands is in the process of acquiring a normal position, with more attention to the international consequences of these conduit activities. The committee has looked for ways of maintaining and perhaps strengthening this tendency to further limit undesirable forms of conduit activities, taking into account the measures already in place and those announced, the effects of which are not yet fully visible. The international context is also in a state of flux, with an international agreement on a minimum tax on the profits of the largest multinationals possibly imminent, and the announcement of a new proposal for a directive by the European Commission. Viewed in this light, a proactive role for the Netherlands is both desirable and possible.

Definition

In common parlance, the terms "conduit companies", "letterbox companies", and other similar terms are used interchangeably. The committee concludes that adherence to the definition of 'conduit' and 'conduit companies' in the existing legislation and regulations leads to an excessively limited concept of a conduit that probably does not meet the expectations of parliament, the government or the wider public.

Therefore, the committee uses a number of characteristics. These are about international structures, transactions with affiliated parties, limited real presence (also referred to as *substance*) in the Netherlands, the presence of fiscal, financial or legal motives and large international money flows or balance sheet positions. The presence of some of these characteristics indicates a 'conduit' or a 'conduit company'. The characteristics used coincide to a large extent with the concept of "financial institutions and intra-group lenders" used in the statistics (S.127). This S.127 concept is therefore used for the quantitative analyses in this report.

[1] Article 3, first paragraph, of the Decree Establishing the Committee on Conduit Companies, Government Gazette 2021, 11844.

Analysis and findings

The committee has summarised the broad remit in the following five main questions, the conclusions of which are then briefly explained:

1. What is the extent of conduit activities and their contribution to the Dutch economy?
2. What are the tax motives for conduit activities in the Netherlands?
3. What are the non-tax motives for conduit activities in the Netherlands?
4. What is the relationship between money laundering and tax avoidance?
5. What is the effect of (recent) international developments?

1. What is the extent of conduit activities and their contribution to the Dutch economy?

Using data from the Dutch Central Bank (DNB), the committee mapped the extent of conduit activities in the Netherlands. In 2019, the Netherlands had approximately 12,400 conduit companies with a balance sheet total of approximately EUR 4,500 billion or 550 per cent of Gross Domestic Product (GDP). The interest, royalty and dividend payments that flow through these conduit companies annually amounted to an average of EUR 170 billion in the period 2015-2019. The size of the flows mentioned and the fact that incoming and outgoing flows are of the same order of magnitude confirms the existing image of the Netherlands as a transit country.[2][3] The fact that a relatively large proportion of these payments flowed from the Netherlands to low-tax jurisdictions, while the ultimate parent company is based in the United States (US), emphasises the relevance of tax motives.

Compared to their size, the importance of conduit companies for the Dutch economy is limited, both in terms of employment and tax remittance. Direct employment is estimated at three to four thousand jobs. The corporation tax[4] remittance of conduit companies is estimated at about EUR 650 million in 2019, or 0.2 per cent of total tax revenues. According to the committee, this is disproportionate to the adverse effects on other countries and thus on the reputation of the Netherlands. It is difficult to say exactly how much other countries miss out on in terms of tax revenue because of the conduit activities in the Netherlands. However, it is assumed that developing countries are especially sensitive to *treaty shopping* through the Dutch treaty network.[5]

2. What are the tax motives for conduit activities in the Netherlands?

The Netherlands has traditionally been fiscally attractive for international companies and also for conduit companies. The most relevant elements of the Dutch tax system that have made the Netherlands attractive for conduit companies, at least until recently, are the participation exemption, the extensive treaty network, the absence of withholding tax on interest and royalties and the practice of tax rulings. In combination with the well-organised financial advice and service sector, the Netherlands became a common intermediary for these elements to avoid withholding taxes elsewhere. For a long time, the government deliberately refrained from obstructing the emergence of this conduit practice.

To find out how the Netherlands currently compares to other countries in certain areas the committee commissioned an external study. This study shows that the Dutch system has not been unique in the abovementioned respects for some time; other countries (now) also have an extensive treaty network and a participation exemption.

---

[2] IMF (2021). Capital Income Taxation in the Netherlands. IMF Working Paper. Capital Income Taxation in the Netherlands (imf.org)

[3] CPB (2019). Doorsluisland Nederland Doorgelicht. CPB.nl

[4] Corporate Tax.

[5] Van 't Riet, Maarten and Arjan Lejour, 2020, "Dutch Tax Treaties and Developing Countries-a Network Analysis," CPB Note.

In addition, the Netherlands - partly following the European and global developments in this area - has recently taken and announced several measures to discourage certain forms of conduit activity as they are not (or no longer) considered desirable by the legislator. For example, a conditional withholding tax on interest and royalties was introduced as of 2021, the practice of tax rulings was tightened as of 1 July 2019, and the Netherlands aims to include a Principle Purpose Test (PPT) in all tax treaties. The effects of many of these measures are not yet visible in statistics but should be in the coming years.

The committee concludes that a certain 'policy stacking' has taken place recently while the effects of the measures taken are still largely unclear, partly because the relevant figures only become available after a number of years. That is not to say that there are no voids in what has been regulated or announced in the meantime, or that nothing can be said about the effectiveness of rules that have been introduced. For example, many Dutch companies have foreign shareholdings and only act as conduits for dividends and capital gains. This suggests that further measures could be taken to reduce unwanted use of the Dutch jurisdiction.

3. What are the non-tax motives for conduit activities in the Netherlands?
The committee's investigation shows that, in addition to tax rules, other factors play a role in the decision to establish a conduit company in the Netherlands. Experts interviewed by the committee point to the generally favourable business climate in the Netherlands, particularly the legal infrastructure, including the presence of knowledgeable service providers such as lawyers, civil-law notaries and tax consultants, and the quality of the judicial system. Also, the flexibility of Dutch company law compared to other countries appears to be a reason to establish a conduit company in the Netherlands. In addition, the bilateral investment treaties concluded by the Netherlands reduce the risk for investors abroad. The Netherlands is also sometimes chosen as a neutral jurisdiction to establish a conduit company, for example if two companies from two different relatively large countries decide to set up a joint venture.

4. What is the relationship between money laundering and tax avoidance?
Various elements associated with conduit activities, tax-driven or otherwise, are also relevant in the context of money laundering. The tax and investment climate can provide financial incentives for the proceeds of crime to flow through the Netherlands, just as it does for 'legal' conduits. In addition, money launderers may use conduit companies to disguise the origin of the assets and the identity of beneficial owners. Large-scale cash flows also offer money launderers the opportunity to merge their criminal transactions and cash flows into a larger, legal whole. The infrastructure of service providers, especially trust offices, which is associated with extensive conduit activities is susceptible to money laundering risks.

In recent years, various measures have been taken at both national and international level to combat money laundering. They include strengthening the role of the gatekeepers of the financial system as well as various other measures aimed at reinforcing the anti-money laundering chain. This includes improving the transparency of legal entities, including through the introduction of an 'ultimate beneficial owner' (UBO) register. Although many steps have been taken, the committee does see possibilities to improve the framework. The elements that provide opportunity for money laundering, as outlined above, can be discouraged by: i) promoting transparency among legal entities, ii) preventing abuses of and by service providers and iii) reducing the attractiveness of the Netherlands as a conduit country.

5. What is the effect of (recent) international developments?
The latest International Monetary Fund (IMF) figures on Foreign Direct Investment (FDI) run until the first quarter of 2021 and suggest a downward adjustment of conduit acticity volumes via the Netherlands. It cannot be ruled out that this is caused by international developments. Although the figures are certainly incomplete, they do not provide any basis to expect that conduit activities via the Netherlands have ended up on a structural downward path. Nor did the committee receive any indications of this in the interviews it has conducted.

The committee concludes that unilateral measures do not directly solve international tax avoidance and that stricter rules in the Netherlands are expected to lead to more conduit activities elsewhere. That would perhaps be good for the reputation of the Netherlands but not helpful for those countries that continue to miss out on tax revenue because of conduit activities. Therefore, the committee views the international initiatives in tax reform, tax harmonisation, and the fight against tax avoidance with interest. In addition, the initiative of the OECD Inclusive Framework[6] has recently gained momentum due to a changed position on the part of the USA, although its direct effect on conduit structures seems to be limited for the time being. Within the framework of the Communication on Company Taxation in the 21st century, the European Commission is also working on an initiative to 'combat the abuse of shell entities for tax purposes.' At the same time, the committee (on conduit companies) notes a changed attitude on the part of the Netherlands in the international discussion on tax avoidance, with a more proactive stance in the negotiations. The committee believes that tax avoidance and other undesirable forms of conduit activities are best tackled multilaterally. Nevertheless, meaningful steps can also be taken unilaterally on specific issues.

Framework for action, advice and recommendations

Although there may be legitimate reasons for setting up a conduit company, the committee concludes that some of the conduit activities through the Netherlands are driven by tax or investment protection and are undesirable from an international perspective. The committee concludes that the contribution of the conduit sector to the Dutch economy is limited and disproportionate to the lost tax revenues and risks of improper access to investment protection in other countries, especially developing countries. This is undesirable because of the possible consequences for those countries as well as bad for the Netherlands' international reputation and, accordingly, its negotiating position. Also, several elements associated with tax avoidance are susceptible to abuse by criminals.

The committee started out from a certain action framework to get a tighter grip on both the tax and non-tax driven conduit activities, especially on the large group of low-substance entities with little added value for the Dutch economy. The committee is aware of the (complicated) selection regarding these entities. It has sought ways to reduce the attractiveness of the Netherlands for low-substance entities, such as by increasing the proverbial "price tag" in a targeted manner. It looked at the tax burden, information exchange, administrative obligations, transparency, access to bilateral investment treaties, further research and monitoring.

The committee notes that many measures have already been taken at the national level to counter conduit activities, mainly in the area of taxation. Many measures have also been taken to combat money laundering and terrorist financing. However, it is not yet clear how effective the fiscal measures are at preventing conduit activities, partly because the effects are not yet visible in the (lagging)

[6] The OECD/G20 Inclusive Framework on BEPS was formed in 2016 to implement the measures from the OECD/G20 project to combat tax base erosion and profit shifting (the BEPS project) and further international cooperation on taxation. Within the Inclusive Framework, OECD member and non-OECD countries work together on an equal footing. The Inclusive Framework has 140 members at the time of writing.

figures. International agreements are also needed to prevent international tax avoidance through 'shell entities'. The Netherlands cannot do this alone but does have a responsibility to play a leading role, given the size of the financial flows through the Netherlands. Developments in this area have been accelerating for a few years now. This results in a combined uncertainty about the effectiveness of national measures already taken and the outcome of international negotiations in this area. This combined uncertainty can be seen as a reason for restraint in the recommendations for new measures and an opportunity for the Netherlands – as an important conduit jurisdiction - to send a clear signal.

In its advice the committee combines both these elements with the position that it is advisable to closely monitor the effects of the measures already taken and the outcome of the international negotiations. The committee recommends that the Netherlands adopt a constructive and, where possible, initiating attitude towards current international initiatives.

However, the committee certainly sees opportunities for measures in the areas of increased transparency, strengthened supervision and reporting requirements.

The committee further recommends that a clear signal be sent internationally that the Netherlands is taking its responsibility seriously and will continue to actively work to reduce the flow of money through the Netherlands (even if this is not yet evident from the statistics), and that, in addition to the measures already taken, a number of additional fiscal measures should also be pursued. For example, it could be investigated, preferably at the European level, whether the application of tax benefits such as the participation exemption can be restricted in a targeted manner for low-substance conduit companies. In any case, the tax transparency of conduit companies can be increased, for example by actively exchanging information on conduit companies with foreign countries.

The committee also recommends increasing the transparency of legal entities to prevent abuse by further tightening up the UBO concept in certain respects and making adjustments to the UBO register. It is also important to advocate internationally for the introduction of public UBO registers. Furthermore, the limited requirements for preparing financial statements, which currently apply to many conduit companies, can be brought more in line with the reporting requirements for legal entities with substantial economic activities. The committee also recommends that stricter action be taken against trust and company service providers that evade the requirements of the Trust Offices (Supervision) Act 2018 (Wtt 2018), so called 'illegal' trust offices, and that capacity and resources be made available for this purpose. The Netherlands could also put more effort into international cooperation to effectively combat the improper use of Dutch legal entities for money laundering and other criminal activities. Finally, the committee recommends that the relationship between conduit activities and money laundering be further investigated by the Financial Expertise Centre (FEC), a partnership between the authorities involved.[7]

[7] The FEC is a collaborative effort involving the Authority for the Financial Markets (AFM), De Nederlandsche Bank (DNB), the PPS, the Police, the Financial Intelligence and Investigation Department (FIOD), the Tax and Customs Administration and the Financial Intelligence Unit-the Netherlands (FIU-NL).

Overview of tax and non-tax policy measures

Tax	Non-tax
Taxation • The removal of the safe harbour for interest and royalty conduit activities.	**Transparency of UBOs** • Tighten up the obligations where 'senior management' is designated as UBO. • Make currently public data in the UBO register more easily searchable • International introduction of UBO registers with public data.
Information exchange • Extension of the spontaneous exchange of information on companies. • Spontaneous exchange of information in the case of exempted gains on disposal.	**Financial statements** • Deletion of the exceptions in Article 2:403 of the Dutch Civil Code. • When determining the size of a company, always include data from holdings and, if relevant, financial income.
International • Extension of the PPT to the entire tax treaty (if not multilaterally regulated). • A proactive stance on the forthcoming EU directive proposal on shell entities. • A clear interpretation of the EU anti-abuse principle.	**Monitoring and Investigation** • Tighten approach to combatting illegal trust services. • Follow-up research on money laundering and conduit activities. • Intensifying international cooperation in countering criminal conduit activities.
	Bilateral investment treaties • Deny conduit companies access to bilateral investment treaties.

1 Introduction

1.1 Terms of Reference

The Committee on Conduit Companies was established in response to a request of Dutch Members of Parliament Omtzigt (CDA at the time) and Van Weyenberg (D66) during the plenary debate held on 8 September 2020 on the Bill on the Taxation (Miscellaneous Provisions) Act 2020 (Fiscale Verzamelwet 2020), which has since passed into law.[8] As a follow-up to the work of the Multinational Tax Committee, the intention was to set up an independent committee to look into the issue of 'conduit companies'.

The committee's remit was to "*study the phenomenon of conduit companies in all its aspects and advise on policy options based on this study*."[9] This request for advice includes fifteen subquestions which focus on tax issues, but which also call for attention to the issues of 'non-taxation' and 'money laundering'.[10]

The Committee has clustered these subjects in the following five main questions, the content of which is dealt with in Chapters 3 to 6:

1. What is the extent of conduit activities and their contribution to the economy?
2. What are the tax motives for conduit activities in the Netherlands?
3. What are the non-tax motives for conduit activities in the Netherlands?
4. What is the relationship between money laundering and tax avoidance?
5. What is the effect of (recent) international developments?

The remainder of this chapter outlines the broader social and international context in which the Committee advises. This is followed by an explanation of the Committee's investigative approach.

1.2 Context

Social context

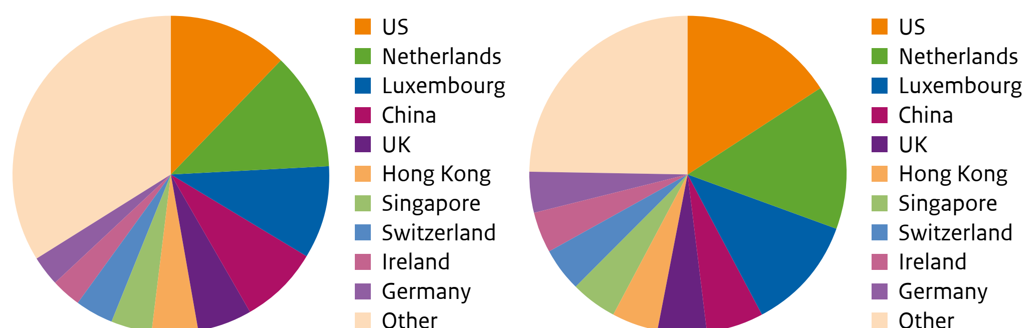
In principle, companies are free to design their internal organisation and corporate structure as they see fit and spread it over various jurisdictions. This freedom also allows multinationals to take advantage of the legal benefits of countries where they have (practically) no economic activities or to evade the laws and regulations of countries where they do. This may involve tax rules (reduction of the tax burden), but also civil law rules (for example, rules on *corporate governance* or debt restructuring) or treaty protections, as provided by bilateral investment treaties. This freedom can also be used by ill-intentioned parties, such as criminals who set up international structures to launder illegally acquired assets.

Recent years have seen a decline in public tolerance for 'having the benefits but not the burdens' attitude of certain users of conduit structures. This is partly due to the continuous negative reporting on conduit structures, partly in response to sensational leaks such as the Panama Papers. It also casts a negative light on countries that facilitate such structures. In this context the Netherlands is high on the list of conduit countries or tax-havens. For example, the Netherlands is in fourth place on the Tax Justice Network's Corporate Tax Haven Index.[11] This is not so much because the Netherlands is a classic tax haven with no, or a low, statutory rate for corporation tax, but mainly because a large part of global foreign direct investment (FDI) flows through the Netherlands (see Figure 1). The exceptionally high FDI position of the Netherlands in relation to the size of the Dutch economy is an

[8] Parliamentary Papers II 2019/20, 35 437, no. 98-25, p. 10.
[9] Article 3, first paragraph, of the Decree Establishing the Committee on Conduit Companies, Government Gazette 2021, 11844.
[10] For the complete list, see: Parliamentary Papers II, 2020/21, 32140, no. 83.
[11] Corporate Tax Haven Index 2021 (taxjustice.net).

indication that the Netherlands is a popular conduit country for parties wishing to avoid taxation.[12] This role as a conduit country also has an impact on other countries. For example, it is estimated in the literature that other countries have lost more than 20 billion euros a year in tax revenues due to conduit activities through the Netherlands.[13] Developing countries are particularly sensitive to the consequences of *treaty shopping* via the Netherlands.[14] All of this adds to the public call for more measures against conduit and tax avoidance activities through the Netherlands.

Figure 1: *Incoming (left) and outgoing (right) FDI- 2019*



Source: IMF CDIS database

International context

Internationally, initiatives around tax harmonisation and combating tax avoidance have accelerated. As a follow-up to the OECD/G20 BEPS[15]project, the OECD/Inclusive Framework, in the context of taxation in the digitising economy, continued to look at adjustments to the internationally accepted conventions on the taxation of large multinationals. The discussions on what is known as pillar 2 touch on the conduit problems that this report investigates. Pillar 2 focuses on measures to ensure that large internationally operating companies pay a minimum level of tax. If countries to which the taxing right is initially allocated - based on the traditional approach in combination with the measures from pillar 1 - levy too little profit tax, other countries must be able to levy up to an agreed minimum level. The EU has also taken steps towards tax harmonisation in recent years, including the Anti-Tax Avoidance Directive and the European Committee's recent initiative in the context of the Communication on Company Taxation in the 21st Century to 'tackle the abuse of shell entities for tax purposes'.[16]

The Netherlands is regularly called to account by organisations such as the IMF, the OECD and the European Committee for its international position as a conduit country. For example, these organisations recently referred to the Netherlands as "*a major conduit*" (IMF, 2021)[17] and "[A country

[12] Lejour, Möhlmann & van 't Riet (2019). Doorsluisland Nederland doorgelicht. CPB Policy Brief.

[13] Lejours (2020) estimate of € 22 billion is based on the estimated globally forgone corporation tax revenue from previous studies, which is allocated to the Netherlands based on its share of global FDI. Tax Justice Network (2020) uses a different method that compares profits reported by companies against theoretically expected profits based on the labour and capital present in a country, and estimates the lost tax revenue at 26.6 billion euros.

[14] Van 't Riet & Lejour (2020), Dutch Tax Treaties and Developing Countries-a Network Analysis, CPB Note

[15] Base Erosion and Profit Shifting.

[16] Communication on company taxation in the 21st century, COM (2021) 251 (final).

[17] IMF (2021). Capital Income Taxation in the Netherlands. IMF Working Paper. Capital Income Taxation in the Netherlands (imf.org)

with] *tax rules that are used by companies that engage in aggressive tax planning*" (EC, 2020)[18] and "*a reputational issue linked to aggressive tax planning*" (OECD, 2021).[19] Such a reputation can affect the Dutch international negotiating position and the investment climate in the Netherlands, such as the termination of the tax treaties with the Netherlands by Russia and Mongolia or the termination of the bilateral investment treaties by Indonesia and South Africa. Such a reputation can also contribute to a decline in domestic tax ethics of both small businesses and citizens. Against this background, the Netherlands has recently taken various measures to reduce the conduit activities via the Netherlands. Table 1 provides an overview of the most prominent tax measures, of which the conditional withholding tax on interest and royalties is the most recent[20]. However, the effect of these measures is not yet clearly reflected in the FDI figures. Although the Dutch share of global FDI declined slightly in the first quarter of 2021 (see Figure 2), it is still too early to conclude that there has been a trend reversal.

In their most recent reports, the international organisations referred to above mention the positive change of course and constructive attitude of the Netherlands in the international tax arena, or in the words of the IMF: "*The Netherlands has undertaken several concrete measures and made public announcements, in a clear political signal, to reduce the potential spillovers of its international corporate tax system on tax bases of other countries*".

Table 1: *Overview of adopted and announced tax measures*

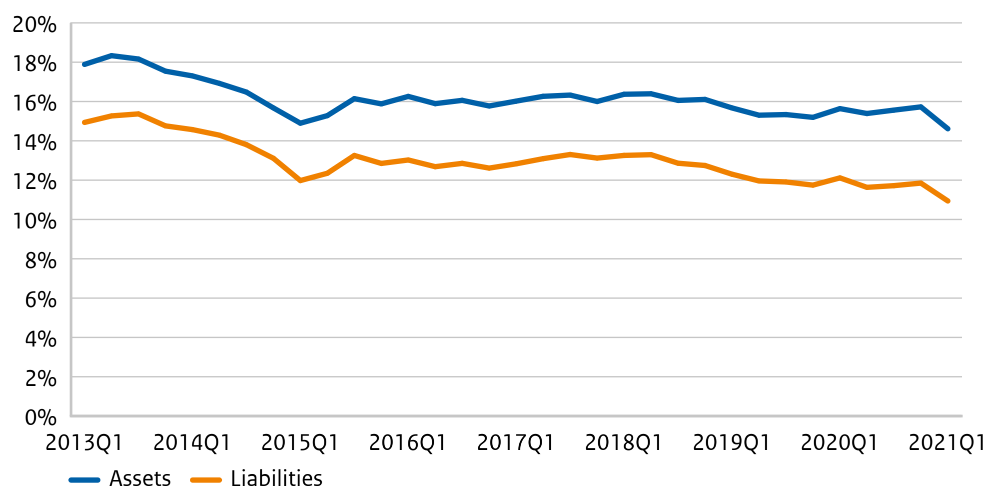
Year	Measure
2001	Introduction of the APA/ATR policy (no more standard rulings)
2002	Tightening of the actual presence and risk requirements for service providing entities (Section 8c Corporate Income Tax Act 1969)
2013	Inclusion of anti-abuse clauses in treaties with developing countries
2014	Spontaneous exchange of information on service providing entities (Article 3a of the Implementing Decree on the Income Tax Act)
2018	Withholding obligation for holding cooperatives
2019	Renewed ruling practice (economic nexus required)
	Publication of ruling summaries
2020	Revocation of limited partnersship/private limited company (CV-BV) decree PPT to prevent the abuse of tax treaties
2021	Conditional withholding tax on interest and royalties
2024	(announced) Additional conditional withholding tax on dividends

[18] Council Recommendation on the National Reform Programme 2020 of the Netherlands, including a Council opinion on the Stability Programme 2020 of the Netherlands: EUR-Lex - 52020DC0519 - EN - EUR-Lex (europa.eu)

[19] OECD (2021). Economic Surveys: Netherlands. June 2021. https://www.oecd.org/economy/surveys/Netherlands-2021-OECD-economic-survey-overview.pdf

[20] See the fact sheet on measures to increase transparency and integrity, for example, measures against tax evasion and tax avoidance: Fact sheet on measures against tax avoidance and tax evasion, 4 March 2021.

***Figure 2:** Development of Dutch FDI position as share of total global FDI*



Source: IMF IIP database

1.3 Research approach

Earlier research into conduit activities shows that it is difficult to delineate this concept satisfactorily and make it quantitatively clear. Furthermore, it is methodologically complex to explain the estimated size of conduit activities by tax or non-tax motives. This is all the more true of investigating (the extent of) criminal financial flows in relation to tax evasion, as crime by its very nature is hidden and complex and professionally constructed concealment schemes are often used, particularly in the case of money laundering. An additional complicating factor in investigating criminal money flows through the Netherlands is that they often have a foreign origin, with the predicate offences usually taking place abroad as well, so that the Dutch authorities have limited insight into them.

Against this background, the Committee made use of various quantitative and qualitative sources in its investigation. First of all, the committee members were asked to submit *position papers*. There were also roundtable discussions on tax, non-tax and money laundering issues with relevant stakeholders. The opportunity was given to submit *position papers*. In this context, the Committee held talks with representatives and experts from various parties, including service providers, consultants, the business community, non-governmental organisations (NGOs), public parties in the supervision and criminal law chain and relevant parties within central government. Apart from these round-table discussions, the Committee also held talks with various experts, such as members of the notarial profession and the Netherlands Foreign Investment Agency (NFIA). The Committee also carried out desk research, including a literature study based on, among other things, reports by the IMF, OECD and FATF, and an analysis of policy documents and legislation and regulations. In addition, analyses were made in response to media reports concerning the various 'leaks', the large-scale data leaks about tax avoidance and evasion via tax-havens.

To better understand how the Dutch tax system compares with that in other countries, the Committee commissioned an external study into the relevant elements of the tax system in some other countries. This analysis was performed by PricewaterhouseCoopers (PwC) and validated by the International Bureau of Fiscal Documentation (IBFD). Both documents are included as appendices to this report. The Committee has set out to conduct a similar, comparative external study of non-tax factors - particularly corporate law - among law firms and professors, but this has not yielded the desired result.

The committee has also made use of quantitative analyses provided by DNB, which is responsible for compiling the statistics for the sub-sector "*Financial institutions and intra-group credit providers*" (see Box I), the statistical definition of conduit entities used in this report. This concerns analyses concerning numbers, balance sheet totals and income flows by geographical distribution. To gain an insight into the extent of conduit activities outside sector S.127, the CBS made a rough estimate of the conduit activities through non-financial companies. Finally, in cooperation with the Anti Money Laundering Centre (AMLC) with data from DNB and support from iCOV, an analysis was made of the degree of (over)representation of S.127 conduit companies in 'leaks', such as the 'Panama Papers'.

2 What is a conduit company?

2.1 Introduction

As indicated in Chapter 1, the Committee has been tasked with "studying the phenomenon of conduit companies in all its aspects and advising on policy options based on this study". Part of this is the question 'what interpretation should be given to the concept of a conduit company?[21] This chapter addresses this sub-question.

In common parlance, the terms "conduit companies", "letterbox companies", and other similar terms are used interchangeably. There is a certain idea of a conduit or letterbox company concept, but no fixed definition. A conduit company is often thought of as an entity without its own staff, office or other significant presence (also known as 'substance') established in a particular country primarily for tax or legal reasons. As a rule, the activities of such entities consist of receiving and paying substantial flows of money from and to foreign countries.

This chapter begins with an overview of the various existing terms in legislation and regulations (section 2.2). Next, it is argued why this report assumes a broad concept of 'conduit company' based on a number of characteristics (section 2.3). Finally, the statistical definition used is explained, and how it relates to the characteristics from the previous section (Section 2.4) is discussed.

2.2 Terms in legislation and regulations

Conduit companies

The term 'conduit company' is defined as such in the Trust and company service providers (Supervision) Act (Wtt 2018), as offering a conduit company is one of the services that qualifies as a 'trust service'. Section 1 of the Wtt 2018 defines a conduit company as:

> *"a legal person or company belonging to the same group as the one that uses that legal person or company to provide the trust service referred to in subsection (c) of the definition of a trust service."*[22] The trust service in subsection (c) is described as *"the use of a conduit company for the benefit of the client."*

This is therefore a very narrow definition that only includes companies belonging to the same group as a trust and company service provider. The number of conduit companies meeting this definition has fallen sharply in recent years. Only four conduit companies active in the Netherlands on 31 December 2019 met this statutory definition. A recent bill to amend the Wtt 2018 seeks to prohibit conduit companies as defined in the Wtt 2018. The definition in the Wtt 2018 is therefore not sufficient for a complete examination of the phenomenon of conduit companies.

Target companies

The Wtt 2018 also includes the term 'target company'. These are companies that make use of the services of a trust and company service provider. These are usually entities with a branch address at the trust and company service provider, with little or no substance in the Netherlands other than the services provided by the trust and company service provider. However, not all low-substance entities use the services of a trust and company service provider.[23] Conversely, not all target companies are part of an international corporate structure. Therefore, this term from the Wtt 2018 is also inadequate for this broader investigation.

---

[21] Parliamentary Papers II, 2020/21, 32140, no. 83.

[22] A new definition is offered in the proposal to amend the Wtt 2018 submitted for consultation: *"For the purposes of this Article, a conduit company means a legal entity or company with no economic activity, which is used for the benefit of one or more third parties who do not belong to the group to which the legal entity or company belongs, and whose use is not for the purpose of complying with any legal obligation."*

[23] See Figure 5.2. 60-65 per cent of conduit companies are represented by a trust and company service provider.

Service entities

There is no definition of 'conduit company' or 'letterbox company' in tax law. However, the term service providing entities is used. Service providing entities are defined in the Decree of 3 June 2014, DGB 2014/3101 (Service entities and certainty in advance) as:

> *"entities with intra-group financial services activities (hereinafter: service providing entities) domestic taxpayers as referred to in Article 3a(1) of the Uitvoeringsbesluit internationale bijstandverlening bij de heffing van belasting" [Implementing decree on international assistance (levying of taxes) Act]*

These domestic taxpayers are described in Article 3a, paragraph 1, of the Implementing decree on international assistance (levying of taxes) Act as:

> *"Domestic corporate taxpayers whose activities in any year consist primarily of the direct or indirect receipt and payment, in law or in fact, of interest, royalties, rent or lease payments, under whatever name and in whatever form, from or to entities not resident in the Netherlands that belong to the group of which the taxpayer is a member."*

This includes companies whose activities consist primarily - at least 70 per cent - of the receipt and continued payment of interest, royalties, rental or lease payments. To assess this, factors such as the types of assets and liabilities on the balance sheet, turnover, the activities from which the profit is derived, the time allocation of employees, etc. play a role. Taxpayers must indicate in their annual corporate income tax return whether they have engaged in international holding, licensing, rental, leasing or financing activities within the group. The definition of service providing entity better fits the purpose of the study but is not comprehensive enough. The receipt and payment of dividends, for example, is not included.

Low-substance entities

A conduit company is often thought of as an entity with little substance. Concrete requirements have been formulated to determine whether a service providing entity has sufficient substance. If a service providing entity has insufficient substance, information about this substance is spontaneously exchanged with the tax authorities of the country from which interest, royalties, rental or lease payments are made (the source country). The substance requirements are listed in Article 3a(7) of the International Tax Assistance (Implementation) Decree (Uitvoeringsbesluit internationale bijstands-verlening, UB WIB) on the levying of taxes:

> *"a. at least half of the total number of the taxpayer's statutory and decision-making board members reside or are actually domiciled in the Netherlands;*
> *b. the members of the management board who reside or are domiciled in the Netherlands have the professional knowledge required for the proper performance of their duties, which duties include at least deciding, on the basis of the taxpayer's own responsibility and within the framework of the normal concern of the group, on the transactions to be concluded by the taxpayer, and ensuring that the transactions are properly concluded;*
> *c. The taxpayer has qualified personnel for the proper execution and recording of the transactions to be entered into by the taxpayer;*
> *d. the management decisions are taken in the Netherlands;*
> *e. the main bank accounts of the taxpayer are held in the Netherlands;*
> *f. the accounts are kept in the Netherlands;*
> *g. the taxpayer has a wage bill that constitutes remuneration for the activities referred to in the first paragraph, which is at least equal to EUR 100,000;*
> *h. the taxpayer has at his disposal for a period of at least 24 months real estate or part of real estate situated in the Netherlands, in which real estate or part thereof has an office equipped with the usual facilities for carrying out the activities referred to under g, and the activities are actually carried out in that office;*

i.the taxpayer bears a real risk as referred to in section 8c, second paragraph, of the Corporation Tax Act 1969 *with respect to the monetary loans or legal relationships and the related monetary loans or legal relationships underlying the interest, royalties, rent or lease instalments received and paid*
j.the taxpayer has at least an equity capital appropriate to the actual risk referred to in subsection i."

These requirements are referred to in various places in tax legislation and regulations, both about entities established in the Netherlands and entities established abroad. For the application of the Principal Purpose Test (PPT) - based on which treaty benefits can be denied if it can reasonably be concluded that obtaining this benefit is one of the principal reasons for a construction or transaction - these requirements can also constitute a signal of abuse (see also section 4.3). Nevertheless, for the PPT, substance is a relatively concept. If the substance requirements are not met, this has no consequences for the taxation in the Netherlands except possibly for the profit attributable to the company concerned. It is up to foreign countries to attach tax consequences to this. The substance requirements are not sufficient for defining the concept of a conduit company, as conduit activities can also take place through entities that would (just about) have sufficient substance. Nevertheless, much of the flow is through low substance companies.

It follows from the above overview that, given the broad scope of its duties, the Committee cannot use existing concepts in legislation and regulations for an adequate interpretation of the concept of a conduit company.

2.3 Assessment on the basis of characteristics

The Committee takes as its starting point an interpretation of the concept of a 'conduit company' that goes beyond the comparable concepts referred to above in legislation and regulations. A more limited definition of a conduit company would not be in keeping with the Committee's terms of reference or the intentions of the resolutions of the House of Representatives.

In this context, the Committee notes that the Netherlands is regularly cited - and not in a favourable sense - as one of the countries in the world with very high FDI ratios from abroad to the Netherlands and from the Netherlands to other countries, in relation to its GDP.[24] FDI from abroad in the Netherlands consists of participations (equity interests) in, and receivables from affiliated companies on, Dutch entities. The Netherlands' foreign FDI consists of, among other things, participating interests in, and debt-claims of Dutch entities on, foreign (subsidiary) companies.

However, having participations and receivables in and by Dutch companies does not necessarily mean that these entities always have large, regular incoming and outgoing flows of fiscally relevant funds.[25] In view of the broad concept of the term 'conduit companies' in the social and political debate, the Committee has examined the entire group of Dutch companies with little or no substance, even if money does not regularly flow through them.

The research question included[26] what influence bilateral investment treaties have on the decision of multinational groups to use a company in the Netherlands. In such a situation, there is not always a flow of income from and to foreign countries, but the use of a Dutch company with no or little substance may be motivated by the desire to invoke the protection of an bilateral investment treaty and to submit an investment protection claim to a foreign government.

[24] IMF (2021). Capital Income Taxation in the Netherlands. IMF Working Paper. 2021/145.
[25] Inbound and outbound dividends, interest and royalties are particularly relevant for taxation.
[26] In the Explanatory Memorandum to the Decree establishing the Committee on Conduit Companies.

On the other hand, distributing company profits to shareholders or paying interest or royalties *only* to related parties - i.e. without first having received them from other related parties - should not by definition be included in the concept of 'conduit'. While payments to related parties may be tax-driven, not all forms of tax planning involve channelling funds through Dutch companies. For example, the limited partnership/private limited company (CV/BV) structure (the tax attractiveness of which has been terminated partly due to the hybrid mismatch measures) was not always used to 'channel' money flows via the Netherlands without (direct) taxation. This structure was also set up to reduce the taxable profits from the active Dutch company of a private limited company by making business payments[27] to a limited partnership contracted under Dutch law but not liable for taxation in the Netherlands. The latter situation certainly involved tax avoidance. It often concerned the reduction of company profits taxable in the Netherlands[28] without the corresponding benefit being directly taxed elsewhere, reducing the worldwide tax burden. This did not primarily involve directly channelling funds through Dutch companies.

Given the wide range of views on what should come under 'conduit' and 'conduit companies', the committee notes that there is no clear and conclusive definition of this concept that does justice to the phenomenon of conduit companies in all its aspects. In the Committee's opinion, the assessment of the existence of a conduit company should be made based on a number of characteristics.

The characteristics are as follows:
1. There is a Dutch entity (i.e. an entity incorporated or entered into under Dutch law, or an entity incorporated under the law of another country and actually located here) that is part of an international structure. Although the term 'company' is often used, it does not necessarily have to be a company within the meaning of the Dutch Civil Code (BW) - such as a public or private limited company. A conduit company can also have another legal form, such as a cooperative or a foundation, or be a legal person incorporated under foreign law and established in the Netherlands, or another type of legal entity.
2. The Dutch entity's transactions are (mainly) with (directly or indirectly) related parties.
3. The Dutch entity has no actual presence in the Netherlands (e.g. no own office and domiciled at a trust and company service provider) or only a limited presence (e.g. a small office with only a few employees).
4. In the international structure, use is made of the Dutch entity to obtain one or more financial, fiscal, legal or other benefits.
5. Substantial amounts flow through the Dutch entity from and to foreign countries. Cash flows in this context refer to dividends, interest, royalties, rental or lease payments. These need not be annual income streams. Apart from the above cash flows, there are no substantial business activities in the entity (and in the Netherlands).
6. The Dutch entity has substantive balance sheet positions, for example several participations in foreign subsidiaries with a high book value.

The presence of some of these characteristics indicates a 'conduit' or a 'conduit company'. Therefore, not all these characteristics need not be present. Holding companies with foreign subsidiaries and a foreign parent (or foreign portfolio shareholders) through which no dividend flows for several years, for example, are also covered. Whether there is a conduit company therefore depends on the facts and

[27] The business expenses were and are determined by the Tax and Customs Administration in accordance with the 'at arm's length principle' (Section 8b of the 1969 Corporate Income Tax Act) tested for acceptability of deduction from Dutch profits.

[28] The limited partnership was transparent for tax purposes under Dutch law and the managing partners were located outside the Netherlands. The US considered the limited partnership to be a corporate body for tax purposes but not liable for tax in the US.

circumstances of the case. The concept is considered neutral in itself; whether a particular conduit company or conduit should be considered undesirable is the next question.

2.4 Definition for statistical purposes

The definition of a conduit company is also important to charting in figures the financial flows and positions of the entities in the Netherlands that qualify as such. The characteristics listed above coincide to a large extent with the concept of "financial corporations and intra-group credit institutions" (sector S.127) used in the statistics, as explained below.

Financial corporations and intra-group lenders' (S.127)

Within the European System of Accounts (ESA 2010), 'conduit companies' characteristics described in section 2.3 are mainly observed in the sub-sector 'Financial corporations and intra-group credit institutions' (S.127).[29] Within the ESA, this sub-sector is defined as follows:

> *'all financial institutions and quasi-corporations, not engaged in financial intermediation or the provision of financial auxiliary services [in other words not banks, insurance companies, pension managers, investment advisers, etc.] and the majority of whose assets or liabilities are not traded in open markets.*

Within the subsector S.127, DNB[30] distinguishes between *Special Purpose Entities* (S.127.a, also known as SPEs)[31] and other intra-group financial services companies (S.127.b, also known as other *captives*):

1. **SPEs (S.127.a)**
   This concerns entities with a foreign ownership that mainly receive financial flows in the form of dividends, interest and royalties from abroad and subsequently pay these dividends, interest and royalties to the foreign country. For determining S.127a entities, since 2020 DNB has followed the internationally accepted IMF definition of SPEs under which these entities have a maximum of five employees, no or little physical presence and no or little physical production in the country of domicile.

2. **The other captives (S.127b)**
   These entities provide intra-group financial services and are therefore not engaged in financial intermediation for (intermediary) or the provision of services to third parties. The assets and liabilities of these entities consist largely of interests in or receivables from group companies in the Netherlands or abroad, and of liabilities to group companies. Another captive could be, for example, a holding company that mainly holds equity investments on its balance sheet, but does not manage, provide administrative or other services to the subsidiaries concerned. Another example of a captive is a finance company that raises money from the market (e.g. by issuing securities) and lends it on to its group companies. Entities that lend parent company finance on to group companies also fall into this category.

SPEs and other captives differ in their economic presence in the Netherlands. By definition, SPEs have a minimal impact on the Dutch economy, with gross income streams adding up to virtually zero net. Retained earnings of Dutch SPEs are usually attributed to foreign parent companies and regarded

---

[29] Regulation (EU) of the European Parliament and of the Council of 21 May 2013 on the European system of national and regional accounts in the European Union, No. 549/2013

[30] In the Netherlands, DNB is responsible for observing and compiling statistics on this sector. In cooperation with the CBS, a questionnaire is periodically sent to 13,000-14,000 entities for this purpose.

[31] A specific part of the SPEs - the securitisation vehicles - is not included in the sector 'Financial corporations and corporate lending' (S.127) but in the sector 'other financial intermediaries' (S.125) and therefore falls outside the scope of this report.

as an outgoing income flow. The other captives have a more substantial influence on the Dutch real economy, for example, through Dutch subsidiaries or because they generate net income flows to the Netherlands as a (listed) top holding company. To the extent that these profits from top corporations are not distributed to external shareholders, they contribute to Dutch Gross National Income (GNI). In addition, SPEs always concern a Dutch entity that forms part of a structure with a foreign owner. Although this also applies to the majority of the other captives, both groups also include some holding companies of Dutch multinationals and foreign multinationals that have chosen a Dutch public limited company as their legal form. For both categories of entities, there are significant financial flows to, or balance sheet positions in, foreign countries, as section 3.4 shows.

When the characteristics of conduit companies mentioned in section 2.3 are compared with the definitions of SPEs and other captives, they largely correspond. In a simplified diagram, this looks as follows:

Table 2: *Characteristics of SPEs and other captives*

No.	Key features	S.127a	S.127b
1	Part of international (foreign) group/structure	+	+/-
2	Transactions (e.g. granting a loan) take place with related parties.	+	+
3	Low actual presence	+	+/-
4	The entity takes advantage of one or more tax or legal benefits in the Netherlands.	+	+
5	Significant financial flows flow through the entities.	+/-	+/-
6	The entity has significant balance sheet positions in relation to affiliated foreign entities.	+	+

Statistics on SPEs capture only low-substance entities and are therefore 'pure' in the context of conduit activities. This is also why this definition has been used in relevant studies into the role of the Netherlands as a conduit country up to now.[32] This was also why the State Secretary for Finance - Taxation and Customs Administration indicated that, when monitoring the effects of the conditional withholding tax on interest and royalties to Low-tax jurisdictions (LTJs) introduced on 1 January 2021,[33] and in abuse situations, use would be made of DNB's data on the financial flows that pass through the Netherlands via Special Purpose Entities (SPEs) or Special Financial Institutions (SFIs).[34]

At the same time, the SPEs provide an incomplete picture regarding the total scale of conduit activities through the Netherlands. Given the low materiality threshold in economic contribution, other captive insurance companies may also be subject to significant conduit activities, for example if they are established here through relatively small non-financial subsidiaries.[35] Moreover, since 2020, DNB has been forced to align itself with the internationally recognised operationalisation of the concept

32 The reasons for establishment in the Netherlands, the tax motives and the economic importance of SFIs are described in detail in the 2013 report 'Uit de schaduw van het bankwezen' (out of the shadow of the banking sector) by SEO Economic Research. See also SEO, Balance sheets, income and expenditure of SFIs, 2018.

33 A low-tax jurisdiction is understood in this report to be the same as in the Withholding Tax Act 2021: a state with a statutory tax rate on profits of less than 9 per cent or a state included in the EU list of non-cooperative jurisdictions for tax purposes. The list of low-tax jurisdictions is updated annually. The list used for the statistics in the report is given in Annex 3.

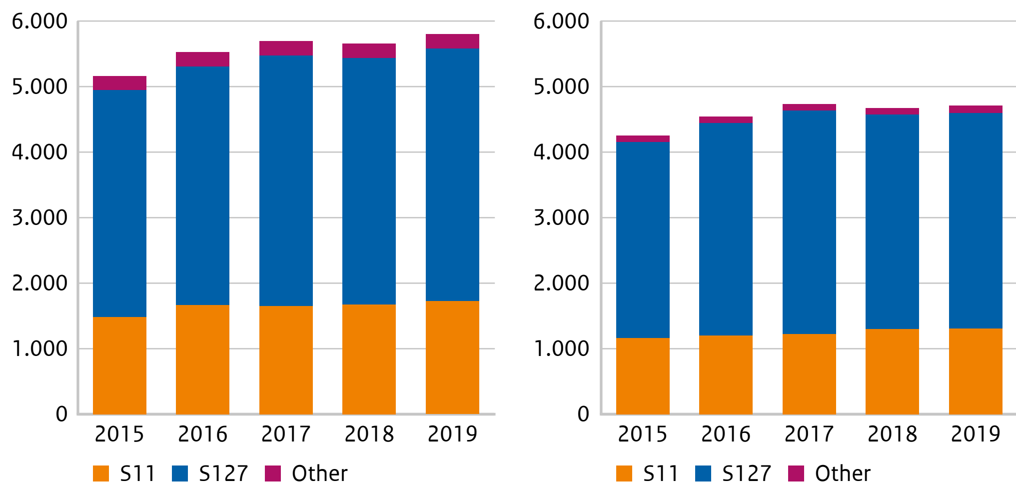
34 It should be noted that the definition of SPEs/SFIs has not remained constant over the years. For example, until 2018 the SFIs included mixed forms, which have now moved to the S.11 sector. As such, the population of SPEs is not directly comparable to that of pre-2018 SFIs.

35 See also: Decrease in activities of smaller SFIs in particular', DNB 2020.

of SPE. As this definition is narrower, a significant part of the original captive SFI population shifts to the other captives, which would risk falling out of scope. To obtain a more complete image of the conduit activities through the Netherlands, the Committee therefore chooses to focus on the entire S.127 category in this report. Where possible, the figures for the other captives have been adjusted for entities that are part of Dutch multinationals and foreign multinationals with a public limited company as their top shareholder.

Figure 3 shows that over two-thirds of FDI liabilities in the Netherlands and Dutch FDI assets abroad are accounted for by sector S.127. Foreign liabilities exceed foreign assets because there are entities in the (S.127B) population that are holding companies over a non-financial corporate structure in the Netherlands. In this situation, the assets are usually domestic, while the ultimate ownership (i.e. liabilities) lies abroad. The fact that FDI positions attributed to the S.11 sector are almost twice the size of GDP is an indication that conduit activities are also taking place in the non-financial company sector. This is because conduit activities do not play a primary role in the statistical classification of a company, while foreign multinationals may also use a Dutch subsidiary with non-financial activities as a conduit. The more hybrid nature of conduit entities in S.11 makes the precise conduit activities more difficult to identify. At the Committee's request, CBS therefore made a rough estimate of the conduit activities within this sector. In this estimate, conduit is defined as the part in the outgoing income flows of foreign non-financial corporations financed by an incoming flow from abroad.[36] Technically, such flows are not necessary for the functioning of Dutch non-financial corporations. At the same time, however, this assumption probably represents an overestimation of the actual flow and is therefore best interpreted as a maximum. Based on the CBS estimate, it can be concluded that the conduit activities through non-financial entities (S.11) is at most one-fifth of the total.

***Figure 3:** Share of sector S.127 in total FDI assets (left) and liabilities (right)*



Source: DNB, integrated balance of payments data

[36] This is an estimate of the dividend, retained earnings and total (i.e. both intra-group and external) interest flows. Unfortunately, no data is available for royalty flows for sector S.11. The micro data used is raw micro data from, among others, the Statistics on the Financial Position of Large Corporations, and therefore cannot be compared unambiguously with the integrated results from the national accounts. As a result, these figures have a larger margin of uncertainty. However, checks with other data sources show that the figures can be interpreted in terms of an order of magnitude of the underlying flows.

3 Dear flow in figures

3.1 Introduction

As indicated in the previous chapter for the concept of conduit companies, the Committee follows the statistical sector S.127 - 'Financial corporations and intra-group credit institutions' - as included in the European translation (ESA2010) of the United Nations Manual of National Accounts (SNA2008). This chapter provides a further insight into the number of entities covered by this definition and the tax-relevant income flows related to these entities. A typology based on balance sheet data will also be introduced to gain a clearer image of the diversity within this group of S.127 entities. The importance of this sector to the Dutch economy is then discussed in terms of both employment and tax payments. The figures in this section are based on both integrated sector statistics and more finely-meshed microdata from DNB for sector S.127, with 2019 as the latest available year. The data used is further explained in Box 1.

Box 3.1: explanation used data

DNB has a statistical task under the Banking Act: the collection of statistical data and the production of statistics. To this end, DNB is working closely with Statistics Netherlands (CBS) to improve the quality of its statistics more efficiently. Within this partnership, the mutual comparative advantages are exploited and DNB is responsible for monitoring the financial sectors, including S.127, the securities statistics and the preparation of the Dutch balance of payments, and the international investment position. The CBS is responsible for compiling the National Accounts and includes the non-financial sectors.

Periodic reports of this type of financial institution are the main source for mapping out the financial sub-sector S.127. Approximately 800 reporters have a (more extensive) monthly or quarterly obligation, collectively referred to as the 'sample', while another 12,000 reporters are required to submit a report annually (also referred to as the 'benchmark'). The total of all reporters is referred to as the population.

The data submitted is microdata and provides an insight into the composition of the balance sheets and incomes of the individual reporting institutions, among other things. For statistical purposes, this data is corrected, added to and augmented by DNB to produce an overall representative picture, also known as the macro picture. Finally, this data is confronted with the data available at Statistics Netherlands in the National Accounts context. This can further increase the plausibility of outcomes - possibly by performing integration corrections. This is also referred to as integrated statistics.

This report mainly uses integrated statistics across the population. Nevertheless, cases based on microdata information are added, or specific use is made of data on the sample reporters. These are situations where integrated data is not available, or where microdata (about the sample) can add more detail. Based on aspects including the contribution to the Dutch economy, DNB distinguishes two groups within the S.127 subsector:

1. SPEs with limited impact on the Dutch real economy, with gross income flows adding up to approximately zero (S.127A); and
2. Other Captive Financial Institutions (other CFIs) with a closer link to the Dutch economy (S.127B).

DNB uses international standards for the statistical description of these entities, including SPEs. These are determined in part by the IMF's Statistical Committee, which revised its definition of SPEs in 2020, with the following key features: institutional units with up to five employees, little

or no physical presence (assets thus foreign-owned) and no/little physical production in the host economy.

For the sake of international comparability, this adjustment affects the S.127 sub-sector at the aggregate level to a limited extent but has a substantial impact on the ratio between S.127A and S.127B entities. Since the new definition of SPEs is narrower for the number of employees (max five) and the relationship with the foreign country (100 per cent ownership), a substantial number of parties have moved from S.127A to S.127B. This involves a total balance sheet size of over 1,000 billion euros or 20% of the entire sub-sector.

Given that this new definition will be used internationally, that DNB has designed its systems and statistical processes accordingly and that the results will be somewhat comparable in the future, the analysis below uses statistics based on this new definition. The relationship between S.127A and S.127B is thereby set back in time through an allocation key. However, this does mean that some care must be taken when comparing these figures with those obtained in previous studies on the nature and size of Special Financial Institutions (SFIs).

3.2 Number of conduit companies and balance sheet size

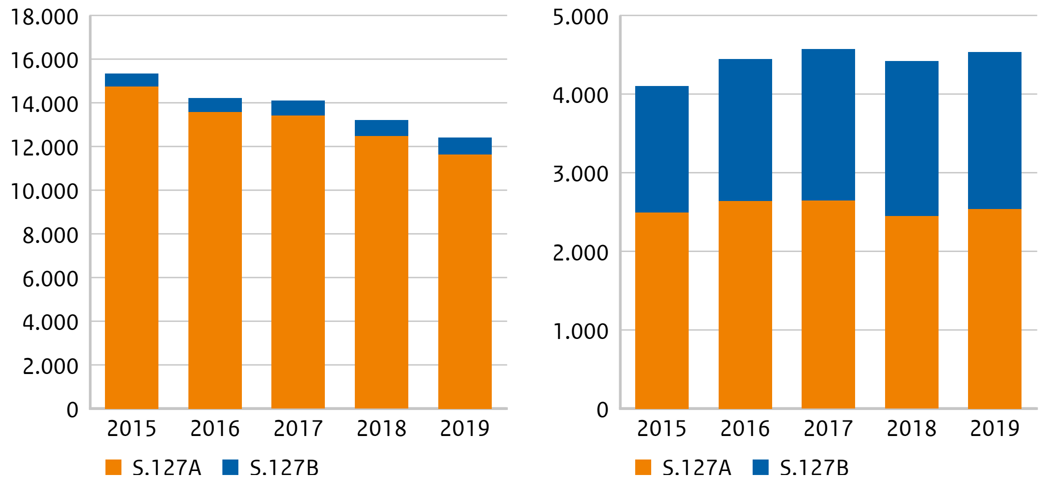
Figure 4 shows that S.127 entities decreased from almost 15,300 in 2015 to about 12,400 in 2019. This decrease is (largely) a statistical artefact. Since an increasing number of entities have developed non-financial activities, these entities are no longer classified as financial but as non-financial.[37] Tightening up how statistical distinctions are made between financial and non-financial entities by DNB and CBS respectively also leads to a shift of entities between S.127 and S.11. This has implications for monitoring the effects of policy measures to reduce income flows to LTJs (see section 4.4). It is also noteworthy that the number of S127b entities is limited compared to SPEs (S127a). The number of S.127b entities was approximately 800 in 2019 and has slightly increased over time.
Despite the decrease in the number of entities, the total balance sheet size of the S.127 entities remains relatively constant. In 2019, the balance sheet total of these entities was approximately € 4,400 billion, or 550 per cent of GDP at the time, similar to previous years. This means that the average balance sheet size of S.127 entities has increased. This is partly because other captives' average balance sheet size (S.127.b) is a lot higher than SPEs (S.127.a); S.127.b makes up about 6 per cent of S.127 entities but accounts for 45 per cent of the total balance sheet value.

The balance sheet of S.127 entities consists mainly of foreign financial assets and liabilities. Figure 5 shows the geographical distribution of this. The country grouping used is based on defined categories such as LTJs and Offshore Financial Centres (OFCs). LTJs are thereby defined as a jurisdiction that does not subject bodies to a tax on profits or to a statutory rate of less than 9 per cent or a jurisdiction included in the EU list of non-cooperative jurisdictions for tax purposes. The list is published annually.[38] An OFC is defined as a "country or jurisdiction that provides financial services to non-residents on a scale inconsistent with the size and financing of its domestic economy". On the other hand, from an income perspective, relevant country groups or specific countries have been highlighted, such as Luxembourg, Switzerland, and emerging economies, including Brazil, China, and Mexico. Annex 3 provides an overview of the country classification used in this report.

[37] See DNB (2018): Decrease in activities mainly of smaller SFIs (dnb.nl)

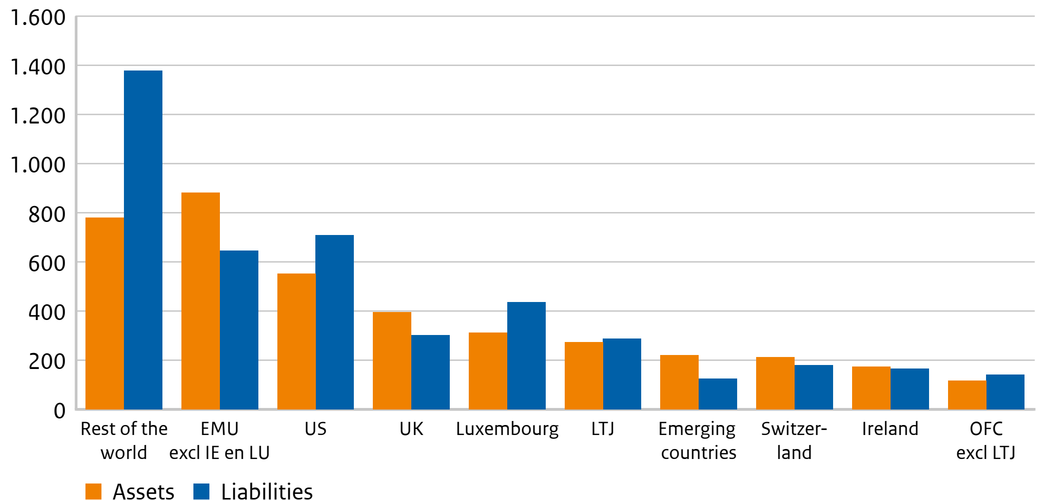
[38] Regulation on low-tax states and non-cooperative jurisdictions for tax purposes (Netherlands Government Gazette). 2018, 72064), as amended by the Regulation of the State Secretary for Finance of 18 December 2019 amending, among other things, some implementation regulations in the field of taxes and benefits (Government Gazette 2019, 69810) and the Regulation of the State Secretary of Finance of 31 December 2020 amending, among others, some implementation regulations in the field of taxes and benefits (Government Gazette 2020, 64029).

***Figure 4:** Number of entities (left) and balance sheet size in billions of euros (right) by subsector*



Source: DNB, based on microdata

***Figure 5:** Balance sheet size by geography in billions of euros (average 2015-2019)*



Source: DNB, based on integrated statistics

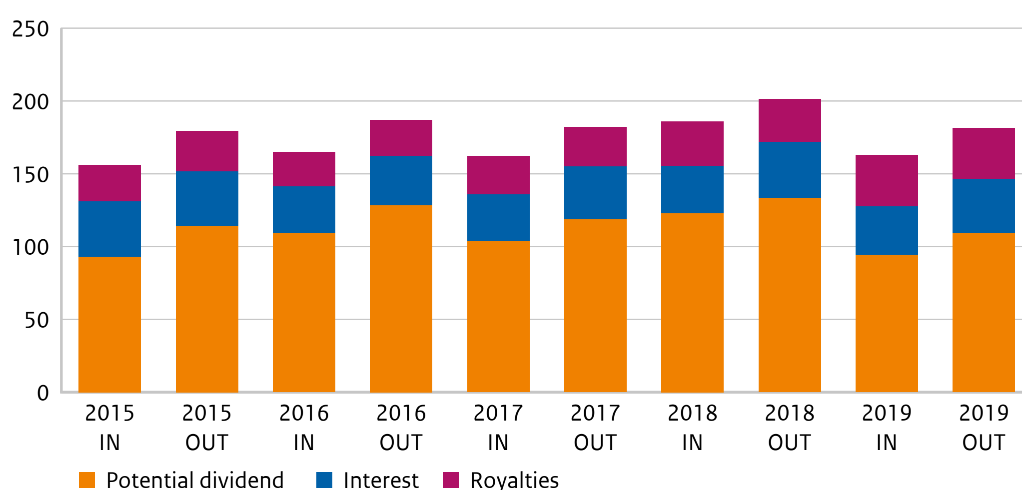
3.3 Income streams

Looking at the tax-relevant income flows - those relevant for taxation - we see that around 170 billion euros of dividend, interest and royalty payments flow through Dutch S.127 entities annually in the period 2015-2019 (see Figure 6). This amount is lower than in previous publications, such as the parliamentary letter on monitoring the effects of the approach to tax avoidance[39], partly because a reclassification of 'mixed forms' has taken place since then. As a result of this reclassification, more entities have been classified as non-financial corporations and thus ended up in S.11. Also missing are the incomes of entities whose ultimate ownership lies in the Netherlands.
The total income flows and the distribution between types of income seem to be fairly stable over the period analysed. The largest part of this income stream (almost 65 per cent) consists of dividends,

39 See parliamentary letter on monitoring the effects of the approach to tax avoidance (2020); Parliamentary Papers II 2019/2020, 25087, No. 259

including retained earnings (also referred to below as potential dividends).[40] Interest flows account for about 20 per cent of income flows. What is also striking is that the incoming and outgoing interest and royalty flows are almost equal to each other; this is an indication that the incoming flows are paid directly to foreign entities. Because outgoing potential dividends here include retained earnings, the outgoing dividends in Figure 6 are larger on average than the incoming dividends. This is because the retained earnings of listed entities are not attributed to portfolio shareholders, unlike retained earnings of associates attributed to parent companies. A large part of the total income flows is accounted for by a small proportion of entities or clusters of entities. For example, Figure 7 shows that only 12 clusters - with 182 underlying entities - account for 42 per cent of total income and 70 per cent of total income is accounted for by about 70 clusters with more than 500 underlying entities.[41]

***Figure 6:** Incoming and outgoing income flows S.127 in billions of euros*

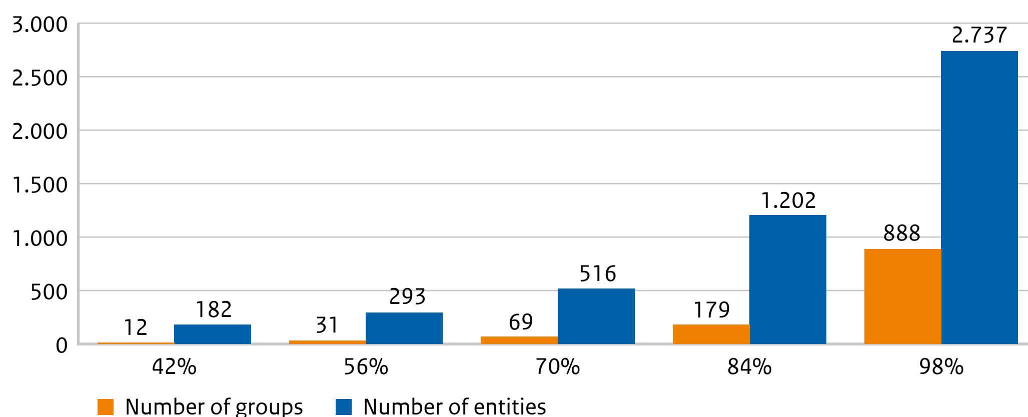


Source: DNB, based on integrated statistics (for interest and potential dividend) and microdata (for royalties)

[40] In the DNB statistics, within the income from equity participations (that is, the operating profit of the subsidiaries under the S.127 entity) a distinction is made between dividends paid in the same year (as dividends) and the part that is not yet paid in that year but is retained and may be paid in a subsequent year (retained earnings). Whenever reference is made in the remainder of this section to potential dividends, this means both dividends and retained earnings. It should be noted that part of the retained earnings may never be distributed or may ultimately be distributed to a shareholder in a country other than that to which the retained earnings were originally attributed. When the retained earnings are distributed as dividends in a subsequent year, the same amount is adjusted to avoid double counting.

[41] A cluster is a group of entities belonging to the same multinational. The percentages in Figure 7 are based on shares of total income, i.e., both incoming and outgoing from all entities over 2015-2019. Percentages smaller than 42 per cent are not shown due to the traceability to individual clusters. Only the entities for which income flows were reported in 2015-2019 have been counted here (so clusters are actually even larger - and thus more complex)

Figure 7: Distribution of total income by entities and clusters - average 2015-2019



Source: DNB, based on microdata

Figure 8 shows where the inward and outward income flows of Dutch S.127 entities come from and go to for the years 2015-2019. This varies greatly by type of income stream. Inward and outward potential dividend and interest flows are geographically reasonably balanced and inward and outward flows to LTJs are relatively limited.[42] In contrast, inbound and outbound royalty flows show a specific pattern whereby the Netherlands is used as a link for royalty flows mainly from Ireland and offshore financial centres to LTJs (see also structure 1 in Annex 2). [43] On average, in the period 2015-2019, 79 per cent of royalty flows passing through the Netherlands went to low-tax jurisdictions. This is in line with the findings of Lejour et al (2021) who - by comparing the income flows to and from Dutch SPEs with the bilateral differences in statutory tax rates - calculate that the conduit of royalties by Dutch SPEs provided multinationals with annual tax savings of approximately € 3 billion in the period 2014-2016.[44]

Figure 9 provides an insight into the chain by comparing the country of exit from the Netherlands with the country of the ultimate parent company.[45] The middle numbers represent the percentage of the Netherlands outgoing income flows to a specific country or group of countries. For example, in the period 2015-2019, an average of 25 per cent of the Netherlands outgoing income flows went to LTJs. The rightmost numbers show the percentage of Dutch outbound income flows to the country of the ultimate parent company. It is notable that for almost 55 per cent of Dutch outbound income flows the ultimate parent company is located in the US. For real income flows, outgoing income flows might be expected to go directly to the country of the ultimate parent company. However, based on data on the sample of reporters - for whom information on the home country is available - it appears that this only applies to 40 per cent of the Dutch outgoing income. In particular, income flows from multinational companies with the US as their home country take a detour and go to LTJs in particular. This suggests that, at least until recently, the Netherlands was used as a conduit country to LTJs in order to avoid taxation. Combined with Figure 8 and the aforementioned study by Lejour et al, we know that this mainly concerns royalty flows that went via the Netherlands to LTJs such as Bermuda, while the ultimate parent company is located in the US. A study shows that by 2020, these royalty

[42] It should be noted, however, that substantial inbound and outbound flows to, for example, Luxembourg and Ireland may flow indirectly to low-tax jurisdictions.

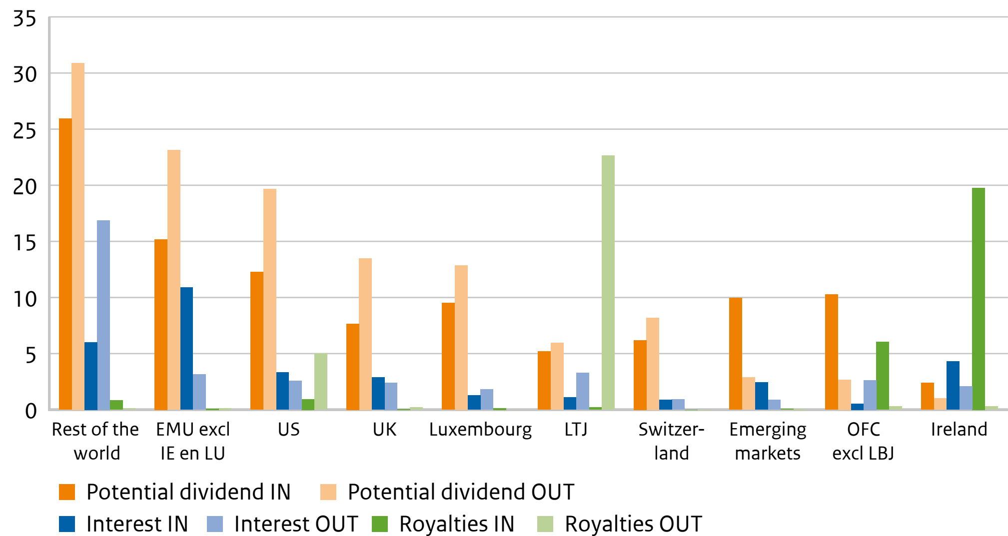
[43] See Annex 4 for the country classification used in this report.

[44] Lejour et al (2021). The immeasurable tax gains by Dutch shell companies | SpringerLink

[45] The figure is based on DNB microdata, based on a sample of reporters (and therefore not the entire population).

streams had largely dried up.[46] Due to the recently introduced conditional withholding tax on interest and royalties, it is expected that the remaining interest and royalty flows to LTJs will almost completely cease to exist or be shifted. Section 4.3.4 discusses this measure in more detail.

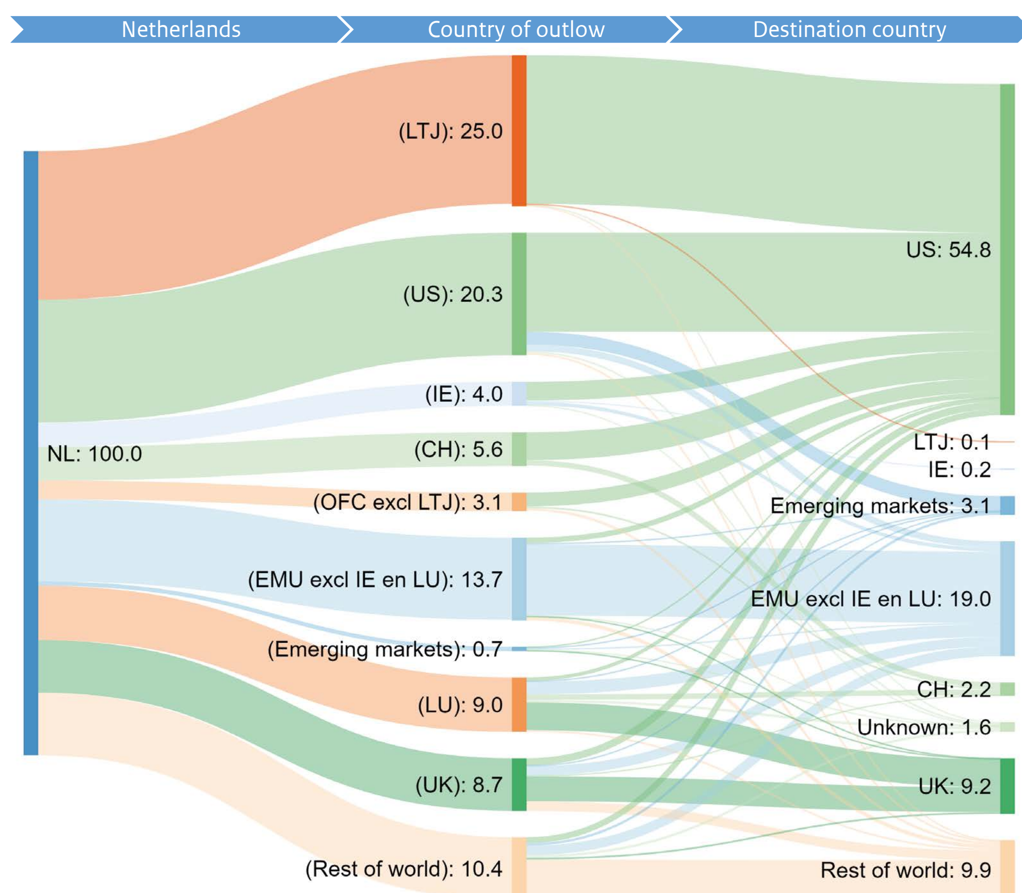
***Figure 8:** Geographical distribution of income flows S.127, average 2015-2019, in billions of euros*



Source: DNB, based on integrated statistics (for interest and potential dividend) and microdata (for royalties)

[46] Coffey et al (2021). The changing nature of outbound royalties from Ireland and their impact on the taxation of the profits of US multinationals.

Figure 9: *Percentage of total NL outgoing income flows by country of outflow and home country (average in the period 2015-2019)*



Source: DNB, based on microdata on 'sample' reporters

3.4 Types of conduit companies

A definition of 'Financial institutions and intra-group lenders' (S.127) has already been given in section 2.4. To get a better idea of the diversity within this group, various archetypes can be distinguished on the basis of balance sheet composition, including the proportion of participating interests and group loans on the balance sheet. The balance sheet ratios have been chosen primarily so that the heterogeneous group S127 can be broken down into more homogeneous sub-groups; they are not based on recognised definitions or statistical practices.[47] The classification is intended primarily to provide a better understanding of the nature of the activities of these entities.

Table 3 provides an overview of the distinguishable types of S127 companies based on balance sheet composition. Holding companies mainly have participations in other entities on the balance sheet. They may or may not have partial ownership of these entities without having management control over them. On the other hand, 'Loan conduits' and 'intra-group financing companies' have many group loans on their balance sheets and therefore function (in part) as an internal bank. The money of a group is collected in the entity and then used again to benefit the same group. Loan conduits focus only on issuing loans, whereas intra-group financing companies may also have holding activities.

47 The chosen percentage of 70% is in line with what is understood in tax law as being predominant.

Fund raising vehicles and mixed financing companies aim to attract funding from outside the group. Both issue debt securities, but the former only aims to lend the funds raised to a parent entity, while the latter is a mix of all the previous archetypes and thus may have holdings on its balance sheet.

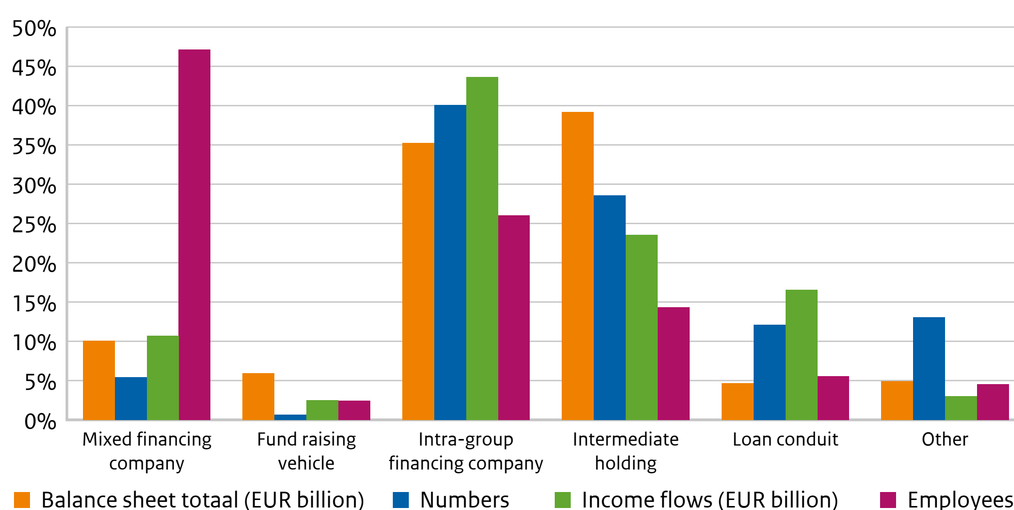
Figure 10 shows for each type of conduit company its average share of the total number of S.127 entities and the total balance sheet and income flows of this group during the period 2015 and 2019. Intra-group financing companies represent 46 per cent of the total balance sheet and are therefore the largest group, followed by intermediate holding companies (29 per cent) and mixed financing companies (12 per cent). The category 'other' includes entities that have assets unrelated to group companies.

Table 3: *Distribution by type based on average balance sheet size 2015-2019*

Type	Description	Definition
Intermediate holding	Holding company	Participations in subsidiaries/ of parent company >70% of both assets and liabilities
Loan conduit	Passes on loans from parent to subsidiaries	Group loans make up >70% of both assets and liabilities
Intra-group financing company	Combination of the two above	Participating interests and group loans jointly account for >70% of both assets and liabilities
Fund raising vehicle	Issues debt and lends proceeds to parent	Securities (plus derivatives) represent >70% of liabilities and loans represent >70% of assets
Mixed financing company	Combination of all of the above	Participations and group loans constitute >70% of the assets and there is no criterion concerning the liabilities
Other	For example, assets are not intra-group	Other, for example >30% securities on asset side

Source: DNB based on microdata

Figure 10: *Type of conduit company as a percentage of total*



Source: DNB, based on microdata

3.5 Importance for the Dutch economy

3.5.1 Employment

Conduit companies make only a limited direct contribution to employment in the Netherlands. Of the S.127 entities, approximately 90 per cent report having no employees. The total number of employees of S.127 is between three and four thousand, on a balance sheet total of almost 4500 billion euros. As expected, the average number of employees for S.127a entities, at 0.15 employees per entity, is smaller than the average number of employees in sector S.127b, which has an average of 2.5 employees per entity.[48] If we look at the type of conduit company, we see that on average most employees work in fundraising vehicles and mixed financing companies. Loan conduits and holding companies have the fewest employees on average. The balance sheet total per employee also varies significantly between the different types of conduit companies. Mixed financing companies have the lowest average balance sheet amount per employee, less than EUR 200 million. Intermediate holdings have the largest balance sheet amount per employee at approximately EUR 4 billion.

The indirect employment associated with S.127 companies in the Netherlands - such as employment in trust and company services - is difficult to estimate.[49] At the same time, long-term structural employment is mainly determined by the labour supply in the Netherlands. In other words, if employment in sector S.127 declines, then workers from this sector are likely to be employed in another sector.

Conduit companies are estimated to have paid around € 350 million in labour costs (wages and contributions) in 2019. Comparing this with the limited number of employees in Table 4 confirms the picture that conduit companies lead to few, but high-quality jobs with an average wage bill per employee of approximately 100,000 euro.

3.5.2 Tax payment

DNB estimates that the corporation tax payments of conduit companies will average 650 million euros a year in the period 2015-2019.[50] This is approximately 2.6 per cent of corporate income tax revenues and 0.2 per cent of total tax revenues. This is probably an overestimate because S.127 entities may form a tax entity with other entities; as a result, the S.127 entity may also pay tax for entities outside of sector S.127.

As far as dividend tax is concerned, the withholding exemption applies to dividend payments to shareholders with an interest in treaty countries that do not qualify as a portfolio. Since this is the bulk of unlisted S.127 entities, the dividend tax remittance is expected to be negligible since 2018.

---

48 Indeed, this follows in part from the statistical definition of S.127A <5 employees.

49 An earlier estimate was between 5000 and 7500 FTEs. Source: SEO (2013). Out of the shadow of the banking sector. Facts and figures on special financial institutions and shadow banking

50 DNB's estimation model is based on self-reporting of a sample of S.127 entities. The estimation model was last fully calibrated in 2016 when it corresponded relatively well with the realization figures of CBS. For this report, the 2016 estimated amount of corporate tax payments by S.127 entities of €629 million has been carried forward to later years.

4 What is the role of taxation?

4.1 Introduction

This chapter looks at the most relevant elements that have made the Dutch tax system attractive for conduit companies, at least until recently. The following components are often mentioned in this context: the extensive tax treaty network, the participation exemption, the absence of withholding tax on interest and royalties and the ruling practice. These components are discussed in turn in this chapter. Some examples of structures are given for each section. By way of illustration, Annex 4 provides a more comprehensive overview of some common tax-driven conduit structures using a number of simplified, stylised examples. This chapter also compares this with similar regulations in several other countries. This comparison is based on an external study the Committee had carried out by PwC and verified by the IBFD. The Committee requested this for Belgium, Cyprus, Germany, Ireland, Jersey[51], Luxembourg, Malta, Singapore, the United Kingdom (UK) and Switzerland. The complete study and the quick scan by IBFD are attached to the report as separate annexes. That is followed by a discussion of the most relevant measures that have already been taken and announced to make certain forms of conduit activities unattractive because they are no longer considered desirable by the legislator. Finally, the monitoring of these measures is discussed.

4.2 Main tax elements for conduit companies

4.2.1 The extensive tax treaty network

General

To avoid double taxation, a tax treaty divides the taxing power between countries. In other words, a tax treaty determines which country may levy tax on which income or capital. Whether an income or asset is taxed depends on the national legislation of the country to which the taxing right is attributed. A tax treaty only distributes the power to levy taxes but does not in itself create a right to levy taxes.

The Netherlands has had a large bilateral tax treaty network for many decades. Currently, a tax treaty is in force with 93 countries.[52] In its tax treaties, the Netherlands adheres as much as possible to the OECD Model Tax Convention (and the most recent version thereof).[53][54] The Netherlands has therefore concluded a large number of bilateral tax treaties, but on average not many more than other European countries, as shown in Figure 11.

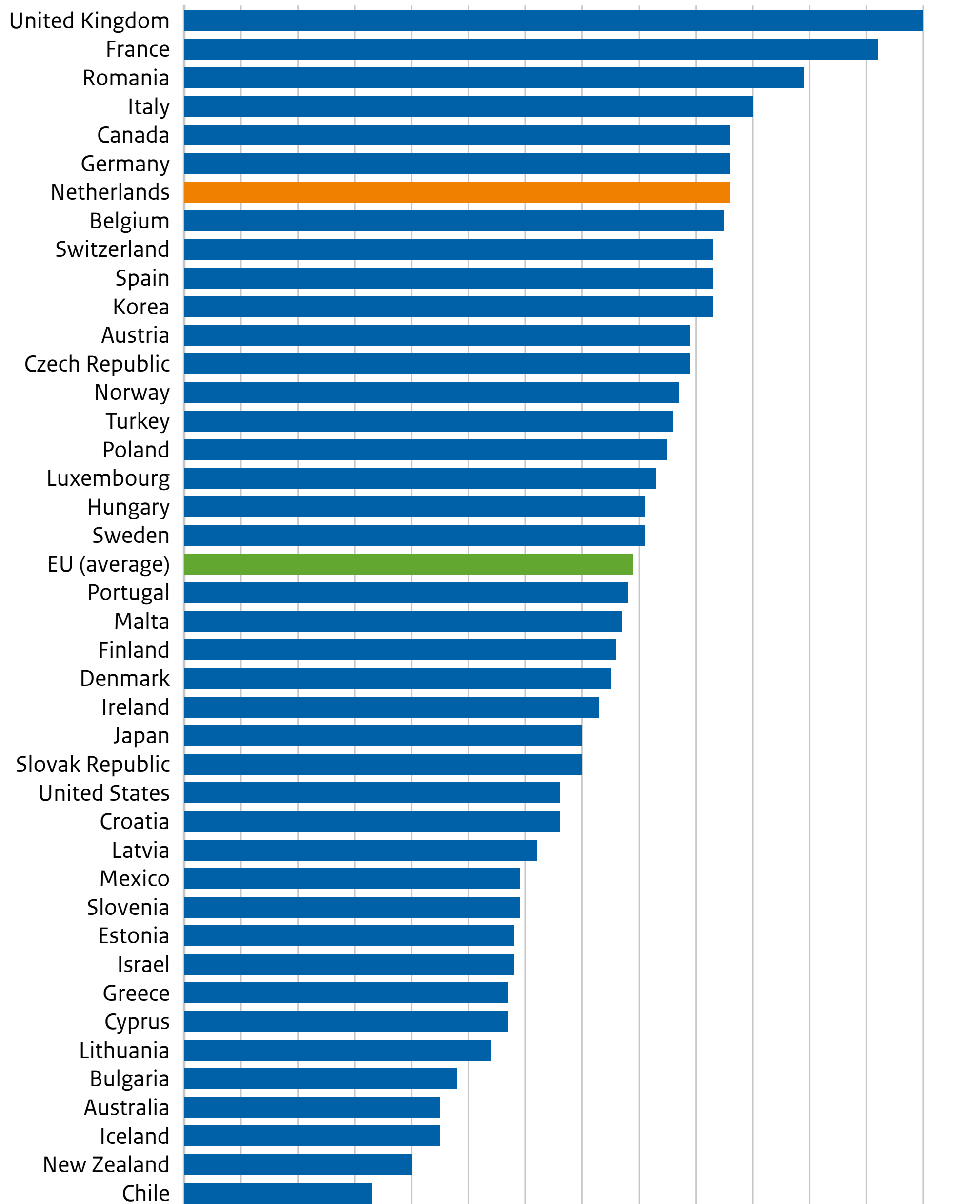
[51] The Committee notes in advance that the Jersey system is not easily comparable with that of the other countries (and the Netherlands), because a 0% rate of income tax generally applies in Jersey, Jersey has no withholding tax and, apart from Tax Information Exchange Agreements (TIEAs), hardly any tax treaties.

[52] Tax Information Exchange Agreements (TIEAs) are not included. For the most current status we refer to www.rijksoverheid.nl/onderwerpen/belastingverdragen.

[53] OECD (2017), Model Tax Convention on Income and on Capital: Condensed Version 2017 (http://dx.doi.org/10.1787/mtc_cond-2017-en).

[54] The OECD Model Tax Convention is a standard model treaty on which bilateral tax treaties are often based.

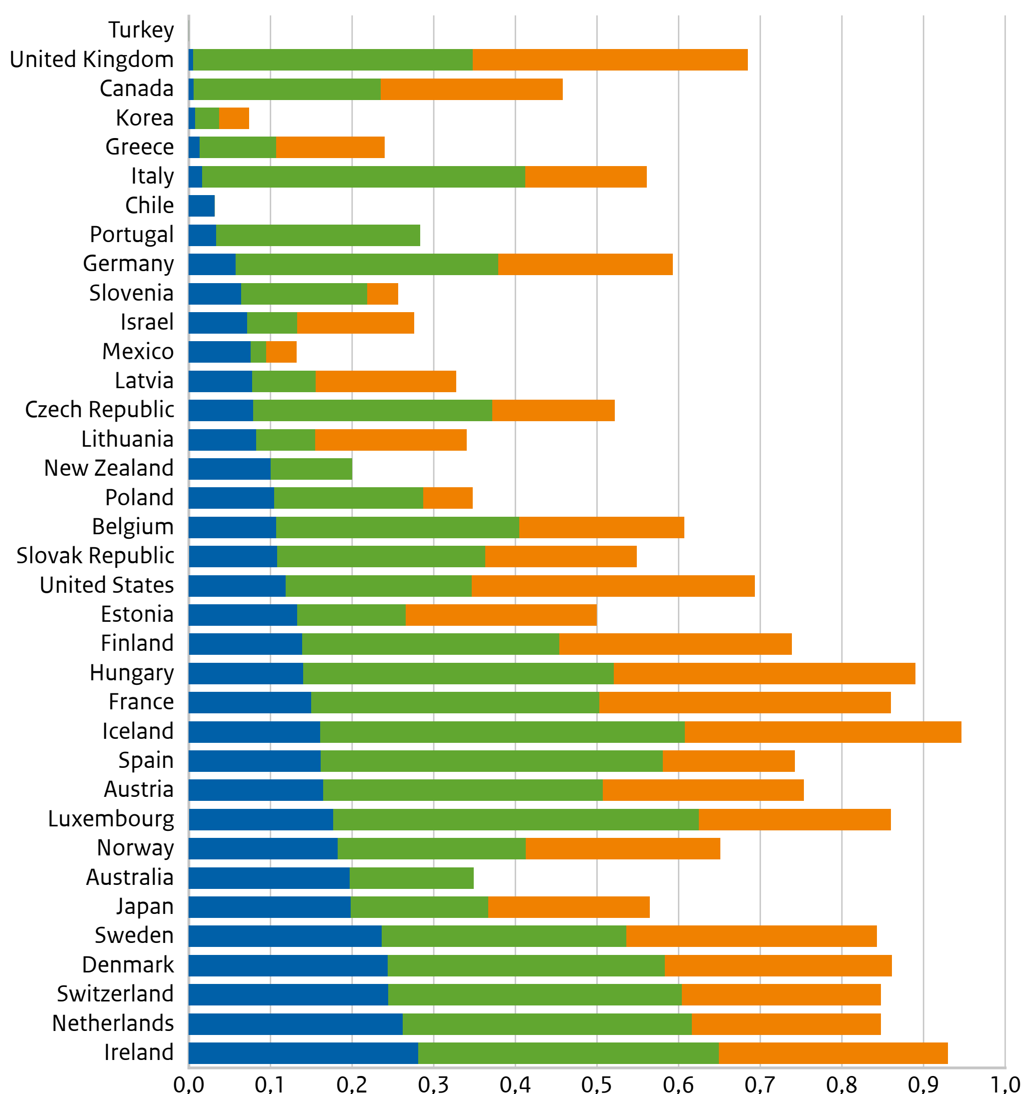
Figure 11: *Number of tax treaties per country in 2020*



Source: Tax Foundation (2021) and European Committee (2021)

The Dutch treaty policy has traditionally been to reduce withholding taxes on dividends, interest and royalties as much as possible because the levying of withholding taxes (after profit tax has been levied) can lead to double taxation. The overview below (figure 12) shows that the Netherlands is one of the countries that has managed to limit withholding taxes to zero in a large number of treaties.

Figure 12: *Share of tax treaties with a zero withholding tax rate*



Source: IMF (2021). Capital Income Taxation in the Netherlands. IMF Working Paper.

On a limited number of points, the Dutch treaty policy deviates from the OECD Model Tax Convention; in relation to developing countries, the Netherlands sometimes also accepts certain parts of the United Nations Model Tax Convention (UN Model Tax Convention, which grants more taxing rights to the source country.[55]

Relevant treaty provisions for conduit companies

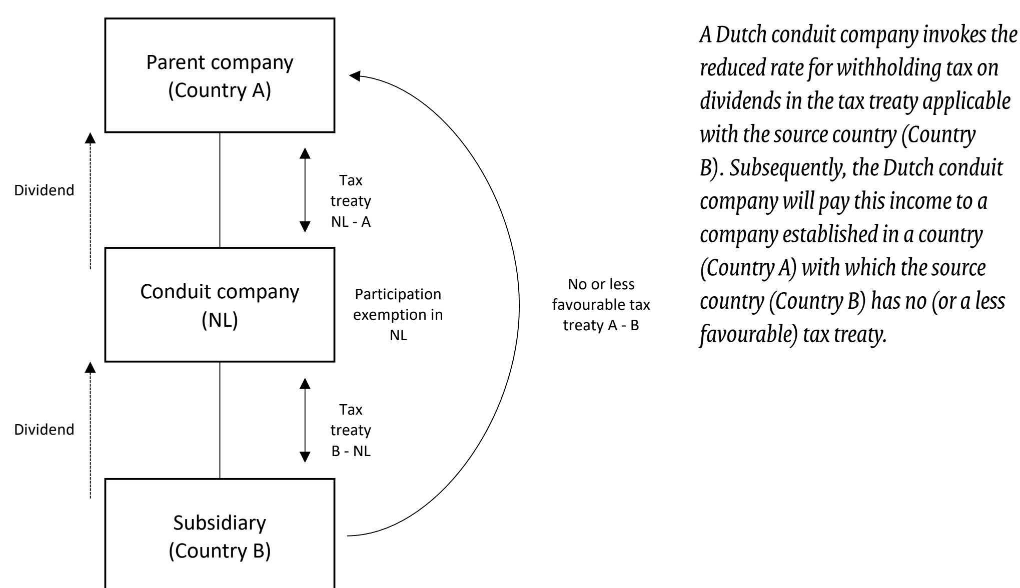
The most relevant treaty provisions for conduit companies deal with dividends, interest, royalties and gains on disposal. This concerns Articles 10 to 13 of the OECD Model Tax Convention.

[55] See p. 28 et seq. of the Tax Treaty Policy Document 2020.

The Netherlands' treaty policy has traditionally been that withholding taxes will not be levied on interest and royalties and on dividends only where portfolio dividends are concerned[56].[57] The idea behind this is to minimise the double taxation and administrative burden for Dutch companies operating with a subsidiary abroad.[58] [59]

Unintended use of treaties by conduit companies
Unintended use here refers to what is known as 'treaty shopping'. An example of treaty shopping is provided below.

Sample structure 1



A Dutch conduit company invokes the reduced rate for withholding tax on dividends in the tax treaty applicable with the source country (Country B). Subsequently, the Dutch conduit company will pay this income to a company established in a country (Country A) with which the source country (Country B) has no (or a less favourable) tax treaty.

The advantage of this structure is that, by using the Dutch treaty network, the dividends arrive at the parent company in the country of residence (Country A) without or with reduced withholding of local tax compared to the situation where the source country (Country B) had made the payment directly to the country of residence (Country A). This is just one example of a (conduit) structure in which the Dutch treaty network plays a role, combined with the participation exemption and the dividend withholding tax exemption in treaty situations.

Because the Netherlands has had a large bilateral tax treaty network for some time, it has proved to be an attractive country for 'treaty shopping'. When tax treaties are concluded, it is assumed that it is up to the source country to prevent the reduced withholding tax rate from being wrongly applied.

---

[56] The Netherlands aims for 0 per cent dividend withholding tax for intra-group dividend distributions (to which the participation exemption in the Netherlands applies) and 15 per cent in other cases (portfolio dividends).

[57] In principle, therefore, the Netherlands pursues exclusive residence taxation of interest, royalties and participation dividends. See also the Tax Treaty Policy Document 2020, pp. 17 and 18.

[58] See e.g. pp. 17 and 18 of Tax Treaty Policy Document 2020.

[59] In certain cases the Netherlands is prepared to agree to a withholding tax. This specifically concerns withholding tax concerning developing countries (section 5.2.3 of the Tax Policy Document for 2020) and withholding tax under the Dutch Withholding Tax Act 2021 (see also section 4.2 of this report and section 5.3.3 of the Tax Policy Document for 2020).

Qualifying as a resident of one of the contracting countries is a condition for access to a tax treaty. Based on the OECD Model Tax Convention, a company is deemed resident if it is subject to taxation.[60]

Whether a person is subject to taxation and therefore resident is determined by reference to national law. Under Article 2(4) of the Corporation Tax Act 1969 (Wet Vpb 1969), an entity incorporated under Dutch law is subject to corporation tax and is therefore deemed to be resident in the Netherlands. This means that, in principle, any company incorporated under Dutch law is a resident here for tax purposes, unless a company is deemed to be a resident of the other treaty country based on the tie-breaker rule in the applicable tax treaty, for example because its actual management is exercised there. The actual activities of a conduit company are often limited. The actual leadership is not comprehensive. A conduit company usually qualifies as a resident for the tax treaties concluded by the Netherlands Since at least 50 per cent of the formal management is usually carried out by a director/resident (hired) in the Netherlands, board meetings are held in or from the Netherlands, and no formal managerial duties are performed elsewhere.

When a conduit company has a limited presence in the Netherlands, it cannot easily be claimed based on the facts and circumstances that it is established in another country. The Tax and Customs Administration have no direct interest in taking such a position and this will therefore not be their highest priority.[61] The tax authority of the country in which the shareholder of the Dutch conduit company is resident also has no interest in claiming the resident status of the subsidiary. That is the case even if the material decisions about the activities performed by the Dutch company are taken within its territory (and are only ratified in board meetings in the Netherlands, whether or not through online meetings). Claiming the residence of the Dutch conduit company barely results in additional tax revenue, since the profit of the company that has moved is small and, in addition, a (higher) withholding tax will probably be levied on the payments to the Dutch conduit company, which will have to be settled. The only party interested in contesting the resident status of the Dutch conduit company is the tax authority of the source country from which the payments of dividends, interest and/or royalties are made. This is a major challenge and, while not impossible, extremely difficult without a full understanding of all the facts and circumstances. If there is no PPT in the treaty between the source state and the Netherlands, successfully combating the unintended and undesired use of the tax treaty is practically very difficult.

The domicile of a conduit company is usually confirmed by the Tax and Customs Administration when issuing a certificate of residence. This is a declaration in which the Tax and Customs Administration formally states that a company is a resident of the Netherlands within the meaning of the applicable tax treaty. If a company is listed in the Tax and Customs Administration's records as a resident taxpayer and there are no indications that the entity may also be established elsewhere, the Tax and Customs Administration will issue such statements on request. [62]

The fact that access to a tax treaty is relatively easy does not mean that the relevant treaty benefits can always actually be obtained. For this purpose, it is important whether the conduit company

[60] Tax Treaty Policy Document 2020, p. 15.

[61] Even if the Tax and Customs Administration were to attempt this, success is not guaranteed. See the judgment of a French-incorporated loss-making company incorporated under Dutch law and included in a tax entity with a Dutch parent.

[62] For entities incorporated under foreign law that are actually established in the Netherlands, the Tax and Customs Administration will, in case of doubt, conduct a fact-finding investigation into their establishment in the Netherlands before proceeding to register them as resident taxpayers. Since Article 2(4) of the 1969 Corporate Income Tax Act is not applicable, it is necessary in such a situation to determine whether a residence certificate can be issued under the tax treaties concluded by the Netherlands.

qualifies as the beneficial owner (the OECD Model Tax Convention and the UN Model Tax Convention speak of 'beneficial owner'). However, if the recipient is legally entitled to the payment and there is no obligation to make a further payment in return for receiving it, it is assumed in many cases that the recipient can be regarded as the 'beneficial owner'.[63] The legal assessment (does the company have power of disposal over the funds received) may produce a different outcome from an economic assessment (does the company use this power of disposal or does it in fact appear that it only pursues conduit activities).

The fact that undesirable use of treaties still takes place despite the 'beneficial ownership' requirement has led, among other things, to the OECD Base Erosion and Profit Shifting (BEPS) project identifying treaty abuse as one of the main forms of base erosion and profit shifting. To combat this, measures for combating treaty abuse have been proposed in BEPS Action Plan No. 6. This is discussed in more detail in section 4.3.6.

International comparison of treaty residency and issuance of certificates of tax residence
The provisions on residency and obtaining a certificate of tax residence are no different in the countries investigated, except for Singapore (see Table 4). If a company has its registered office somewhere by virtue of the law of incorporation or registration, it is in principle also a resident of that country. This is only different if there is dual domicile, whereby the company is actually domiciled in another country. In other countries, under more or less the same circumstances as in the Netherlands it is possible to obtain a certificate of tax residence even if the actual presence in those countries is limited.

Table 4: *Country comparison of conditions of tax residence and certificate of tax residence*

	Tax residence determined by		Possibility of obtaining a certificate of tax residence under certain conditions	
	Registered office	**Effective place of management**	**Yes**	**No**
Belgium	X	X	X	
Cyprus*		X	X	
Germany	X	X	X	
Ireland	X	X	X	
Jersey	X	X	X	
Luxembourg	X	X	X	
Malta	X	X	X	
The Netherlands	**X**	**X**	**X**	
Singapore		X	X	
Switzerland	X	X	X	
UK	X	X	X	

Source: PwC report

*Cyprus: the Cypriot Ministry of Finance has proposed legislation in Q1 2021 to extend the corporate tax residency test. See chapter 1 of the PwC report for more details.

[63] See e.g. Hietland, M. (2019). How the Indonesia-Netherlands tax treaty enables tax avoidance. An analysis of the treaty and Indonesian court decisions on corporate tax disputes. https://www.somo.nl/how-the-indonesia-netherlands-tax-treaty-enables-tax-avoidance.

4.2.2 The participation exemption

General
The participation exemption is an exemption for the levying of corporate income tax on the benefits that a Dutch taxpayer (parent) company derives from participation in a subsidiary. The exemption applies to domestic and foreign subsidiaries. The participation exemption covers dividends that the parent company receives from the subsidiary, price gains on the shares in the subsidiary and the gain on the sale, whether partial or full, of the subsidiary (gains on disposal). By contrast, losses incurred by subsidiaries are not deductible.[64] This concerns, for example, a loss on the sale of shares or a price loss on shares in a subsidiary company (loss on disposal).

Basis and rationale
Although the participation exemption has been amended several times, the principle underlying it has remained unchanged: the profits of a (subsidiary) company are taxed only once (the ne bis in idem principle).[65]

The idea behind the participation exemption is to prevent economic double taxation. For foreign subsidiaries, this means that their profits are only taxed in the country where they are established. This ensures that Dutch companies can compete with companies established abroad based on an equivalent tax position. This made the participation exemption an attractive feature of the Dutch tax system and was/is thus a decisive element both for the competitive position of Dutch multinationals abroad and the Dutch establishment climate for internationally operating groups. However, the Netherlands has not been unique regarding the participation exemption for a long time (see Table 5).

Conditions
To be eligible for the participation exemption, the parent company must be liable for Dutch corporate income tax and must therefore be established in the Netherlands.

In addition, the shareholding and the qualification of the subsidiary must meet certain conditions. The main rule regarding share ownership is that the parent company must hold at least 5 per cent of the shares in the subsidiary. The subsidiary must also satisfy at least one of the following three tests:
- *'Purpose test':* the holding in the subsidiary must be held with the purpose of achieving a return going beyond normal asset management.
- *'Subjectability test':* the subsidiary is subject to a tax that is realistic according to Dutch standards (in general, at least 10 per cent on a profit base determined according to Dutch standards).
- *"Possession test*. the assets of the subsidiary company do not consist for more than 50 per cent of investments that are taxed at a low level.

The parliamentary explanatory notes to the purpose test state that a participation is not held as an investment if, among other things, the subsidiary's business is an extension of the business of the taxpayer parent company. Even if this parent company does not carry on a material undertaking but fulfils a 'material function', the participation is not deemed to be held as an investment holding. This is the case if the parent company fulfils a material function in the group's operations. Think of it as a top corporate executive. The same applies to an intermediate holding company which, within a

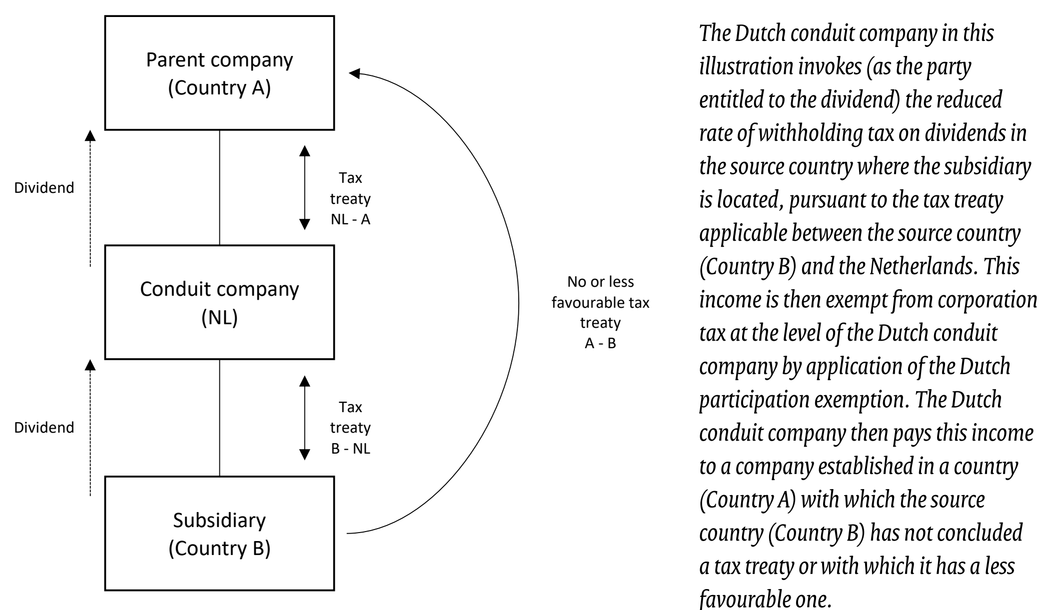
[64] An exception to this is the liquidation loss scheme (included in Section 13d of the 1969 Corporate Income Tax Act), under which liquidation losses are deductible under certain conditions.

[65] The Controlled Foreign Company (CFC) measure corrects the situation where double taxation occurs formally, but not actually. Under this measure, benefits from mobile assets derived from an entity or permanent establishment are included in the Dutch tax base under certain conditions. The rationale behind this measure is to counter tax avoidance by shifting profits to low taxed, controlled entities or permanent establishments.

group, fulfils a linking function between the business activities of the companies in which it has an interest and the (parent) companies higher up in the group.[66] This link approach is derived from an old resolution[67] that followed a judgment in which the Supreme Court ruled that the participation exemption in place at that time does not apply if there is no link between the business activities of the parent company and the subsidiary company if the parent company does not itself operate a business.[68] This was deemed undesirable because the Netherlands would then no longer be an attractive country for holding companies. Applying the participation exemption to the benefits from foreign subsidiaries by Dutch (intermediate) holding companies that fulfil a linking function makes the Netherlands an attractive country for holding companies.

Relationship with conduit companies
The participation exemption applies in principle to all taxpayers for Dutch corporate income tax purposes and does not impose any requirements on the (actual) presence of the taxpayer in the Netherlands. Companies with only a very limited presence or none at all in the Netherlands also qualify for the participation exemption. As a result, international holding structures can be designed in such a way that dividends and gains on disposal are realised without Dutch corporate income tax, which can then leave the Netherlands as dividends[69] or be reinvested, while the taxpayer's presence in the Netherlands is limited. Combined with the extensive Dutch tax treaty network, this has made the Dutch tax system vulnerable to holding activities of no real significance

***Sample structure** 2*



The advantage of this structure is that, by using the Dutch treaty network and the participation exemption, the dividends arrive at the parent company in the country of residence (Country A) without or with reduced withholding of local tax, compared to the situation in which the source country (Country B) had made the payment directly to the country of residence (Country A). This

[66] Parliamentary Papers II 2009/10, 32129, no. 3, pp. 59.
[67] Resolution of the Secretary of State for Finance dated October 15, 1974, no. BNB 1974/21 516, BNB 1975/11.
[68] Judgment of the Supreme Court of 7 November 1973, BNB 1974/2 (the Holding judgment).
[69] The levy of Dutch dividend tax on such distributions of untaxed profits can often be reduced to 0 per cent through the application of tax treaties, the effect of the EU Parent/Subsidiary Directive and international structuring.

form of unwanted use is also known as '*treaty shopping*'. Although the Dutch treaty network also plays a role in this respect, the participation exemption is essential because it ensures that the dividend is exempt from corporation tax in the Netherlands. In addition, until recently, a Dutch cooperative was frequently used in international structures. [70] Unlike private and public limited companies, cooperatives in the Netherlands were exempt from the dividend withholding tax up to 1 January 2018.

Undesirable or improper use can also take place in the case of gains on disposal. Gains realised on the disposal of a qualifying participation are exempt in the Netherlands. In some countries, these are taxed at source by the transferor of the shares. This is, for example, the case when the disposal concerns a real estate company. If the right to levy tax on the gains on disposal has been allocated to the Netherlands based on the applicable tax treaty, taxation on disposal can thus be avoided.

Finally, it may be advantageous to use an intermediate holding company in the Netherlands if a scheme comparable to the participation exemption in Country A applies to a subsidiary in the Netherlands - for example, under the Parent-Subsidiary Directive - but not to a subsidiary in Country B, while the Dutch participation exemption applies to that subsidiary.

International comparison

The Netherlands has traditionally been known for its participation exemption, but nowadays, almost all other European countries also have a participation exemption for dividends and capital gains (see Table 5). In certain respects, most countries impose somewhat stricter requirements on applying the participation exemption than the Netherlands. In some countries a higher minimum holding percentage applies (in Belgium, Germany, Luxembourg, Switzerland and the United Kingdom this is, for example, 10% where in the Netherlands it is 5%) or a minimum holding period applies (at least one year in, for example, Belgium, Ireland and Luxembourg, and for the exemption on capital gains also at least one year in the UK and Switzerland where in the Netherlands there is no minimum). In Germany, 95 per cent of the profit is exempt (while in the Netherlands, the entire participation benefit is exempt).

In most countries, the participation exemption is not applied in all cases, but requirements are set for the activities and taxation of the subsidiary in which the participation is held. Of course, the extent of this differs. For example, Belgium has detailed regulations under which it does not apply the participation exemption if the subsidiary is insufficiently taxed or benefits from a special regime, while in Malta the participation exemption only does not apply if the holding is held in a subsidiary in a jurisdiction on the European Union's (EU) 'black list' of non-cooperative jurisdictions.

Overall, Cyprus, Luxembourg, Malta and the UK have a 'flexible' participation exemption. The other countries generally make more demands. Although the Dutch participation exemption is not (and no longer) unique, which has been the case for some time, it has a fairly wide scope compared to other countries, and the participation exemption still contributes to the Netherlands being an attractive country for holding companies.

[70] This is discussed in more detail in Section 4.3.3 and in Example Structure 5 in Annex 4.

Table 5: Country comparison participation exemption

	Has a participation exemption		Substance requirements for participation exemption	
	Yes	No	Yes	No
Belgium	X		X	
Cyprus	X		X	
Germany*	X			X
Ireland	X		X	
Jersey		X	N/A	N/A
Luxembourg*	X			X
Malta*	X		X	
The Netherlands	**X**		**X**	
Singapore	X		X	
Switzerland	X			X
United Kingdom*	X		X	

Source: PwC report

* Luxembourg can deny the participation exemption to artificial structures under existing general anti-abuse rules.

* Malta indicates that for non-EU subsidiaries the use of the participation exemption requires that there should be no receipts of passive interest or royalties. The rules have also been tightened up for subsidiaries from non-cooperative jurisdictions. the participation exemption is available for dividends and capital gains under certain conditions. The main exceptions are non-trading subsidiaries and companies acquired in the previous year. See chapter 1 of the PwC report for more details.

4.2.3 The absence of withholding tax on interest and royalties

General

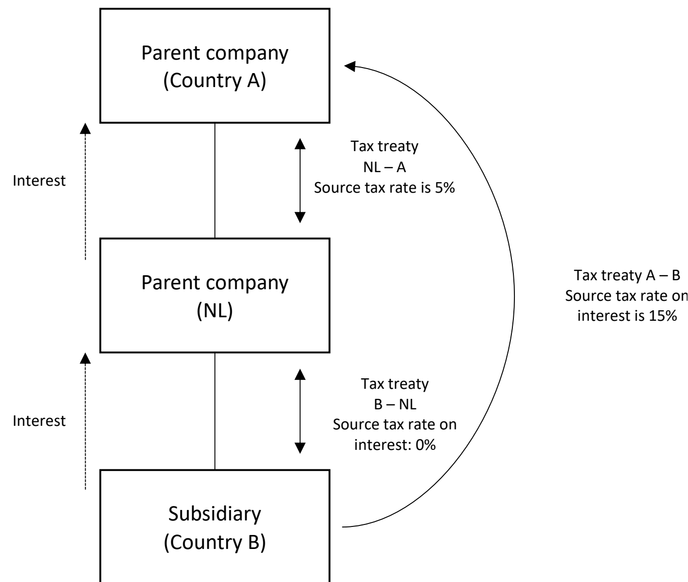
Withholding taxes are taxes levied at the source[71] of an income stream such as a dividend, interest or royalty payment. The absence of withholding tax on interest and royalties was for a long time one of the elements that made the Netherlands attractive to companies operating internationally. The idea behind this was to avoid double taxation and reduce the administrative burden to promote cross-border investments. The idea of not levying withholding tax is in line with the EU Interest and Royalty Directive. Based on this Directive, withholding tax may not, in principle, be levied on interest and royalty payments made to an associated company established in another EU Member State.

Unintended use through conduit companies

An example is given below to illustrate why it was fiscally attractive (particularly until recently) to set up a structure via the Netherlands due to the absence of withholding tax on interest and royalties.

[71] Where the income stream 'originates'.

Sample structure 3



A Dutch conduit company invokes the 0 per cent rate for withholding tax on interest in the tax treaty applicable with the source country Country B. The Dutch conduit company then pays this interest to a (non-hybrid) company established in Country A with which the source country, Country B, has concluded a less favourable tax treaty. In the treaty between the Netherlands and Country A, a rate of 5 per cent applies. The rate in the treaty between Country B and Country A is 15 per cent. Under Country B's domestic law, interest is taxed at a 15% withholding tax rate.

The advantages of this structure are as follows: if the conduit company in the Netherlands had not been interposed, a direct payment from Country B to Country A would have incurred 15 per cent withholding tax on the interest payment. However, in the current example, by using the Dutch treaty network in combination with the absence of withholding tax on interest payments in the Netherlands, the payment is received more favourably for tax purposes at the parent company in the country of residence (Country A). (N.B. This is obviously only advantageous if any withholding tax withheld in Country A by Country B (in the case of direct payment without the intervention of the Netherlands) cannot be set off, or set off in full, against the local tax on the interest income.

The withholding tax rate between Country B and the Netherlands is 0 per cent. Based on the tax treaty between the Netherlands and Country A, a reduced withholding tax rate of 5 per cent applies. However, as indicated above, a treaty only governs the power to levy taxes. The right to levy taxes is a national matter. Until recently, the Netherlands endeavoured to include an exclusive residence tax for interest and royalties in tax treaties. In this example, therefore, in all likelihood no tax would effectively be levied on the payment from the Netherlands to Country A. This is even though the Netherlands would be allowed to levy taxes under the treaty. Although the Dutch treaty network plays an important role in this respect, the absence of withholding tax in the Netherlands is an essential element.

The Netherlands has recently partly abandoned the principle of not levying withholding tax on outgoing interest and royalty payments. For example, on 1 January 2021, the Withholding Tax Act 2021 entered into force.[72] Based on this law, a withholding tax is levied on interest and royalty payments to LTJs[73] in case of payments to hybrid entities and in abuse situations. This measure is further explained

72 Act of December 18, 2019, to introduce a withholding tax on interest and royalties (Withholding Tax Act 2021) (Bulletin of Acts and Decrees 2019, 513).

73 An LTJ is defined as a jurisdiction that does not subject bodies to tax on profits or to a statutory rate of less than 9 per cent or a jurisdiction included in the EU list of non-cooperative jurisdictions for tax purposes.

in section 4.3. However, if Country A is not an LTJ, the above structure could still lead to a tax saving if the withholding tax levied in Country B is not (entirely) creditable in Country A.

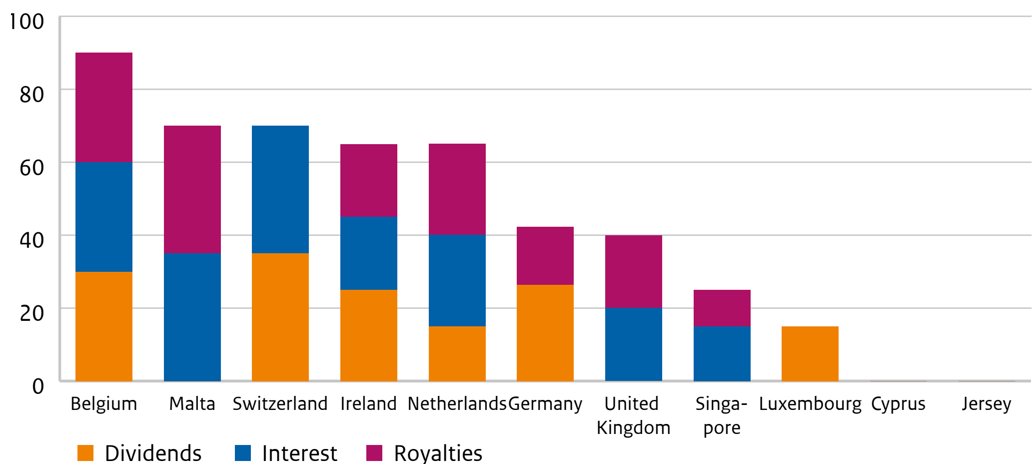
International comparison

The absence of withholding taxes until 2021 combined with the treaty network has made the Netherlands an attractive country for conduit companies. The Netherlands compared favourably with other countries in this respect.

Of the countries examined, most have one or more withholding taxes. Only Cyprus has no withholding taxes, although it has proposed to introduce a withholding tax on payments to jurisdictions on the aforementioned EU black list (see also Figure 13).

Most other countries (Belgium, Cyprus, Ireland, Luxembourg, Malta, Singapore and the UK) do not apply targeted anti-avoidance rules or substance requirements, but a general anti-abuse rule (GAAR) or PPT when a particular transaction is designed to avoid (withholding) tax. Payments to LTJs are subject to deduction restrictions in Belgium (for interest) and Germany (for royalties). Different criteria apply in Belgium and Germany than in the Netherlands to determine whether a payment is low-taxed. With the introduction of the conditional withholding tax on interest and royalties paid to LTJs, to hybrid entities and in abusive situations, the Netherlands has become less attractive for interest or royalty conduits , certainly compared to other countries. Given the recent date of implementation, no figures are yet available to support this. [74]

Figure 13: *Country comparison of withholding tax rates on dividends, interest and royalties*



Source: PwC report

[74] See also Section 4.3 which discusses in more detail the monitoring of the effect of the 2021 Withholding Tax Act.

4.2.4 Ruling practice

General
When it comes to tax avoidance, a link is often made with the ruling policy of the Dutch government. A ruling is an agreement between a taxpayer and the tax authorities. Such an agreement lays down how the tax laws and regulations are applied in a specific situation.

The advantage of obtaining a ruling is that, provided the facts and circumstances remain unchanged, including legislation and regulations, an agreement on the tax consequences exists even before the taxpayer submits a tax return to the Tax and Customs Administration. This therefore provides certainty for taxpayers. A ruling is established based on the Basic Model Settlement Agreement. See Annex 1 for the Basic Model as presented on the Belastingdienst website.

The effect of the ruling practice
In the build-up phase of the Netherlands after World War II and in the wake of real corporate investment in the Netherlands, consultations with, in the first instance, the Ministry of Finance and, later, the Tax and Customs Administration, also led to an ever-growing number of Dutch companies with limited business activity and presence in the Netherlands.

The large number of tax treaties concluded by the Netherlands with reduced withholding taxes, the open attitude of the Tax and Customs Administration, the willingness to make agreements in advance with internationally operating companies and the model rulings developed and published in consultation with the consultancy practice, have contributed to the fact that the international consultancy practice has started to recommend the use of the Netherlands for conduit companies.

Although the purpose of a ruling is to lay down how the tax laws and regulations are applied in a specific situation, the Dutch ruling practice has been severely criticised. Criticism of Dutch ruling policy began with the Primarolo working group. That group tested the ruling policy against the EU Code of Conduct and concluded that the policy was in conflict with the code in important respects.[75] This has led to adjustments and the introduction of the APA[76]-/ATR[77] practice with effect from 1 April 2001. At the same time, stricter substance and risk requirements were imposed on service entities. The practice of creating certainty for entities established in the Netherlands that act as facilitators in acting as a conduit for international financial flows of business investments has not diminished. After the financial crisis of 2007/2008, the social debate about the improper use of the Netherlands by the international business community increased. The ruling practice was therefore drastically revised in mid-2019. The revised ruling practice will apply from 1 July 2019. This is discussed in more detail in section 4.3.

International comparison
Since it was possible in the Netherlands to gain certainty in advance regarding the profit to be declared (the remuneration) when, for example, borrowing and forward-lending funds, it was an attractive option to set up a company in the Netherlands for such conduit arrangements.

Not all countries have such a form of (formal) prior certainty of the profit to be declared (i.e. the remuneration), for example, in the case of borrowing and forward-lending (see Table 6). This is not

75 Report of the Code of Conduct Group on Business Taxation of 23 November 1999 to the ECOFIN Council of 29 November 1999, SN 4901/99.

76 Advance Pricing Agreement (APA).

77 Advance Tax Agreement (ATR).

possible in Cyprus, Germany and Ireland. This is possible in Belgium, Luxembourg, Malta, Singapore, Switzerland and the UK. It should be noted that in practice the requirements for this in Belgium are considerable.[78] In all countries remuneration for intra-group financing (and other services) must be *at arm's length*.

Table 6: *Comparison of ruling practice between countries*

	Is it possible to get a ruling/ certainty in advance for a "spread" [79]?		If Yes, what are the substance requirements?		
	Yes	**No**	**Light**	**Medium**	**Extensive**
Belgium	x				x
Cyprus		x			
Germany		x			
Ireland		x			
Jersey*		x			
Luxembourg		x			
Malta	x			x	
The Netherlands	**x**				**x**
Singapore	x			x	
Switzerland	x		x		
UK			x		

Source: PwC report

Ireland requests are only accepted in a limited number of more complex cases where the circumstances are complex or unusual, or where certain public information is not available. See chapter 1 of the PwC report for more details.

** Jersey: rulings are only available when there is uncertainty in the law.*

4.3 Measures taken and announced

There are already a number of provisions in the tax laws and regulations that are intended to make certain forms of conduit activity unattractive because these forms were not (or were no longer) considered desirable. Without being exhaustive, this section looks at the main measures already taken and those announced (see Table 1 for an overview).

4.3.1 Section 8c of the 1969 Corporate Income Tax Act (taxation of interest and royalties from service providing entities)

Section 8c of the 1969 Corporate Income Tax Act (tax on interest or royalties) came into force on 1 January 2002. This article was introduced to tighten up the actual presence and risk requirements for service providing entities (the financing and licensing companies under the ruling practice prior to 2001). These amendments resulted from the debate on harmful tax competition in the EU and the OECD and were intended to make the Netherlands less attractive to financial service entities that bore hardly any risks concerning the transactions they carried out and had little or no actual presence in the Netherlands. The use of such entities as intermediaries is often tax-driven and leads in particular to harmful consequences for the Netherlands' treaty partners because under a bilateral tax treaty

[78] See comments in paragraph 2.2 of the PWC report. This mainly concerns the amount of information required by the Belgian ruling Committee.

[79] Where the "spread" should be at arm's length. For an explanation of the classification of the substance requirements into light, medium and extensive, please refer to the PwC report in the Annex.

concluded with the Netherlands they may be obliged[80] to reduce the withholding tax to a lower percentage if the receiving entity is a resident of the Netherlands and is also the beneficial owner of the interest or royalties.

Risk requirements
Section 8c of the Corporate Income Tax Act 1969 is particularly relevant to service providing entities (see Section 2.2), but this is not necessarily the case. This article may also apply to companies that do not fall within the definition of service providing entity. Article 8c of the 1969 Corporate Income Tax Act stipulates when interest and royalty receipts of a company are taken into account in determining its taxable profit. This is the case if the equity is at least 1 per cent of the outstanding loans or at least EUR 2 million (whichever is lower). In that case, the taxpayer company is deemed to face a real risk concerning the interest and royalty receipts and may take the income it receives from interest and royalties and the payment thereof into account when determining its taxable profit. Any withholding tax levied in the source country can be offset against Dutch corporate income tax only if this income and expenses can be included in the determination of the taxable profit It should be noted that in many cases the purpose of an interest and royalty conduit entity will be to gain access to the Dutch treaty network rather than to settle foreign withholding tax in the Netherlands.

Section 8c of the 1969 Corporate Income Tax Act builds on the Decree of 30 March 2001, no. IFZ2001/294M, the policy on the provision of certainty in advance and on the restriction of withholding tax relief for intra-group financial service providing entities. That policy concerned the tax consequences of related transactions envisaged by such entities for which interest or royalty payments are received and paid (or repaid). When this policy was introduced in 2001, it was decided that a minimum amount of EUR 2 million in equity capital was sufficient for Dutch taxpayers to meet the actual risk requirement.

If the interest and royalty receipts do not form part of the taxable profit, the company must nevertheless recognise separate business expenses for the functions performed relating to the receipt and payment of interest and royalties.[81] Often this will be a remuneration related to the company's own operating costs and a small margin for facilitating the transactions in view of the absence of substantial risks. The foreign withholding tax can therefore not be set off. In addition, in such a situation, the source country from which the payments originate cannot regard the company as the 'beneficial owner' of the payment because the interest or royalty payments have not been subject to tax in the Netherlands. If the company is not regarded as the 'beneficial owner' of the payments, it is not entitled to the (lower) withholding tax rate agreed in the tax treaty between the Netherlands and the country from which the payments are made (the source country). In such a situation, it is not attractive to use the Netherlands for such a conduit activity.

Many conduit structures are designed to benefit from a 0% withholding tax (or else at the low treaty rate) on interest and royalty payments under the tax treaty between the Netherlands and the source country. Whether or not the interest and royalty flows then form part of the tax base in the Netherlands is immaterial given the set-up of the structure, unless the source country is unwilling to apply the treaty rate. This means that Section 8c of the 1969 Corporate Income Tax Act has little meaning in restricting the low-substance flow of interest and royalties if the source country does not levy withholding tax.

80 This assumes that the recipient is the beneficial owner and the PPT does not apply.
81 This information is exchanged with the source country.

Real presence requirements
The minimum requirements have not proved to be a real obstacle to setting up qualifying service providing entities in practice. The first two requirements concerning the company's management could easily be met by the use of competent staff from trust and company service providers who formed the management board together with a member of the management board residing abroad. In addition, the 2 million requirement for the appropriate risk on equity means that the reduction of this risk, often by means of contracts concluded with related parties, up to an amount of up to 2 million euros is considered appropriate by definition.

The Advisory Committee on Taxation of Multinationals has already advised that Article 8c of the 1969 Corporate Income Tax Act be amended. The proposed amendment removes the statutory interpretation of the concept of 'appropriate shareholders' equity', which means that the measure will apply sooner or can be structured less easily.[82] The Committee supports this proposed change, which removes the largely arbitrary minimum risk requirement.

4.3.2 Article 3a of the PSI Code (exchange of information on service providing entities)

When the renewed APA/ATR policy was introduced in 2001, actual presence requirements were set for obtaining certainty in advance through an APA or ATR for service providing entities. Failure to comply with these requirements meant that no certainty could be obtained and possibly also that information was exchanged spontaneously with the countries involved in the activities carried out by the taxpayer. The lack of certainty in advance and the possibility of information exchange was expected to inhibit the establishment of non-qualifying service providing entities.

In a review of the APA/ATR policy in 2014, it was decided to intensify the automatic provision of information to the relevant foreign country in situations where the minimum requirements for service providing entities have not been met. To this end, Article 3a of the ITC (exchange of information on service providing entities) was introduced on 1 January 2014.

Article 3a UB WIB (Implementing decision on The International Assistance (Levying of Taxes) Act) stipulates that service providing entities must submit certain information on their presence in the Netherlands on their own initiative within an international group context. If a service providing entity indicates that it does not have sufficient presence in the Netherlands, the Tax and Customs Administration will spontaneously (i.e. without a request to that effect) pass on information about this service providing entity to the treaty partner or EU Member State concerned. The purpose of this stipulation is to prevent the improper use of provisions relating to withholding taxes on interest and royalties in treaties or the EU Interest and Royalties Directive.

Based on the information obtained, the source country may rule that the service providing entity is not a beneficial owner and is therefore not entitled to 0% or reduced withholding tax on interest or royalties. However, even if the service providing entity should be regarded as the beneficial owner, the source country could refuse the 0% or lower treaty rate based on an anti-abuse provision in the applicable tax treaty, such as a PPT, or in the case of an EU Member State based on the "Danish rulings", on the grounds of the absence of a relevant (actual) presence in the Netherlands. Both the PPT and the Danish rulings are discussed in more detail further on in this section.
To establish whether a service providing entity has an actual presence in the Netherlands, Article 3a UB WIB (Implementing decision on The International Assistance (Levying of Taxes) Act) incorporates

[82] Rapport Adviescommissie belastingheffing multinationals (Report by the Advisory Committee on Taxation of Multinationals), 15 April 2020, p. 102 and 128.

the substance requirements included in the 2001 service providing entity Decree. These substance requirements related until 1 January 2021 to:

- the domicile of the board members;
- the professional knowledge of the board members;
- the presence of qualified personnel;
- the place where board decisions are made;
- the place where the bank accounts are held;
- the place where the accounts are kept;
- the business address;
- resident under an applicable tax treaty (not actually located in another country);
- the actual risk as referred to in Article 8c of the Corporation Tax Act 1969 that the service providing entity incurs concerning the interest or royalties; and
- an equity capital appropriate to that risk.

Given the nature and scope of a service providing entity's activities, the performance of those activities could also be left to a third party, such as a trust and company service provider.

As of January 1, 2021, a wage requirement of at least € 100,000 and the requirement of office space at the service providing entity's disposal for at least 24 months have been added to the substance requirements. The requirements for the business address and treaty residency have been removed. On balance, this has raised the threshold for meeting the substance requirements. The wage requirement does not imply that it must be an employee employed by the service providing entity who performs the work. That may still be done by a third party. The cost of maintaining a service providing entity did however go up.

In practice, these substance requirements work as a kind of minimum that must be met to prevent the automatic transmission of data abroad. To the Committee's knowledge, the spontaneous exchange of information on substance is unusual in an international context. Therefore, exchanging information with the receiving country may be seen as a 'red flag' and prompt tax administrations not to grant the treaty benefits. On the one hand, Article 3a UB WIB (Implementing decision on The International Assistance (Levying of Taxes) Act) has a preventive effect (because conduit companies are anxious to avoid receiving further attention from foreign tax authorities); on the other, this article also acts as a "safe harbour", ensuring that sufficiently "dressed-up" service providing entities are left alone.

The State Secretary of Finance has announced that he considers it obviously necessary to extend the scope of the mandatory exchange of information.[83] He noted that he is looking into the possibility of a change taking effect on 1 January 2022.

4.3.3 Adaptation of the approach to cooperatives

Public and private limited companies are, in principle, subject to withholding tax on dividends. Until 2018, a cooperative was usually exempt from withholding Dutch tax on profit distributions. Although cooperatives were primarily formed in the agricultural sector in the past, there is no ban on their use within a group of companies. As a result, cooperatives in international structures have been used to avoid paying dividend tax from the Netherlands since the beginning of this century.[84] Since 1 January 2018, this has been made less attractive by the introduction of a withholding obligation for

[83] Cabinet response to the report "Op weg naar balans in de vennootschapsbelasting" (Towards a balance in corporate taxation) by the Advisory Committee on the taxation of multinationals, 15 September 2020.

[84] The shares of Dutch holding companies in particular were then held by a cooperative and distributions could then be made within the Netherlands without the actual levy of dividend tax. Further distributions were not subject to any tax. This was generally accepted, also by the Tax and Customs Administration, because there are many other ways to avoid the levy of Dutch dividend tax, and there have been plans to abolish the dividend tax for some time.

what are known as holding cooperatives.[85] A holding cooperative is defined as a cooperative whose actual business consists mainly of holding participations or directly or indirectly financing bodies or natural persons linked to it. A bill is currently before the House to further tighten up legislation on cooperatives. This bill also makes non-resident cooperatives subject to taxation in certain cases. The Committee discusses this in more detail in the following section, 'Conditional withholding taxes on interest, royalties and dividends'.[86]

4.3.4 Conditional withholding taxes on interest, royalties and dividends

As of January 1, 2021, a conditional withholding tax on interest and royalties to LTJs and in abusive situations has been operated in the Netherlands (Withholding Tax Act) (Wet bronbelasting 2021). As indicated in Section 4.2.3, this introduction breaks with the past, when the Netherlands was characterised by the absence of withholding taxes on interest and royalties.

The purpose of the Withholding Tax Act 2021 is twofold. On the one hand, to prevent the Netherlands being used as a gateway to LTJs and, on the other, to reduce the risk of tax avoidance by shifting the (Dutch) tax base to LTJs[87]

If the withholding tax applies, a rate equal to the highest statutory rate in corporate income tax applies. Withholding tax applies to interest and royalty payments made to affiliates in LTJs. The concept of qualifying interest is used for the affiliation. A qualifying interest exists if an entity can directly or indirectly influence the decisions of a body that determines its activities.

The starting point in the Withholding Tax Act 2021 is that it applies to direct payments. However, withholding tax is also payable in the case of artificial structures designed to avoid Dutch withholding tax. This is because withholding tax could otherwise easily be avoided by paying the interest or royalties not directly to an entity resident in an LTJ, but artificially through an entity resident in a high taxing jurisdiction (HTJ). The payment to a hybrid entity that is not domiciled in an LTJ will also be subject to withholding tax.

One month after the end of the calendar year, a withholding entity must report the withheld withholding tax on interest and royalties and remit the withheld tax to the Tax and Customs Administration. In the course of 2022, it will be possible to see for the first time whether the flows, as envisaged by the government, have virtually ceased to exist or have shifted. A measurement of the impact of withholding taxes on interest and royalties will probably not be possible until 2023.[88]

As a follow-up to the 2021 Withholding Tax Act, the Cabinet announced in its letter of 29 May 2020 that it will take measures against dividend flows that can be distributed untaxed under current legislation and regulations [89]to entities established in LTJs.[90] The additional measures are included in the bill to introduce conditional withholding tax on dividends that was submitted to the House of Representatives on 25 March 2021.[91] The bill integrates the measures relating to dividend flows into the Withholding Tax Act 2021.

---

85 Parliamentary Papers II 2017/18, 34788.
86 Parliamentary Papers II 2017/18, 34788.
87 See, inter alia, Parliamentary Papers II 2019/20, 35305, no. 3.
88 Parliamentary Papers II 2019/20, 25087, no. 259.
89 Although dividend payments to LTJs are already subject to withholding tax of 15 per cent.
90 Parliamentary Papers II 2019/20, 25087, no. 259.
91 Parliamentary Papers II 2020/21, 35779 no. 2.

Unlike the withholding tax on interest and royalties, the Netherlands already had a withholding tax on dividends. Based on the Dividend Tax Act 1965 (Wet DB 1965), 15 per cent dividend tax is levied. Despite this withholding tax on dividends, the government felt that there were two situations not subject to dividend tax and for which this was considered undesirable. More specifically, the bill proposes additional measures to prevent the following flows of corporate dividends from flowing untaxed to an LTJ:

- intra-group profit distributions to entities established in LTJs with which the Netherlands has a tax treaty[92]; and
- Intra-group profit distributions to entities established in an AIF by so-called non-resident cooperatives (see also paragraph 4.3.3 *Adjustments to the approach to cooperatives*).

If the bill is approved by parliament, the scheduled effective date is 1 January 2024. As with the withholding tax on interest and royalties, the measure's effects will only become apparent several years after it takes effect.

4.3.5 The Danish rulings

The effect of the Danish rulings of 26 February 2019 may also impact the countering of conduit companies. In these rulings, the CJEU ruled that the Member States are obliged under the EU law abuse principle to refuse benefits granted by EU law, such as benefits under the Parent-Subsidiary Directive or the Interest and Royalties Directive if EU law is abused.[93] In addition, the CJEU has given a further interpretation of the concept of abuse. The CJEU operates a substantive approach. It cannot be ruled out that in a situation in which the substance requirements are met, assessed on the basis of all the facts and circumstances, there may nevertheless be abuse as set out in the judgments. The Danish rulings have led to changes in corporate income tax and dividend withholding tax, where the existing substance requirements no longer function as a safe harbour but instead play a role in the allocation of the burden of proof.

In the rulings of 26 February 2019, the CJEU addresses the EU law abuse principle concerning the exemption of withholding tax. The CJEU does not explicitly rule on the EU-law principle of abuse or the exemption of profit distributions from a parent company from its subsidiary. According to the government, it will be necessary to wait for further case law to determine the consequences for the Dutch participation exemption.[94]

4.3.6 Principal Purpose Test

Under the PPT, a benefit under a tax treaty will not be granted if, taking all relevant facts and circumstances into account, it is reasonable to conclude that obtaining that benefit was one of the principal reasons for an arrangement or transaction that resulted in that benefit. The PPT aims to prevent the improper use of the Dutch treaty network, including the use of the reduced rates of withholding tax in the tax treaties concluded by the Netherlands. The Netherlands aims to include a PPT in its tax treaties. If a tax treaty between the Netherlands and another state contains a PPT, it is up to that other state to refuse the treaty benefits. This can be difficult to do, for example for developing

---

[92] No dividend tax is currently withheld from these profit distributions because the withholding exemption of Article 4(2) of the Wet DB 1965 applies to them. The withholding tax on dividends could also be reduced on the basis of the applicable treaty. The Netherlands will not levy dividend tax pursuant to Article 4(2) of the DB 1965 Act if a tax treaty applies. The conditional withholding tax on dividends could be reduced under a treaty.

[93] CJEU 26 February 2019, joined cases C-116/16 (T Danmark) and C-117/16 (Y Denmark) and CJEU 26 February 2019, joined cases C-115/16 (N Luxembourg 1), C-118/16 (X Denmark), C-119/16 C-Danmark I, and C-299/16 (Z Denmark).

[94] Cabinet response to the report "Op weg naar balans in de vennootschapsbelasting" (Towards a balance in corporate taxation) by the Advisory Committee on the taxation of multinationals, 15 September 2020.

countries, because it requires insight into the nature and activities of the Dutch taxpayer. However, any information exchanged by the Netherlands may be useful to other countries.

Currently, under the Multilateral Instrument (MLI), a general PPT applies to the Dutch tax treaties with 41 countries, including 8 developing countries.[95] However, the PPT cannot be applied to treaties not covered by the MLI. The *main purpose test*, similar to the PPT, included in some treaties has a more limited scope, namely to the dividend, interest and royalty article of the treaty.

4.3.7 The revised ruling policy

In a conduit situation, it may be interesting to obtain certainty about the participation exemption for inbound dividends, the withholding exemption for outbound dividends or the appropriate remuneration that a service providing entity must declare in the Netherlands.

Since 1 July 2019, it is necessary to have sufficient economic nexus in the Netherlands to be eligible for pre-consultation (of an international nature). This means that 'the applicant entity forms part of a group of companies that carry out operational activities in the Netherlands and, moreover, that carry out operational activities at the expense and risk of the applicant entity, for which a sufficient number of relevant staff is present in the Netherlands at group level'.

Letterbox companies are therefore not eligible for a ruling. Companies are currently classified into three groups. If the company does not meet the substance requirements for the service providing entity, the Netherlands will spontaneously provide information on these companies to other relevant states. If the company does meet the service providing entity criteria, this does not mean that it will be able to obtain a ruling. To obtain certainty in advance, the company must meet the nexus requirements. In addition to the economic nexus, no ruling can be concluded if tax savings in the Netherlands or abroad are one of the main objectives of a transaction or arrangement. Prior certainty will also not be obtained if a low-tax country is involved in a transaction or structure. Other than that, all international agreements made will be exchanged and published (anonymously) in summarised form.

When it comes to obtaining certainty in the form of a tax ruling, the Netherlands is no longer an attractive country for conduit companies lacking substance. On a more general note, it is impossible for a conduit company to obtain a tax ruling under the new ruling policy, as such a company will not have sufficient economic nexus.

4.4 Monitoring the effects of fiscal policy measures

Monitoring the effects of anti-avoidance measures is very difficult in practice for statistical and methodological reasons, as explained in the Parliamentary letter *on monitoring the effects of the tax avoidance approach*.[96] For example, there is no single measure of tax avoidance and reliable data is not always available. Also, the causal link between policy measures and a measure of tax avoidance is difficult to establish in practice. This is because the extent of tax avoidance can also be influenced by external factors, such as foreign legislation or cyclical developments. For example, recent research shows that the Netherlands' inbound royalty flows from Ireland have largely dried up due to the US tax overhaul.[97] The tax reform introduced by the US in 2018 may have a greater effect on conduit activity through the Netherlands than Dutch policy measures. In short, it is not possible to measure

[95] See https://www.rijksoverheid.nl/onderwerpen/belastingverdragen/documenten/brochures/2020/02/17/multilateraal-instrument-mli-en-nederlandse-belastingverdragen.

[96] See Monitoring Letter (2020); Parliamentary Papers II 2019/2020, 25087, No. 259.

[97] Coffey et al (2021). The changing nature of outbound royalties from Ireland and their impact on the taxation of the profits of US multinationals.

what would have happened without the policy measure (there is no counterfactual). This makes it difficult to monitor the (isolated) effect of policy measures. It should also be noted that the figures are at least two years behind the actual figures because of the lead time for settling assessments and then statistical processing of assessment data.

In the absence of a good definition and data, some studies focus on FDI as a proxy for the size of structures aimed at tax avoidance. However, this is not a very good indicator to monitor tax avoidance because FDI includes real investments. Some studies therefore look specifically at the FDI liabilities or assets of SPEs, but again, this need not involve tax avoidance as the use of an SPE may also be motivated by non-tax motives. Appropriate indicators are sometimes available for specific types of tax a and related countermeasures. For example, the State Secretary for Finance has announced[98] plans to monitor the effects of the conditional withholding tax on interest and royalties based on the outgoing income flows from SPEs to LTJs.[99] This appears to be a good measure of tax avoidance because there are few other (plausible) explanations for these flows. The withholding tax came into effect in 2021 and, due to the prohibitive effect of the law, it is expected that interest and royalty flows from the Netherlands to LTJs will almost entirely cease to exist or be shifted.[100] In the course of 2022, it will be possible to see for the first time how much withholding tax has actually been paid. A measurement of the impact of the withholding tax can probably only be carried out in 2023.[101] [102]

At the same time, the continuous reclassification of S.127a entities (the SPEs), with an increasing number of entities no longer classified as financial but as non-financial, is problematic for the proposed monitoring approach. Due to this reclassification, entities fall outside S.127 and are no longer monitored. In the future, such reclassification is also envisaged for a number of companies with large royalty payments to LTJs. Therefore, it is recommended that the monitoring of conditional withholding taxes on interest and royalties should cover income flows to LTJs from a wider group of companies than just SPEs. In addition, the Committee notes that it would be desirable to make a distinction in the analysis, where possible, between different types of outgoing income flows of SPEs. Indeed, Section 3.4 shows that dividend, interest and royalty flows follow very different patterns.

4.5 International context

4.5.1 OECD/Inclusive Framework

As a follow-up to the OECD/G20 BEPS project, the OECD/Inclusive Framework has continued to explore adjustments to the internationally accepted conventions on the taxation of internationally operating large corporations in the context of taxation in the digitising economy. In this context, a project was started around two ‘pillars’.

[98] See monitoring letter (2020); Parliamentary Papers II 2019/2020, 25087, No. 259.

[99] These are jurisdictions with a statutory corporation tax rate lower than 9 per cent. Ideally, the average effective rate would be considered here, but there is no data for this.

[100] This is in line with the results obtained by Van 't Riet and Lejour (2019) in their simulations for the Netherlands. Riet, M. van 't and A.M Lejour, Network analysis of a Dutch conditional withholding tax on interest and royalties, CPB Policy Document (November 2019).

[101] See Monitoring Letter (2020); Parliamentary Papers II 2019/2020, 25087, No. 259).

[102] For the final evaluation of this measure, the SEO (2018) suggests in its baseline report carry out a difference-in-difference analysis comparing the average effect of low-tax jurisdictions with the average effect for jurisdictions that have a corporate tax rate marginally higher than the nine per cent threshold. In this way, external factors can be disregarded as far as possible.

Pillar 1 deals with whether the distribution of tax rates should be adjusted and appears to be moving toward allocating tax rates more on the basis of a company's sales in various countries. Pillar 1 does not seem to have any direct impact on conduit companies.
Pillar 2 focuses on measures to ensure that large internationally operating companies pay a minimum level of tax. If countries to which the taxing right is initially allocated - based on the traditional approach in combination with the measures from pillar 1 - levy too little profit tax, other countries must be able to levy up to an agreed minimum level.

Pillar 2 comprises three categories of measures:
- The income inclusion rule (IIR), where the country of the (top or intermediate) holding company makes an additional payment when the subsidiaries are insufficiently taxed.
- The under-taxed payments rule (UTPR) whereby the country of a group company that cannot apply the IIR can deny the deduction of payments (or else make an adjustment) when insufficient tax is levied on a (related) company.
- The subject to tax rule (STTR) aims to create the possibility for source countries that have agreed in a bilateral treaty on a lower withholding tax rate than their national rate to set aside that agreement and levy up to an agreed minimum rate.

The IIR and the UTPR are applied after the STTR has been applied.

Of these three measures, the STTR appears to have the most direct potential impact on conduit companies. Under the STTR, the source country would be allowed to levy a minimum tax even if a tax treaty limits the source country's taxing rights on certain payments. The source country would be allowed to do so if the payment in question is insufficiently taxed in the recipient country. Whether this is the case would have to be assessed on the basis of the statutory tariff in the recipient country, taking account of preferential adjustments. The STTR applies only to certain payments or income items (called covered income). These include in all cases interest, royalties and (re)insurance premiums. The STTR only applies to provisions between affiliated entities, where the controlling interest is at least 50 per cent. The STTR will be extended with a targeted anti-abuse provision to combat back-to-back structures to prevent its circumvention. The minimum tax that may be levied under the STTR is likely to be limited.

Some payments to affiliated entities in low-tax countries may be subjected to the STTR. It should be noted that dividends will not be regarded as covered income. Therefore, the STTR will not affect holding companies in, or the flow of dividends through, the Netherlands. Furthermore, the added value of the STTR for the Netherlands as a source country appears to be limited to the possibility to levy conditional withholding tax on interest and royalties in more cases where this is currently not possible or only possible to a limited extent under an applicable tax treaty. As the scope of covered income has not yet been defined, it is not possible to anticipate the global implementation of the STTR.

The indirect effect of the above-mentioned Pillar 2 measures on conduit companies is potentially greater. If these measures actually succeed in imposing a 15% 'floor' in the effective tax burden on corporate profits, the raison d'être of those conduit activities that currently achieve a lower effective pressure will be lost. As it is not known how much tax savings Dutch conduit companies generate for the groups to which they belong, the concrete significance of this indirect effect cannot be quantified.

4.5.2 EU initiatives

The European Committee issued a Communication on Business Taxation in the 21st Century on 18 May 2021 with the background of promoting a robust, efficient and equitable tax system for

companies in the European Union.[103] The Communication presents both a short- and long-term vision to support Europe's recovery from the COVID-19 pandemic and ensure adequate public revenue in the coming years.

Part of the communication is a tax agenda for the next two years with several measures envisaged, one of which is to 'counteract abuse by shell entities for tax purposes'. This could take the form of a directive, commonly referred to as the Third Anti-Tax Avoidance Directive 3 (ATAD 3), although it is not yet certain whether the European Committee will present a proposal for a directive.

The Committee believes that it is in the interest of the Netherlands, as a major host country for conduit companies in the EU, to make an active contribution to an EU directive. To this end, it proposes two principles, which must of course be further elaborated in concrete rules.

The first premise is negative. As noted above, about 90 per cent of the conduit companies established in the Netherlands do not have their own staff. Whatever the previous policy views, it is currently considered undesirable for these companies to have access to tax or non-tax rules that are attractive to them. However, the number of options for getting rid of this large group of insubstantial companies is modest from a national law perspective. However, tax disincentives for non-substantial companies (e.g. by making all their outgoing payments subject to withholding taxes, by not granting them the participation exemption, or by not regarding them as residents) quickly lead to the risk of conflict with EU law or tax treaties. An EU initiative in this regard is very welcome.

The second principle is positive, and aims to set a possible goal for an EU directive. It means that Member States will lay down in their national rules that conduit companies are subject to withholding taxes at a prohibitive rate unless these companies demonstrate a proper function within their group. The directive then regulates concepts such as conduit company, group, and proper function. For the concept of a conduit company, following the Danish rulings, a relative substance test can be applied. The concept of a group has been sufficiently developed in the regulations, at least for companies. The outcome to be achieved is that conduit companies will disappear from the EU insofar as they are aimed at tax savings.

Specific recommendation for ATAD 3

Unilateral measures cannot prevent other countries from taking over or maintaining the role of conduit countries. International agreements are therefore also needed to prevent international tax avoidance through 'shell entities'. The Committee therefore recommends that the Netherlands adopt a constructive attitude towards the current European Commission initiative.

[103] Communication on Business Taxation for the 21st Century, COM(2021) 251 final.

5 What is the role of non-tax factors?

5.1 Introduction

For various reasons, the Netherlands is an attractive country for foreign multinationals to set up a company without necessarily having any production or other physical activities there. In many cases, these are holding and finance companies.

The committee's investigation shows that, in addition to taxation, other factors play a role in establishing a conduit company in the Netherlands. Section 5.2 discusses the generally favourable business climate in the Netherlands, pointing to the good legal infrastructure, including the presence of knowledgeable service providers such as lawyers, civil-law notaries and tax consultants, but also the proper administration of justice.

Dutch company law itself is also cited as a reason for establishing a conduit company in the Netherlands. The possibilities of shaping the legal form of a company are broad and flexible compared to other countries. Section 5.3 discusses this in more detail. In addition, the bilateral investment treaties concluded by the Netherlands reduce the risk for investors in the Netherlands and abroad. The importance of bilateral investment treaties is explained in section 5.4.

5.2 Business climate

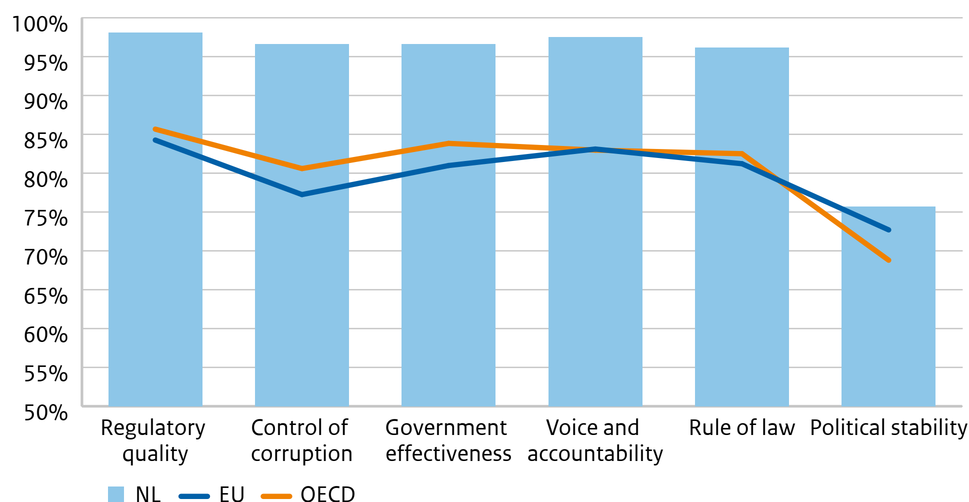
A country's business climate can be defined as the attractiveness for internationally operating companies to establish themselves in that country. In addition to fiscal factors - as discussed in Chapter 4 - the general business climate is also determined by factors such as reliable (digital) infrastructure, a well-educated workforce, efficient and predictable regulations, and legal and political systems that offer assurance and stability. These factors are often analysed using well-known competitiveness indexes such as the World Economic Forum's Global Competitiveness Index. The Netherlands often scores well on these indicators[104]

However, because of the limited physical presence of conduit companies in the Netherlands by definition, not all of these factors appear to be equally relevant to the decision on the establishment of these companies. For example, factors such as physical infrastructure and access to utilities and healthcare seem less relevant. This view has been confirmed in various interviews the committee has held with experts, such as the NFIA, which have placed particular emphasis on independent, effective and stable government institutions. This section, therefore, looks more specifically at how the Netherlands scores on the World Bank governance index indicators, which assigns a score to such institutions based on six indicators.[105] Figure 14 presents these scores - expressed in deciles - for the Netherlands, the EU and the OECD. The Netherlands scores higher than the EU and OECD average on all factors and is among the top five highest-scoring countries on five of the six indicators. This confirms the perception of the Netherlands as a reliable, flexible and stable country. With specific reference to access to the law, it was noted in interviews that it was easily accessible and that the Enterprise Chamber had a good reputation for settling disputes quickly and competently (the law itself is discussed in section 5.3).

[104] World Economic Forum (2020). Global Competitiveness Report Special Edition 2020: How Countries are Performing on the Road to Recovery.

[105] World Bank (2021). Documentation on Worldwide Governance Indicators. WGI 2020 Interactive > Documentation (worldbank.org)

Figure 14: Comparison World Bank governance indicator Netherlands, EU and OECD - 2020



Source: World Bank

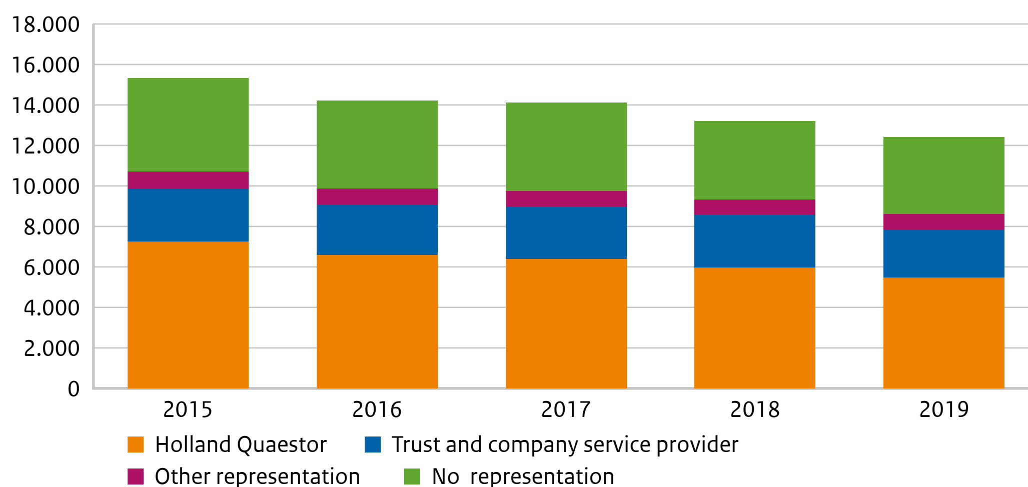
Another reason for conduit companies to establish themselves in the Netherlands is the presence of a (traditionally) large legal infrastructure, including the presence of good professional service providers such as lawyers, civil-law notaries, tax consultants, accountants and trust and company service providers. For example, Amsterdam ranks 9th of financial centres in Europe and 28th worldwide.[106] In addition, as we saw in Chapter 3, 90 per cent of the conduit companies have no employees in the Netherlands. A large proportion of these companies therefore have themselves represented by a trust and company service provider: a firm engaged in the management of corporations. These offices provide services such as offering a registered address (domiciliation), accounting services and arranging natural or legal persons as directors. Figure 15 shows that approximately 65 per cent of the conduit companies in the Netherlands are represented by a trust and company service provider, many of which are affiliated to Holland Quaestor, a trade association for trust and company service providers in the Netherlands. Recent SEO research shows that some trust and company services are also offered illegally (see also section 6.3).[107] It emerged from various discussions and the round tables that the large and specialised business services and trust sector make the Netherlands an attractive country for the establishment of conduit companies. This is also partly seen as a remnant from the period when the Dutch tax system was internationally still much more attractive for conduit companies.

The fact that investors from different jurisdictions sometimes choose a country that they consider to be legally neutral may also play a role in their choice of establishment in the Netherlands. This can be an important reason for choosing the Netherlands if companies from two different, relatively large countries decide to set up a joint venture. The fact that certain companies have no, or limited, activities in the Netherlands can therefore also be a factor that contributes to the attractiveness as a neutral place of establishment for holding companies.

[106] The Global Financial Centres Index Competitiveness GFCI 29 Rank - Long Finance

[107] The category of other representation in Figure 12 refers to representation by, among others, lawyers, accountants or civil-law notaries.

Figure 15: *Number of S127 entities by type of representation*



Source: DNB, based on microdata

5.3 Corporate law

Compared to other countries, the Netherlands has a flexible corporate law system concerning both the legal forms of entities and their organisation.[108] The introduction of the 'flex-BV' has contributed to this. In popular terms, you can set up a Dutch company however you like because Dutch company law consists to a large extent of regulatory rather than mandatory law - in contrast to many other legal systems. This has led to a certain popularity of Dutch companies among foreign multinationals, for example German multinationals wishing to go public in the United States. Another well-known example is establishing a Dutch holding company by Italian listed companies whose shares are partly held by a family to acquire or maintain a majority of voting rights.[109] Furthermore, many top Dutch holding companies that are part of a foreign group are resident for tax purposes in another country. This means that they are subject to tax in another country and are therefore not eligible for any tax relief in the Netherlands. It is also important to note that the Netherlands has what is known as the 'registered office doctrine'. This means that to establish a company, such as a private or public limited company, it does not necessarily have to be physically present in the Netherlands, as long as its registered office is there. This is in contrast to certain other countries, which have the 'actual registered office doctrine', which requires companies to be physically present.

It is not possible to objectively list all the elements that make the Netherlands a suitable country for foreign groups to establish a company because the Committee does not have a clear comparison with neighbouring countries. In general, the Netherlands has a good legal and administrative infrastructure, including up-to-date registers of the Land Registry and the Chamber of Commerce. A number of more specific elements that are known to play a role are described below.

[108] The Minister of Security and Justice also wrote in the letter on the modernisation of company law (Parliamentary Papers II, 2017-17, 29 752, no. 9, p. 6) that "company law aims to contribute to the Dutch business climate. The facilitating character of company law is in line with this objective. Entrepreneurs are given the freedom to choose the most suitable legal form for their company and within that legal form to adapt the layout to their wishes."

[109] FD 18 September 2020, 'How the Netherlands became the top location for Italian companies'.

A number of elements that may play a role are described below.

- First, a company can be established within a short period of time and, by extension, a company structure can be changed.
- Secondly, the possibility exists to issue shares with a low nominal value or without voting or profit rights or to certify shares. Depositary receipts mean that shares with voting rights are placed with a trust office foundation ('Stichting Administratiekantoor' or StAK) and depositary receipts for those shares are issued with certain rights, such as the right to profit. The foundation thus retains control over the shares. This makes it possible to set up structures that offer protection against hostile takeovers. By extension: it is possible in the Netherlands to set up different share structures to protect certain interests, such as different classes of shares with different voting rights, dual and loyalty voting, and preference shares.
- Thirdly, it is relatively easy to make capital changes, such as share deposits, withdrawals and repurchases.
- Fourthly, the possibility of paying out (interim) dividends is also mentioned. Some countries have more restrictions on dividend payments, for example in the case of a negative revaluation of a foreign subsidiary.
- Fifth, the board can be authorised in advance to issue shares for the next few years. Some other jurisdictions more often require the approval of a meeting of shareholders for specific actions by the board of a company.

Sometimes foreign groups have a large number of companies in the Netherlands for legal reasons. This layering is intended for risk spreading within a group, whereby different assets or activities are placed in separate entities. A second reason is that this may be the result of mergers or acquisitions. A (complete) legal restructuring involves a lot of work without necessarily having to. It is then easier to leave the whole 'Christmas tree' of companies intact. There may also be cooperation involving different parties at different levels, in which case the alliance structure is based on various entities. The Committee has the impression that the advantage of setting up companies in the Netherlands, compared to other countries, lies partly in the possibilities for protecting certain interests, particularly the interests of the management board and the sitting shareholders. Dutch companies are also set up to protect (or shield) foreign assets. It is known that in some cases Russian or African interests have been transferred to Dutch entities to prevent them from falling into the hands of local authorities.

5.4 Bilateral investment treaties

An bilateral investment treaty protects investments abroad. This reduces the risk for investors. For example, the Netherlands has concluded bilateral investment treaties to encourage Dutch companies to invest abroad and foreign inward investment. At the time of publication of this report, the Netherlands had concluded an bilateral investment treaty, or a comparable treaty, with more than 90 countries.[110] [111] The Dutch bilateral investment treaties were concluded mainly with emerging economies.

The Dutch bilateral investment treaty model convention of 1990-2000 has been followed in many countries. As a result, the Dutch bilateral investment treaty model was considered the "gold standard" for a long time. The bilateral investment treaties offer a high degree of (legal) protection to the investor, comparable to the protection under Dutch law. The Dutch bilateral investment treaties include a provision that a foreign investor may not be treated worse than a national or other foreign investor (non-discrimination provisions), the right to reasonable and fair treatment and a provision that compensation must be paid in the event of expropriation. The bilateral investment treaty model

[110] Country List Bilateral investment treaty May 2021 | Report | Rijksoverheid.nl.

[111] Not all of these conventions are in force.

in force at the time was based on broad access: every natural person with Dutch nationality and every Dutch legal entity with investments in the country of the other contracting party falls under the scope of the bilateral investment treaty.

The bilateral investment treaties give foreign investors the right to resort to the dispute settlement mechanism provided for in the treaty, ISDS (Investor State Dispute Settlement) or investor-state arbitration. The total number of ISDS lawsuits filed worldwide in recent decades stands at 1104.[112] In 2020, 68 ISDS cases were initiated. Investors from developed countries filed the most - about 70 per cent - of the 68 known cases. Most cases were brought by investors from the United States (10 cases), the Netherlands (7 cases) and the United Kingdom (5 cases).[113] The image of the Netherlands in 2020 corresponds to the image of all decades. A Dutch bilateral investment treaty is used in more than 10 per cent of all known ISDS disputes. More cases are only being filed by investors from the United States[114]

ISDS is a relatively new phenomenon and is subject to change. In practice, the older treaties therefore needed to be improved. For example, it was found that conduit companies made frequent use of bilateral investment treaties.[115] An example is the case of mining company Newmont against Indonesia.[116] Newmont filed an ISDS case under the bilateral investment treaty with the Netherlands in 2014, after Indonesia announced a new mining law. The Committee is not concerned with the substance of this case, but it does note that Newmont could sue the Indonesian government under the Dutch bilateral investment treaty because the majority shareholder was based in the Netherlands under the name Nusa Tenggara Partnership BV. This private limited company was a joint venture between the American mining company Newmont and the Japanese conglomerate Sumitomo. The company had two employees and over a billion euros in FDI assets, consisting of the majority stake in an Indonesian copper and gold mine.

The government considered it undesirable that foreign companies or investors without any connection to the Netherlands could make use of bilateral investment treaties, which is why the Minister of Foreign Affairs recently presented a new model text.[117] [118] Various adjustments have been made in the new model text, including the exclusion of 'letterbox companies'. There must now be 'substantial business activities' to make use of investment protection. The relevant passages in the bilateral investment treaty model text read as follows:

112 World Investment Report 2021, June 21, 2021, p. 129 and site of UNCTAD https://unctad.org/system/files/official-document/wir2021_en.pdf .

113 World Investment Report 2021, June 21, 2021, p. 130.

114 R. Van Os, Rethinking bilateral investment treaties, p. 171 and 176.

115 See e.g. Roeline Knottnerus, Roos van Os, Bart-Jaap Verbeek, Fiona Dragstra, Freek Bersch, 50 years of ISDS, 13 January 2018, p.3, which notes that 77 per cent of total Dutch claims come from 'letterbox companies'.

116 R. Van Os, Rethinking bilateral investment treaties, p. 177 and 178.

117 Policy Document Investeren in Perspective (Investing in Prospects), 18 May 2018.

118 New model text for investment agreements | Publication | Rijksoverheid.nl.

Article 1 – Definitions

(b) "investor" means with regard to either Contracting Party:
[..]
(ii) any legal person constituted under the law of that Contracting Party and having substantial business activities in the territory of that Contracting Party; or
[..]
(c) Indications of having 'substantive business activities' in a Contracting Party may include:
(i) the undertaking's registered office and/or administration is established in that Contracting Party;
(ii) the undertaking's headquarters and/or management is established in that Contracting Party;
(iii) the number of employees and their qualifications based in that Contracting Party;
(iv) the turnover generated in that Contracting Party; and
(v) an office, production facility and/or research laboratory is established in that Contracting Party;
(vi) These indications should be assessed in each specific case, taking into account the total number of employees and turnover of the undertaking concerned, and take account of the nature and maturity of the activities carried out by the undertaking in the Contracting Party in which it is established.

Article 16 Scope of application
[..]
3. The Tribunal shall decline jurisdiction if an investor within the meaning of Article 1(b) of this Agreement, which has changed its corporate structure with a main purpose to gain the protection of this Agreement at a point in time where a dispute had arisen or was foreseeable. This particularly includes situations where an investor has changed its corporate structure with a main purpose to submit a claim to its original home state.

The committee believes that a good step has been taken by excluding letterbox companies. However, there is still criticism of the wording chosen. For example, the definition of 'investor' in the model convention is insufficiently clear; when is there a question of 'substantial business activities'?[119] The real issue here is the choice between an open definition that puts a lot in the courts' hands and a more closed enumeration that easily becomes a safe harbour. The question also arises as to who must prove or disprove that an enterprise has established a company in the Netherlands to submit an ISDS claim (Article 16.3).[120] There will be no rapid clarification on this point as the relevant provisions have not yet been included in any bilateral investment treaty.

[119] This concept is based on the 1994 EU Declaration to the WTO.
[120] Roeline Knottnerus, consultation new model text: critical notes, June 18, 2018.

6 What is the link between tax avoidance and money laundering?

6.1 Introduction

6.1.1 Introduction

One of the questions put to the committee concerns the relationship between tax avoidance and money laundering in the Netherlands. This question follows from the motion by Members of Parliament Snels and Groothuizen[121] of 3 December 2019 calling on the government to investigate (i) the relationship between money laundering and tax avoidance in the Netherlands, and (ii) what this means for the relationship between tackling tax evasion and tackling criminal financial flows.

This chapter first briefly explains the phenomenon of money laundering. The Committee then goes on to look at the relationship between tax avoidance and money laundering. In addition, this chapter looks in more detail at some of the measures taken and announced concerning money laundering. For the underlying question concerning the nature, scope and methods of tax avoidance via the Netherlands, and the role of conduit companies in this, reference is made to earlier chapters, particularly chapters 3 and 4.

6.1.2 What is money laundering?

Money laundering is rendered punishable as a criminal offence in Title XXXA of the Dutch Penal Code. The offence of money laundering is succinctly defined as concealing or hiding the origin or ownership of assets derived from a crime, or which should be reasonably suspected to be derived from any crime, or using or transferring these assets in any way. Important elements in this are that it concerns an act in relation to assets obtained from a crime and that the perpetrator knows, or should know, that it was obtained from a crime. The underlying offence is what is known as a 'predicate offence' for money laundering. Under Dutch law, this is not limited, but certain offences are more obvious, such as tax evasion (see also 6.2.1), which is punishable under article 69 of the General State Taxes Act (AWR).

From a practical point of view, money laundering consists of a number of often intertwined steps that are carried out to profit from criminally acquired assets. For a more detailed explanation of these stages, please refer to the description from the National Risk Assessment Money Laundering 2019[122] (see box 6.1):

Box 6.1: Money laundering phases

"**Placement.** *In this phase the criminal places the money to be laundered in the financial system, thus making it non-cash. A form of crime such as drug trafficking usually involves large amounts of cash that a criminal wishes to place in the financial system. In other forms of crime, the money may already be in the financial system, for example in the case of tax fraud.*
Concealment. *In this phase - which can take place both during and after the placement phase - a criminal conceals his own identity and/or the origin of the criminal money in order to minimise the chance of getting caught. Methods of concealment can be relatively simple or very complex.*
Integration. *In this last phase, a criminal - concealed or not - integrates the criminally obtained money into the financial system, for example by consumer spending or investing in*

The ultimate goal is to make assets with a criminal origin appear legitimate so that they do not arouse suspicion among, for example, trading partners, financial institutions and authorities, and can be used as if they were income from normal business activities. What is important here is the concealment of the (illegal) origin of the assets on the one hand, and the concealment of the

[121] Parliamentary Papers II 2019/20, 31 477, no. 46.
[122] National Risk Assessment Money Laundering 2019, Scientific Research and Documentation Centre.

beneficiary of the assets on the other. In the case of successful money laundering, the assets cannot be traced back to the predicate offences and the criminals who committed them.

When the committee refers to money laundering in its report, it means concealing the illegal origin of assets to ultimately use them in commercial activities. Conduit companies can also play a role in financial structures used to obtain criminal proceeds, which are then laundered. The considerations and risks involved in money laundering generally also apply to predicate financial crime, with concealment playing an important role.

6.2 Concurrence with tax avoidance

6.2.1 Introduction

This section takes a closer look at the relationship between tax avoidance, conduit companies and money laundering. Although tax avoidance, unlike tax evasion, is not prohibited and therefore not a predicate offence for money laundering (see box 6.2), several elements are related to, or result from (tax-driven) conduit activities that can also attract criminal flows and increase money laundering risks.

Box 6.2: Tax avoidance and tax evasion and implications for the study

Tax avoidance and tax evasion are sometimes used synonymously. However, tax avoidance is not prohibited, and therefore not a predicate offence for money laundering. The difference between these two concepts lies in the fact that tax avoidance aims to optimise the payment of tax within the limits of the law, for example by making use of favourable tax treaties. On the other hand, tax evasion is aimed at avoiding taxes outside the limits of the law. Under certain circumstances, however, what appears to be 'regular' tax avoidance may, on closer examination, turn out to be tax evasion. This also applies from the perspective of service providers, such as trust and company service providers, which may be confronted with very complex structures and may therefore be involved, unintentionally or otherwise, in tax evasion. For example, DNB pays attention to this risk in its 'Good practices Tax integrity risks for Trust and company service providers 2019'. [123] The July 2018 FATF report[124] and the Egmont Group[125] on the concealment of beneficial owners notes, about the 106 cases analysed, that tax evasion is one of the most common predicate offences.[126]

Because tax avoidance is not prohibited, and therefore not a predicate offence for money laundering, a direct, numerical link between tax avoidance and money laundering is difficult to establish. For example, there are no statistics on the number of cases where crime is linked to tax evasion. Crime, and money laundering in particular, is by its very nature concealed, sometimes using very complex and professional methods. In addition, tax avoidance via the Netherlands relates to money flows with a foreign origin and foreign destination. The Netherlands only acts as an intermediary so that the Dutch authorities, more so than in the case of domestic crime, have limited insight into the nature of the money flows and any predicate criminal offences. All this makes a more quantitative analysis of this issue complex.

[123] 'Good practices Fiscal integrity risks for Trust and company service providers 2019', De Nederlandsche Bank, 2019
[124] The FATF is an authoritative international organisation that develops anti-money laundering standards.
[125] The Egmont Group is an international partnership of Financial Intelligence Units.
[126] 'Concealment of Beneficial Ownership'. Financial Action Task Force & Egmont Group, July 2018.

6.2.2 Elements

Element 1: Conduit companies

An important element of money laundering is the 'concealment' of the origin and beneficiary of criminally acquired assets. Conduit companies (see 2.3), and the infrastructure surrounding them, are not only an important element in tax avoidance but can also be used to conceal criminal flows of money.

Conduit companies have little or no actual presence in a country and provide an additional legal layer between the (origin of) the assets and the ultimate destination and beneficiaries. This limited actual presence means that there are fewer leads for a possible criminal investigation. The concealing effect of the additional legal layers between origin, assets and beneficiary can also be reinforced by using different jurisdictions. The more 'jumps' made between entities and jurisdictions, the harder it is for national authorities to track money flows. For example, Dutch investigative authorities cannot simply raid foreign business premises or demand foreign data. This means that they rely largely on international requests for legal assistance, which are not necessarily met with a timely and adequate response.

This complexity applies all the more to the 'gatekeepers' of the financial system, such as the banks. In complex international structures with Dutch conduit companies, these will have even more limited means of accurately determining the origin of the assets and the ultimate beneficiaries.

The 2018 FATF and Egmont Group report[127] on the concealment of beneficial owners, to which the Netherlands contributed, cites the use of 'shell companies' in various jurisdictions as a well-known and common method of concealment. The report defines shell companies as entities that do not have independent operations or significant resources, business activities or employees if their own. In the National Money Laundering Risk Assessment[128] (NRA) of the Scientific Research and Documentation Centre (WODC) the AIU-principle is applied to indicate a money laundering risk, which consists of the elements Anonymous, International and Unregulated. In that context, the NRA cites money laundering through legal entities and structures as one of the top ten money laundering threats and the most frequently cited by experts. This threat includes money laundering via arrangements at trust and company service providers, offshore companies and legal forms. The latter includes setting up legal entities (or having them set up) to conceal the ultimate beneficial owner. The more legal entities that are set up or used, the greater the complexity of the money laundering method becomes. Several participants of the Money Laundering Round Table stated in this context that in practice criminals set up structures that are as complex as possible, with as many links and jurisdictions as possible, to conceal the criminal origin of the assets.

To gain an impression of the potential integrity risks in the Dutch conduit companies, an analysis of the representation of S.127 conduit companies in known 'leaks', such as the Panama Papers and Paradise Papers, was carried out in cooperation with the AMLC and with data from DNB[129], with the support of iCOV. This shows an overrepresentation of S.127 conduit companies (see box 6.3).

[127] 'Concealment of Beneficial Ownership'. Financial Action Task Force & Egmont Group, July 2018.

[128] https://www.rijksoverheid.nl/documenten/kamerstukken/2020/07/03/cahier-national-risk-assessment-witwassen

[129] DNB supplied data from its Statistics Division. The input does not come from the Financial Crime Supervision departments that deal with the AML/CFT supervision of Wwft institutions.

Box 6.3: Analysis of (over)representation of s.127 conduit companies in leaks

To gain more insight into the involvement of Dutch conduit companies in money laundering cases, the AMLC and DNB, with support from iCOV, examined how often S127 entities appear in public 'leaks' from the International Consortium of Investigative Journalists (ICIJ).[130] More specifically, we looked at the presence of S.127 entities in the offshore leaks (2013), Panama Papers (2016) and Paradise Papers (2017/2018). If an entity appears in one or more of these leaks, this does not of course mean that these entities are involved in financial crime. Indeed, many of these cases involve legal (aggressive or otherwise) tax planning structures. This is particularly true of the cases in the Paradise Papers. Cases from the Panama Papers may also involve tax planning structures, but here the link to unethical, or even criminal, money flows is stronger than in the Paradise Papers. Ultimately, a legal entity can only be determined with certainty to be involved in criminal acts after a more thorough individual analysis and ultimately a legal ruling. The results found should therefore be interpreted with caution. In that context, it is also relevant to note that the leaks predate certain measures, such as the Wtt 2018.

Analysis of the leaks revealed 542 names of Dutch legal entities, of which DNB could match just under 90 per cent with a known (statistical) category. Of these matches, approximately 90 per cent relate to the Paradise Papers, which indicates that they predominantly concern cases of a tax nature. In terms of entity type, most matches are in the 'financial holding companies' category. This represents 64 percent of all matches.[131] S.127 entities, which also fall under the financial holdings category, account for nearly 40 per cent of all matches. Looking only at the matches with the Panama Papers (approximately 6 per cent of the total number of matches), the share of S.127 entities is 57 per cent. To a certain extent, it is logical that financial service providers, particularly intra-group lenders, are more likely to be involved in the international financial structures that the leaks focus on. At the same time, the share of S.127 entities within the total number of Dutch companies is less than 0.01 percent, implying a solid overrepresentation of S.127 entities in the 'leaks'. This solid overrepresentation could indicate an increased risk of integrity problems in this group. At the same time, a more thorough analysis is required to establish this with greater certainty.

A similar picture of potential integrity risks in conduit companies follows from a recent report by The Sentry[132], which makes links between corruption in the Great Lakes region in Africa and Dutch legal entities. According to the report, there are signs that corrupt money flows from the Great Lakes region, particularly the Democratic Republic of Congo (DRC), are channelled through the Netherlands via conduit companies. The report implies that this is related to the Dutch tax and investment treaties. However, the Netherlands has no tax treaties with the DRC, so tax is not an obvious motive. That said, non-tax factors, such as the desire to keep wealth out of the reach of a particular government (see 5.3), can also play a role. There is more recent case history in which the Netherlands appears to have been used as a conduit country for corrupt money flows, such as the 2019 'Odebrecht' case[133] in which

[130] The AML compiled a list of 561 Dutch legal entities, and their Chamber of Commerce numbers, from the public (leaks) database of the ICIJ. We specifically examined the offshore transactions, Panama Papers and Paradise Papers for this purpose. Using register information from DNB and iCOV and the standard business classification (SBI) codes from CBS, DNB has distinguished between S127 entities, financial holding companies and other entities.

[131] This does not take into account the group structures behind individual entities. In other words, if an S.127 entity is part of a group with other entities, only the S.127 entity is considered. For example, a large Dutch bank may still be considered to belong to S.127 if it has an S.127 entity as part of its group structure. This potentially leads to an overestimation of the number of S.127 entities.

[132] Corruption in the Great Lakes Region and Possible Ties to the Dutch Financial System, The Sentry, 2020

[133] https://www.fiod.nl/aanhouding-en-doorzoekingen-in-onderzoek-naar-faciliteren-corruptie/

bribes were distributed through Dutch conduit companies. There was also a 2016 case[134] in which Spanish corrupt money flows were channelled through the Netherlands ultimately to Algeria with the help of a Dutch trust and company service provider and the Isabel Dos Santos case and the Ematum case (see box 6.4).

Box 6.4: Luanda Leaks[135] and Ematum[136]

Two of the most high-profile corruption cases in recent years involving Dutch conduit companies and service providers are the cases concerning Isabel Dos Santos and the EMATUM case.

Dos Santos is the daughter of a former Angolan president and was considered at one point the richest woman in Africa. Through the 'Luanda Leaks' and the efforts of the International Consortium of Investigative Journalists (ICIJ), it came to light that Dos Santos' wealth had been accumulated to a significant degree through corruption. A network of conduit companies and service providers from various countries, with an important role for the Netherlands, Portugal and Switzerland, was used to control the empire and channel assets.

The Ematum case concerns a scandal in Mozambique in which a number of 'companies' had been set up with the aim, among others, of developing activities in the (tuna) fishing sector. These companies have been lent approximately € 2 billion with guarantees from the Mozambican state. However, no activities worth mentioning have taken place, and a large part of the money, at least EUR 500 million, has subsequently disappeared. A Dutch conduit company, Ematum BV, managed by a Dutch trust and company service provider, was used to raise $850 million on the capital market. Therefore, the money raised through this structure had no illegal origin, but the conduit company did play a role in concealing the financial crime.

Element 2: (extensive) conduit activity

The substantial cash flows associated with tax-driven conduit activities (see also chapters 3 and 4) via the Netherlands may offer opportunities for concealment. As indicated in the FATF and the Egmont Group report, international trade and financial centres are vulnerable to money launderers, particularly from abroad. This is because a presence in such centres is more likely to be seen as legitimate in these countries criminal financial flows can be absorbed into much larger legal financial flows (in terms of both the number and size of transactions). In other words, the large financial flows associated with large-scale conduit activities and tax avoidance may favour anonymity.

The Netherlands is also attractive because of its reputation as a reliable and legitimate trading country. Assets, whether or not of criminal origin, that flow through the Netherlands set off fewer alarm bells than when a country with a lesser reputation is used. This avoids special attention from foreign investigating authorities and the various service providers that act as gatekeepers to the financial system. For example, from the money laundering round table, a picture emerged that the Netherlands is seen as a suitable intermediate station before assets go off-radar in another country, often with a less good reputation.

[134] https://www.transparency.nl/nieuws/2016/08/spaanse-corruptie-gefaciliteerd-door-nederlands-trustkantoor/
[135] https://www.icij.org/investigations/luanda-leaks/
[136] https://www.nrc.nl/nieuws/2021/08/26/hoe-zit-het-met-de-fraude-die-mozambique-zeker-11-miljard-kostte-a4056197

Element 3: Service providers
Another important element, or precondition, for (large-scale) tax avoidance is an extensive infrastructure of service providers. In particular, trust and company service providers have frequently emerged in the Committee's investigation as an important service provider in this respect, given their role in offering, managing, and administering conduit companies. According to DNB's estimate, approximately 65 per cent of the S.127 conduit entities use the services of a trust and company service provider (see 5.2). The recent SEO report on illegal trust services states that the large Dutch trust sector is linked to the favourable climate created by tax and investment treaties. This attracts parties from all over the world who want to channel assets through the Netherlands.

The downside is that various experts and reports associate trust and company service providers with money laundering risks. The 2018 FATF and Egmont Group report identifies trust and company service providers as being widely used to disguise the beneficial owners. The NRA Money Laundering 2019 also mentions that complex arrangements at trust and company service providers pose a money laundering risk. The fact that trust and company service providers can be used for criminal purposes is also evident from an internal analysis by the Public Prosecution Service, which revealed 82 cases in which both Dutch and foreign trust and company service providers were involved in various offences, including money laundering.

However, this problem not only concerns licensed trust and company service providers, but also illegal trust and company service providers. Trust and company services are regulated in the Netherlands in the Trust Offices (Supervision) Act 2018 (Wtt 2018) and in certain respects have stricter requirements than the Prevention of Money Laundering and Financing of Terrorism Act (Wwft), to which, for example, banks are subject. This is related to the increased integrity risk of the trust sector. The above-mentioned SEO report indicates that this strict regulation, together with strict supervision and the associated costs, provides incentives to provide trust services without a licence. DNB had already indicated in its 2019 Supervision of Trust and company service providers that an upward trend was observed in illegal trust services signals. The SEO report estimates the share of the illegal trust sector at approximately 15 percent of all trust and company service providers. This is in itself an indication that there is a demand from rogue parties for trust services (whether or not illegal) because it can be assumed that a bona fide company will generally turn to a legal trust service provider. The NRA money laundering 2019 indicates that the policy toolkit as it relates to trust companies provides a relatively high level of resilience to abuse, but at the same time that this is based on licensed trust companies. The policy instruments do not provide this resilience in the case of illegal trust and company service providers, which evade the requirements of the Wtt 2018. The SEO report states that the number of licensed trust and company service providers is declining and that this trend is expected to continue, partly because of the various tax and legal measures that have been taken in recent years.

Element 4: Financial motive
As mentioned in the FATF and the Egmont Group report, money launderers do not aim to operate in their own criminal economy but to use criminally acquired assets in the real, legal economy. As a rule, part of the money laundering process is then to pay tax on the 'earned' capital to disguise it as income from a normal business activity. In view of this, it may be assumed that a favourable fiscal climate will attract legal money flows as well as criminal ones. After all, money laundering has an important financial motive.

6.3 Measures taken and announced

The previous section described a number of elements that are relevant to tax avoidance and also carry money laundering risks. This section explains what measures have been taken and announced, other than general criminal law measures, to prevent the misuse of these elements by money launderers.

This falls into three parts: (i) measures aimed at combating abuse of service providers (elements 2 and 3); (ii) measures aimed at combating abuse of legal entities (element 1); (iii) measures concerning the tax and investment environment (elements 2 and 4). In this section, (i) and (ii) are discussed in more detail.

6.3.1 Measures taken

The fight against money laundering and terrorist financing has been the subject of increasing attention in recent years. The European Union has already issued various directives to combat money laundering and the financing of terrorism (Anti-Money Laundering Directives or AMLDs). These are partly guided by the work of the FATF. This is an international organisation that sets authoritative standards in preventing money laundering and terrorist financing, of which the Netherlands is a member. This issue is also receiving a great deal of attention at national level, including the role that the 'gatekeepers' of the financial system, such as banks, lawyers and trust and company service providers, should play in combating this problem. The fact that this role has not always been fulfilled satisfactorily is shown by a number of recent cases, such as the transactions involving ING and ABN AMRO by the Public Prosecution Service, which received considerable political and media attention.

This section highlights some of the measures taken, particularly where these relate to preventing abuse among service providers and legal entities. The main purpose of this is to outline a number of important measures without being exhaustive.

Abuse among service providers (elements 2 and 3)
Concerning the prevention of abuse of service providers, various measures have been taken as part of the so-called anti-money laundering framework. This Dutch anti-money laundering framework consists significantly of legal requirements imposed on service providers regarded as the financial system's gatekeepers, also referred to under the Wwft as the obliged entities. These include banks, investment institutions, accountants, lawyers, notaries, trust and company service providers but also brokers and certain traders. Because of these parties' key role in the financial system, they are ideally placed to keep out malicious parties. The requirements that apply to these parties are mainly laid down in the Wwft and, for trust and company service providers, in the Wtt 2018. The anti-money laundering framework sets several obligations, some of which are core obligations set out in more detail here:

- *Customer due diligence:* This concerns the obligation to carry out customer due diligence. The obliged entity must have an idea of who it is doing business with and who is behind an entity (or the UBOs).
- *Transaction Monitoring:* the institution should monitor transactions and report unusual transactions to the FIU[137]-NL.
- *Controlled and sound operational management:* this concerns rules about the internal risk policy and business operations, and about the recording and issue of data.

It is relevant to note that the Wtt 2018 imposes stricter requirements on trust and company service providers in certain areas, such as customer due diligence. This is partly motivated by the high risk that the trust sector entails, which was also discussed in section 6.3.

To ensure compliance with the rules of the anti-money laundering framework, there are various supervisory authorities, depending on the sector, including DNB, the Netherlands Authority for the Financial Markets (AFM), the dean of the district courts, Bureau Toezicht Wwft (BtWwft), Bureau

[137] Financial Intelligence Unit.

Financieel Toezicht (Bft) and the gaming authority. The anti-money laundering framework has been harmonised to a great extent within the European Union through five anti-money laundering directives. These anti-money laundering directives also largely follow the standards of the FATF, of which the Netherlands is a member. The FATF works at a global level to combat money laundering and the financing of terrorism and, to this end, carries out assessments of member states. The Netherlands is being evaluated in 2021.

Abuse of legal entities (element 1)
Several measures help to combat abuse of legal entities, including conduit companies. These are largely aimed at promoting transparency, which is essential in combating concealed (money laundering) structures. A basic condition for transparency of legal entities is the public Trade Register, which must be kept accurate and up to date. Part of this is an annual obligation to file the annual accounts with the Chamber of Commerce. These measures promote transparency and thus mitigate the risk of abuse of legal entities.

In addition, on 27 September 2020, the Netherlands introduced a UBO register which will be populated over an 18-month period. In this public register, the vast majority of legal entities established in the Netherlands must register the ultimate beneficial owners (UBOs). This concerns approximately 1.6 million legal entities. UBOs are natural persons who directly or indirectly have a specified interest or control in the legal entity. For example, a person who directly or indirectly holds more than 25 per cent of the shares in a private limited company. This register gives public access to the name, month and year of birth, state of residence, nationality and the nature and extent of the interest held. The date of birth, Citizen Service Number (BSN) or comparable number, country and place of birth, address and identity documents, and documents showing the nature and extent of the interest held are also registered. This information is not public but can be consulted by competent authorities, such as investigative bodies or the Tax and Customs Administration. The register is also searchable for personal data only by such competent authorities. Obliged entities are required to consult the UBO register as part of their customer due diligence and to report any discrepancies they find with their own data on the UBOs. In that context, obliged entities may explicitly not rely on the UBO register but must continue to conduct their own screening. The same obligation to report discrepancies applies to competent authorities insofar as it does not interfere with their statutory duties. The UBO register follows from the AMLD and has been introduced EU-wide. Part of this is that the EU UBO registers must be interconnected. This is expected to take place by the end of 2021.

In addition to the above measures, there are several other measures and projects that are aimed (indirectly or otherwise) at combating the abuse of legal entities. Two special initiatives are the Infobox Criminal and Undeclared Assets (iCOV), a partnership between thirteen government agencies and supervisory authorities that conducts data-driven research into, among other things, the finances of legal entities or groups of legal entities, and the relationships between various legal and natural persons. There is also TRACK from the Justis department, which performs automated checks on legal entities, e.g. at the time of incorporation or a change of board, and the data on the companies, directors, shareholders and the immediate surroundings. Of these, TRACK (on a solicited and unsolicited basis) makes risk reports to member agencies. TRACK also makes network charts of legal entities, showing visually the legal entities, partnerships and natural persons involved.

Finally, it is important to note that as of July 2019, the Act on the Conversion of Bearer Shares entered into force, under which bearer shares[138] have been abolished (dematerialised) in a practical sense

[138] Bearer shares are shares which are not registered, and for which a physical (transferable) certificate serves as proof of ownership.

based on a growth model. This means that all holders of bearer shares in the Netherlands will be identified, and it will no longer be possible to hold physical bearer shares. These can only be traded via a securities account. In addition, shares that are not traded in book entry form are converted into registered shares. Bearer shares that have not been deposited or converted into registered shares are deemed to be registered shares, and holders can no longer exercise the rights under the bearer shares.

6.3.2 Measures announced

National measures

The Money Laundering Action Plan of 30 June 2019 announced a large number of measures aimed at combating money laundering and terrorist financing. Particularly relevant in this context are the various measures announced concerning trust and company service providers. For example, a bill submitted to the Council of State in the meantime[139] prohibits the offering of conduit companies within the meaning of the Wtt 2018. The term 'conduit company' within the meaning of the Wtt 2018 is narrower than that used by the Committee. This concerns a conduit company that is part of the structure of the trust and company service provider (see also chapter 2). In addition, trust and company service providers will be prohibited from providing services to clients domiciled in third high-risk countries[140] according to the European Committee's list and to clients from countries on the EU's list of non-cooperative countries for tax purposes. In the Government's response of 8 July 2021 to the SEO report on illegal trust services, a number of other measures were announced concerning the trust sector. The following measures have been announced in this letter: (i) tightening up of the legislation to prevent parties who split up services from remaining outside the scope of the Wtt; (ii) intensification of the supervision and cooperation between DNB and the BtWwft, which supervise trust and company service providers and providers of domiciliation services respectively; (iii) a joint approach to illegal trust services through the Financial Expertise Centre[141] (FEC); (iv) the Multidisciplinary Intervention Team[142] (MIT) will focus on financial services; (v) research will be carried out into whether the penalties for illegal trust services are effective; and (vi) a study will be carried out into the future of the trust sector, which will also take account of the results of the research carried out by the Committee on Conduit Companies.

European action

Furthermore, on 20 July 2021, the EU published a major package of anti-money laundering legislation. Given the recent publication date, this package is still in the European legislative procedure, which is still an early stage. This concerns three legislative proposals aimed at strengthening the European anti-money laundering framework. Essentially, this consists of a regulation introducing a central European anti-money laundering supervisor with both direct and indirect powers. In addition, a regulation has been published in which various obligations that were previously included in a directive (the AMLD) are further harmonised at a European level, including the previously mentioned 'core obligations' such as client due diligence, including more extensive rules regarding the identification of UBOs. Thirdly, the package contains a new version of the AMLD, which includes further requirements for the UBO registers and for the banking data referral portals[143]. The package also introduces a cooperation and coordination mechanism for European FIUs. However, upon entry

[139] Bill on Action Plan against Money Laundering

[140] These are countries outside the European Union which the European Committee has classified as high risk because of deficiencies in the AML/CFT framework and risks to the financial system.

[141] The FEC's partners are the AFM, DNB, the Public Prosecution Service, the Police, the FIOD and the FIU.

[142] The MIT is a collaborative effort between Customs, the Tax and Customs Administration, the FIOD, KMar/Defence, the police and the Public Prosecution Service.

[143] The Bank Details Reference Portal is a central portal where certain competent authorities, subject to conditions, can view bank details

into force, this package is expected to amend the European anti-money laundering framework in a significant number of respects. This is also expected to have an impact on measures already in place.

7 Findings

7.1 Introduction

The position of the Netherlands as a conduit country has historically grown as a result of fiscal policy aimed at facilitating the cross-border activities of Dutch companies and attracting foreign investment. In general, the Netherlands offers optionality and stability. Optionality in terms of tax planning and legal options. Stability as a country with a good infrastructure and financial services. However, the use of the Dutch legal infrastructure is not limited to entities held by Dutch residents or those that develop substantial activities in the Netherlands. Individuals and entities residing outside the Netherlands have, with the help of Dutch service providers, set up and used many entities to avoid or prevent (potential) taxation in other countries, sometimes legally and sometimes not. This is partly the reason why the Netherlands is known as a conduit country. There are also indications that elements that follow from the tax and investment environment attract less honest, or even criminal, money flows. The committee has been looking for ways to reduce the attractiveness of the Netherlands to those entities and money flows.

7.2 Fiscal measures

In recent years, the Dutch government has already taken many measures to reduce the tax-driven flow of funds through the Netherlands. The effectiveness of these measures cannot yet be fully assessed, as the realisation dates are several years behind the entry into force of a measure. For the time being, inward and outward foreign direct investment from the Netherlands still seem to be very high, as is the number of holding, financing and licensing companies. Although the Dutch tax system can still be considered favourable to the shareholdings and the tax-friendly organisation of capital gains and dividend flows in respect of foreign subsidiaries, the committee's study shows that it is no longer significantly different in this respect compared to other European countries. Non-fiscal factors such as flexible business law, legal services, good infrastructure and international orientation also play a role in establishing holding and finance companies in the Netherlands. These include holding and finance companies with an actual presence in the Netherlands for which the favourable tax treatment of company profits earned outside the Netherlands is an important but not necessarily the decisive reason.

However, there is still a large group of (almost) empty conduit companies that use the Dutch infrastructure, whose contribution to the economy is small and which at the same time contribute to the bad image of the Netherlands when it comes to international tax avoidance. This is partly due to the former successful marketing of the Netherlands as a hub for international expansion but has led to a legacy that the Netherlands must part company with if it is to retain its national and international credibility. The measures already in place are expected to end (part of) the tax-driven interest and royalty flows but will not cause the Netherlands to lose its position as a country of establishment for (virtually) empty holding companies. The Committee therefore recommends further steps. At the same time, the committee sees that unilaterally taking far-reaching measures has limits, especially under European law.

Fiscal measures can be divided into measures in the tax laws that increase the fiscal costs ("the price tag") of using low-substance entities in the Netherlands and measures that provide other countries with information about Dutch entities in order to deny them certain benefits.

Measures in the tax laws must avoid, on the one hand, a situation where an excessively large group - and thus the real economy - is affected and, on the other, where an excessively sharp demarcation would conflict with EU law. If, for example, the participation exemption no longer applied to empty holding

companies[144], many domestic holding structures would be affected. The distinguishing criterion should be whether the holding company belongs to a group with sufficient economic activity in the Netherlands. To be able to implement this as intended, an early initiative at European level is desirable.

The Committee believes that the PPT is a good instrument against the intermediation of conduit companies aim to avoid withholding tax. The advantage of the PPT is that it applies to all provisions of the relevant tax treaty. Where this is not already done through the MLI, the Netherlands should strive to include the PPT in as many tax treaties as possible.

The committee believes that measures providing unilateral and unsolicited information to other countries are not a panacea against the use of conduit companies. Nevertheless, this could enable other countries to take measures within their own responsibility. To enable foreign tax authorities to determine, for example, whether they need to apply an anti-abuse provision, the Tax and Customs Administration would ideally provide information on the (relevant) economic nexus in the Netherlands. However, information on the economic nexus is strongly related to the activities of the company concerned (and of its affiliated companies) in the Netherlands and requires a case-by-case consideration by the Tax and Customs Administration. Given the large number of companies to be screened, this would be impracticable. In addition, an open standard may lead to more discussions with and litigation by taxpayers, as a taxpayer can appeal against the provision of information to a foreign country.

It would, however, be feasible to have businesses provide information on certain criteria and then exchange it, as is already the case with the application of Article 3a of the Implementing Decree on the provision of international assistance on the levying of tax (UB WIB), which applies to the interest and royalty conduit companies (service providing entities). However, such a measure has limitations. On the one hand, there may be a flow of unfocused information to foreign countries that remains unused there, as it is questionable whether the information provided meets the needs of other countries. Such a flow could also have a masking effect in the sense that the impression could be wrongly created that in the case of entities about which no information has been exchanged there is, in the opinion of the Netherlands, no wrongful use of a tax treaty or directive. On the other hand, information about one particular entity within a Dutch group structure may give foreign tax authorities the false impression that certain benefits should be withheld from that entity. To prevent the undesirable use of the Netherlands for conduit purposes without harming the real business community, the provision of information should be limited to entities belonging to a group that has no other relevant activities in the Netherlands (a kind of 'group test') and of which the Netherlands would agree to withhold the benefits in question in a mutual consultation procedure with the other country. However, the further delineation in taking the appropriate measures runs up against the limits of EU law on this point. Given the freedom of establishment, no distinction should be made between, on the one hand, Dutch intermediate holding companies whose interests are ultimately held by a Netherlands company and, on the other, Dutch intermediate holding companies whose interests are ultimately held by a foreign company. The main reason for not distinguishing between these cases is to avoid the measure favouring domestic situations over cross-border ones (at least within the EU) and thus contrary to EU law.

As an aside, the committee notes that requests from abroad for information should, of course, continue to be answered as well and as completely as possible. The Committee believes that there are

[144] The legislator would thus break with the policy pursued for years based on the 'linking idea' of resolution BNB 1975/11.

opportunities here for other countries that are not always fully exploited. Here, the Netherlands, more specifically the Tax Administration, can continue to offer and provide practical assistance to foreign tax administrations to optimise effective information exchange and international cooperation.

At the time of finalising this report, the committee is hopeful that the developments at the OECD and the EU will lead to a reduction in flow, respectively to more opportunities to target flow on the basis of a level playing field. That is, conduit activities are not moved to other jurisdictions, but are actually reduced. The work of the OECD in reviewing the international tax system (in particular Pillar 2 - a minimum profit tax for multinationals) may result in it no longer being attractive to have interests in subsidiaries in low-tax countries held by a Dutch (intermediate) holding company. The intended rapid realisation of pillar 2 means that it does not appear opportune for the Netherlands to consider a broader structure for withholding taxes at this time. The European Commission has announced proposals to combat the use of "shell companies". This presents opportunities for an EU-wide approach, which is preferable to a national one. The directive to be drafted could provide a basis for targeted information exchange between Member States on conduit activities. The new proposal may also limit existing directive benefits (notably those in the Parent-Subsidiary Directive and the Interest and Royalty Directive) for conduit situations, i.e. those where an intra-group income stream passes through an entity established in a Member State to a non-Member State. Such an EU directive would provide a good opportunity to set effective limits on tax-driven conduit activities within the EU and globally. The committee believes that the EU initiative presents an excellent opportunity for the Netherlands to promote and enforce an international standard that makes tax-driven conduit activities undesirable.

In the unlikely event that the international developments do not yield sufficient results, the Committee believes that there could still be grounds for the Netherlands to take unilateral measures, for example, concerning the scope of conditional withholding taxes. However, the committee sees this as a suboptimal solution that will only come into play if the international and EU initiatives currently underway do not produce as good a result as might be expected.

In the short term, the Netherlands itself can increase the costs of conduit activities (by increasing or more frequently applying the substance requirements, imposing administrative requirements and increasing fiscal uncertainty). The result is that conduit activities are either incorporated in group activities with substance in the Netherlands or disappear from the Netherlands, but may appear elsewhere. The goal of effectively discouraging tax-driven conduit activities calls for an international approach, also to mitigate or clarify EU law restrictions. This international approach is now emerging and must be actively promoted by the Netherlands. The Netherlands, as a leading conduit jurisdiction, also has a special responsibility in this regard.

7.3 Non-fiscal measures

For tax measures, the committee saw a division whereby either the tax burden could be increased, or the cost of using empty entities (the administrative burden) could be increased, or, by exchanging information, foreign tax authorities could be better enabled to make their own assessment of tax liabilities. The Committee applies a different categorisation for measures concerning entities established in the Netherlands for non-fiscal reasons. Many non-fiscal reasons affect the good business climate in the Netherlands. The committee believes that this child should not be thrown out with the bath water. However, the committee also sees less benign non-fiscal reasons for establishing, such as tactical manoeuvring with bilateral investment treaty provisions and channelling or covering up illegal money flows. For such reasons, it may also be appropriate to increase costs in these cases. In addition, transparency requirements can facilitate the assessment of the desirability of the flow.

In line with this, the committee advocates intensifying the supervision. Finally, the committee sees ways of tightening up access to a bilateral investment treaty.

Although flexible Dutch corporate law plays a role in the presence of many low-substance entities in the Netherlands, the Committee does not propose to impose any restrictions on this because (too many) bona fide companies would also be affected. Moreover, the Committee has reservations about assessing the desirability of conduit companies that are primarily intended to take advantage of the flexibility of Dutch company law. However, it should be noted that as with tax-driven structures, businesses using conduit companies can get around legislation in other countries, such as equal voting rights for all shareholders, without substantial activities taking place in the Netherlands. However, unlike tax-driven structures, this does not usually have a direct impact on other governments. Often, these are provisions on the rights of shareholders, creditors and directors of a company. Potential shareholders, creditors, suppliers and customers can in principle judge for themselves whether they find these provisions acceptable. If their rights were to be unduly restricted, they could choose not to invest in the company, not give the company a loan, and not do business with it or impose additional conditions on it. In the case of conduit structures set up jointly by joint-venture partners, consent appears to have been given by the shareholders involved. In the case of conduit structures aimed at obtaining external debt financing, the structure may also be aimed at the interests of those financiers.

The broader social implications of the use of Dutch company law by conduit companies are not straightforward. There are both positive and negative implications. Take, for example, constructions that protect foreign companies against hostile takeovers. These structures can provide stability and allow for a greater focus on long-term social value creation in business operations; otherwise, a company could be vulnerable to activist shareholders focusing on short-term shareholder value. The same applies to provisions on voting rights that allow families to control a listed company. On the other hand, such constructions can reduce economic dynamism by reducing the disciplining effect of the capital market. Moreover, unequal voting rights may contribute to the concentration of economic power in a limited group. Furthermore, conduit structures designed to keep investments out of the sphere of influence of foreign governments can protect against expropriation or political interference. On the other hand, such structures may also hinder the imposition of legitimate sanctions and, for example, make it more difficult for other stakeholders to recover damages. This may also have consequences for the political reputation of the Netherlands. How such effects should be weighed up depends partly on political preferences, and the committee does not take a position on this.

However, the committee does suggest bringing the reporting requirements for conduit companies more in line with those with Dutch operations. This includes preparing and filing financial statements, management reports, auditor's reports, and the like. This is also part of company law, but reporting requirements do not limit the flexibility of the company form. In the Committee's opinion, it cannot be the intention that conduit companies, because of their limited substance, have fewer reporting obligations than ordinary companies with substantial economic activities in the Netherlands. In the current situation, however, this is the case. Many conduit companies fall under the lightest reporting regime for micro-enterprises, as they have a net turnover of up to EUR 700,000 and up to 10 employees. In this case, only a limited balance sheet needs to be published, without notes, a profit and loss account, management report or auditor's report. This also applies to conduit companies with very large foreign direct investment assets and financial income, such as interest income and participation gains. This is because the balance sheet total is not the only criterion for determining company size and the corresponding reporting obligations. A conduit company with foreign direct investment assets of more than a billion, but no turnover or employees, therefore falls into the category of micro-enterprises. This is because financial income, such as interest, dividends

and profits from the sale of participations, is not taken into account when determining net turnover. Moreover, the size of holdings is regularly not taken into account when determining the size of a company, as there is an important exception to this rule. The EU's accounting directive does not allow the balance sheet total to be used as a criterion in its own right, independently of net turnover or the number of employees. However, the directive does leave room for an adjusted income threshold for companies for which the net turnover is not relevant. The Committee therefore recommends using this space.

There is a risk that some multinational companies will avoid the reporting requirements by using a '403 exemption'. Under Section 2:403 of the Dutch Civil Code, a legal entity that is part of a group does not have to file annual accounts if certain conditions are met. For example, the ultimate parent company must then issue a declaration that it guarantees the debts of the legal entity and consolidated annual accounts must be filed containing the financial data of the legal entity. It is expected that not all conduit companies will make use of this exemption. For example, a guarantee statement may hinder the sale of the conduit company, as the ultimate parent company cannot immediately withdraw liability for existing liabilities, such as loans and tax obligations. Furthermore, some conduit companies are part of an unlisted company with an ultimate parent outside the EU that does not publish consolidated financial statements. In such situations, no consolidated financial statements of the ultimate parent will usually be filed by a conduit company. However, to make the reporting requirements for conduit companies more effective, consideration could be given to removing the reporting exemptions in Article 403. In addition to conduit companies, this also affects subsidiaries of Dutch companies, which make use of a 403 exemption in the current situation. However, it is not possible to distinguish between conduit entities with a foreign parent company and entities with a Dutch parent company, as this would be contrary to EU law. This exemption from Article 403 can, however, be deleted in its entirety. Although this also increases the administrative burden for companies operating in the Netherlands that currently make use of the exemption, some of these companies will already be preparing annual accounts for internal purposes. Moreover, there are also companies that give guarantees to clients without filing a 403 declaration in the current situation. The committee notes that in some other countries, such as Belgium and the United Kingdom, the relevant reporting exemptions do not seem to apply, so this is a real option.

Adjusting reporting requirements to create more transparency about conduit companies contributes in several ways to reducing the possible adverse effects of conduit activity. For companies that gain a relatively limited financial benefit from the conduit structure, more extensive reporting requirements may be a reason to stop using the structure or move it to another country. The number of conduit companies is therefore decreasing. More extensive reporting requirements may be discouraging for structures aimed at concealing financial flows and those vulnerable to public criticism. After all, the chances of discovering such flows and structures then increase. By increasing the opportunities for systematic investigation by journalists and scientists, they can be detected earlier. In addition, reporting requirements in line with the financial size of conduit companies are appropriate within the framework of flexible Dutch corporate law. An important condition for the action perspective of stakeholders of a company using Dutch company law is that there is sufficient transparency for all stakeholders about the conduit company and its role in the company's financial structure. The concept of stakeholders should be understood broadly: not only shareholders and financiers but also, for example, parties doing business with the company and parties potentially affected by business activities financed through the conduit company. This does not only concern direct transactions with or business activities of conduit companies themselves, which are limited. Information on links in a company's financial structure, and more specifically information on the finances and management of a conduit company, may also be relevant for parties dealing with business units that are held or financed through a conduit company.

Furthermore, the committee calls on the Dutch government to deny access to bilateral investment treaties to companies established in the Netherlands only on paper. This refers to entities in the Netherlands owned by foreign multinationals or foreign private investors that have no other connection or activities in the Netherlands. In line with current government policy, the Committee considers it undesirable that conduit companies without substantial economic activities in the Netherlands can claim protection under Dutch bilateral investment treaties. It strikes the committee that although tackling the undesirable use of bilateral investment treaties has already been placed on the agenda, there is still a large backlog, both nationally and internationally, in tackling the abuse of tax treaties.

The committee has been informed that, so far, only eight countries have been given the opportunity to negotiate a new bilateral investment treaty based on a new model convention and that this has not yet led to a new treaty. The committee also understands that many countries are hesitant, partly because it contains some new provisions whose impact is still unclear. The committee understands that treaty negotiations are lengthy processes. Nevertheless, the Committee considers it of great importance that the Dutch government shows greater commitment to counteract the unintended use of bilateral investment treaties by conduit companies. The Committee advises the Netherlands to make efforts in a multilateral context to exclude conduit companies from bilateral investment treaties. It may be possible to build on the experience of the multilateral adjustment of tax treaties. If this does not succeed (in the short term), the committee recommends that the Netherlands renegotiate more bilateral investment treaties and do so as soon as possible.

7.4 Money laundering

The committee's view is that the Dutch tax and investment climate, and the tax avoidance that goes with it, entails various elements that can attract criminal money flows and increase the risk of money laundering. In this context, the committee sees that the fight against money laundering and terrorist financing has been given increasing attention in recent years. This is partly due to some high-profile scandals, such as the Panama Papers. Various measures have been taken at the Dutch, European and international levels to deal with this problem. However, the Committee believes that there are opportunities to further tighten up the framework. This is confirmed by the money laundering cases that continue to come to light, but also, for example, by the SEO study on illegal trust services.

It is important to prevent the abuse of legal entities, including conduit companies. An important aspect of this involves addressing the opportunities for concealment provided by legal entities. It is also important to ensure the integrity of service providers. In addition, as already explained above, the committee sees the general importance of tackling the tax and investment climate, especially where it attracts less honest or even criminal flows of money. At the same time, the committee also recognises that even if the financial flows become much smaller, they are probably still so large that criminal money flows can be absorbed into them.

The Committee calls on the government to intensify its supervision of the service industry that facilitates the establishment and maintenance of entities held by predominantly foreign shareholders that operate as holding, financing or royalty (conduit) companies. Intensified supervision will contribute to a more honest and professional sector and reduce the risk of excesses and the media attention that goes with them. Intensified monitoring can also help encourage those companies and individuals that are already showing a more cooperative attitude and further discourage those who may now be operating under the radar. In addition to increasing the chances of being caught, consideration could be given to increasing the fines for uncooperative service providers and possibly using criminal law instruments.

The committee mainly sees risks, and room for improvement, in trust services. The requirements of the Wtt 2018 and the supervision of the sector by DNB are an important mechanism to contain the risks of this form of service provision, but offer limited resilience against illegal trust companies. In this context, the committee also points to the SEO report on illegal trust services and the NRA Money Laundering 2019. In this context, the committee considers it important to devote the necessary attention and resources to dealing effectively with such illegal trust service providers. This requires effort from both supervisors and investigators. The committee does not see a solution in stricter (self or external) regulation of the trust sector alone, or even an outright ban. After all, illegal trust companies evade the rules by their very nature. The expectation is that such steps could act as an impetus for more illegal trust service provision, thereby losing sight of this phenomenon.

The committee also sees room for measures to improve the transparency of legal entities and counteract concealing constructions. Understanding the identity of ultimate beneficial owners is an important part of this. In this context, the committee sees that the Netherlands has taken an important step in introducing a public UBO register. Such a register is intended to promote transparency and prevent concealed constructions. This increases the likelihood of inaccurate UBO information or wrongdoing being discovered. However, the committee sees room for improvement where UBOs and the UBO register are concerned.

Firstly, the Committee sees risks in the legal possibility, if no true UBO can be found, to designate the members of the legal entity's senior management as 'pseudo' UBOs. This possibility applies both in the context of the administration and registration obligation in the UBO register, which is incumbent on the legal entities themselves, and to obliged entities , which are obliged to determine the UBOs of their client in the context of customer due diligence. The Committee believes that relevant information is lost. After all, it is not clear whether the pseudo UBOs will be used because there is actually no UBO, or because there is uncertainty about this. Therefore, the Committee recommends that it should be made clearer, both in the context of legal entities' own records and the UBO register, and in the customer due diligence process, why senior management as 'pseudo UBOs' has been designated.

Furthermore, the committee considers it important to enable further private investigations into money laundering structures. The UBO register is an important tool in this regard, but the current version hinders systematic analysis by NGOs or investigative journalists, for example. The UBO register can only be consulted for payment per legal entity, and other than by competent authorities, it is not possible to search by UBOs or personal data of UBOs. The public can only do one-on-one searches, and cannot request data files or statistics. This is main motivation behind this is the privacy of UBOs. The committee does recognise the importance thereof and is therefore cautious about making more information public than is currently the case. Also, the Committee underlines the value of the existing option to limit access to information on UBOs in where the UBO is a minor, legally incapable or under police protection. Having said that, the committee does see added value in improving the possibilities of analysing the already publicly available data. This can be done by removing barriers such as compulsory payment and enabling complex searches or providing comprehensive public data files. To illustrate, the United Kingdom makes available data files of the UBO register for *limited liability companies* with a snapshot of all public data. These files can be downloaded from the register's website [145] and are actually used for systematic analyses.[146] These data files are provided in such a form

[145] See http://download.companieshouse.gov.uk/en_pscdata.html

[146] See, for example, Global Witness (2019), Hard Data on Lessons Learned from The UK Beneficial Ownership Register, https://www.globalwitness.org/documents/19733/GW.Fact_Sheet_on_UK_Register_Data_for_US.May302019_wohQoid.pdf

that special software is required to read them. As a result, in practice, the files can only be used by professional data analysts and are difficult for private individuals to access, thus limiting the impact on UBO privacy.

The committee also believes that the value of UBO registers as a tool increases as the number of countries that have implemented a UBO register with public data rises. Global implementation allows for the comparison of data and counteracts cross-border concealment constructions. In the EU, UBO registers with public data are already the norm due to the Anti-Money Laundering Directive. However, this is not the case outside the EU. The Committee recognises that the Netherlands cannot impose its will on other countries but recommends that the Netherlands work, and continue to work, towards the worldwide introduction of UBO registers with public information in the relevant forums, such as the FATF.

The committee also notes that criminals use cross-border concealment schemes to impede investigations by local authorities, which are bound by national borders. It is very important to put sufficient effort into international cooperation in monitoring and investigation in this context. This not only concerns situations where Dutch criminals are involved, but also those situations where foreign criminals make use of Dutch conduit companies. If the Netherlands takes a proactive approach here, it can send out a strong message to avoid the Netherlands. This is also important for the international reputation of the Netherlands.

Finally, the committee notes that the importance of the relationships between conduit companies, money laundering and tax evasion has become clear during its investigation. Many questions and uncertainties surround this topic, while the Netherlands is a leader in conduit activities. The committee has been working to shed more light on the matter, but at the same time, has noted that obtaining relevant data and statistics is complex. In this context, the Committee deems it useful to conduct a follow-up FEC investigation into the relationship between money-laundering and conduit activities and the role of conduit companies in this and recommends freeing up the necessary capacity and resources for this purpose.

8 Recommendations

8.1 Introduction

As outlined in the previous chapter, various measures have been taken in recent years to combat conduit and conduit companies and in the fight against financial crime. Nevertheless, the committee sees room to take further steps to further discourage conduit activities and prevent abuse more effectively. Specifically, when considering various tax policy options, the committee has recognised the EU law risks, and the committee therefore sees all the more reason to welcome a European initiative against conduit companies.

The committee has divided the recommendations into tax and non-tax recommendations. The tax recommendations cover withholding tax benefits or securities, improving the exchange of information and tightening up the Dutch stance in treaty and multilateral negotiations on tax matters. The non-fiscal measures relate to withholding the legal benefits that bilateral investment treaties offer to conduit companies, increasing the transparency of legal entities by, among other things, tightening up the obligations concerning the determination of the UBOs, the UBO register, and the law governing financial statements, and combating financial crime through stricter supervision, better international cooperation and additional investigations. These recommendations are summarised in the table below.

Table 7: *Overview of fiscal and non-fiscal policy measures*

Fiscaal	Niet fiscaal
Taxation • The elimination of the safe harbour for service providing entities ("interest and royalty conduit companies").	**Transparency of UBOs** • Tighten up the obligations where 'senior management' is designated as UBO. • Make currently public data in the UBO register more easily searchable • International introduction of UBO registers with public data.
Information exchange • Expansion of the spontaneous exchange of information on companies. • Spontaneous exchange of information in the case of exempted disposal profits	**Annual accounts** • Deletion of the exceptions in article 2:403 BW. • When determining the size of a company, always include data from holdings and, if relevant, financial income.
International • Extension of the PPT to the entire tax treaty if not arranged multilaterally. • A proactive stance on the forthcoming EU directive proposal on shell entities. • A clear interpretation of the EU anti-abuse principle.	**Monitoring and Investigation** • Tighten approach to combatting illegal trust services. • Follow-up investigation into money laundering and conduit activities • Intensify international cooperation in countering criminal conduit activities
	BILATERAL INVESTMENT TREATY • Deny conduit companies access to bilateral investment treaties.

8.2 Fiscal Recommendations

8.2.1 Taxation

Recommendation 1: Remove the safe harbour for interest and royalty conduit companies (service providing entities).
The Committee supports and reiterates the recommendation of the Advisory Committee on Taxation of Multinationals to delete the safe harbour in Section 8c(2) of the 1969 Corporate Income Tax Act for the interpretation of the 'appropriate equity capital' to bear the risks incurred and to replace it with an open standard. As a result, the reduced security makes it less attractive for conduit companies

to establish themselves in the Netherlands. In addition, the company must also have the right functionality to manage the risks involved. Section 8c of the 1969 Corporation Tax Act (in conjunction with the 'service provider entities Decree') aims to discourage interest and royalty conduit companies from using the Dutch treaty network without adding value to the transactions. Article 8c of the 1969 Corporate Income Tax Act on the one hand excludes the foreign withholding tax on these interest and royalty receipts from set-off, and on the other allows the source country to withhold treaty benefits from the conduit company (such as no or a reduced rate of withholding tax). The measure creates uncertainty for companies wishing to carry out conduit activities in the Netherlands. A case-by-case assessment of whether a taxpayer faces a real risk will have to be made. The committee does, however, draw attention to the EU law aspects of this recommendation.

8.2.2 Information sharing

Recommendation 2: Expansion of the spontaneous exchange of information on companies
As currently regulated in Article 3a of the Income Tax Act, the spontaneous exchange of information to source countries should be extended to companies that do not meet the (new) risk requirements of Article 8c of the 1969 Corporate Income Tax Act. Furthermore, the committee believes that there is scope to expand the exchange of information to cover more entities. The crux is to make a meaningful selection of entities while keeping real situations out of the equation. This means that it should only cover situations in which the Netherlands is a link in a cross-border structure. Such a demarcation entails risks under EU law. To mitigate these risks, the forthcoming proposal for a directive could possibly be a solution. With a view to implementation, a running-in period seems to be desirable. Finally, the committee draws attention to the 'monitoring' of source countries in the sense that whether the information provided is actually used is monitored.

Recommendation 3: Spontaneous exchange of information in the case of exempted disposal profits
Exchange with certain source countries that have a withholding tax on the disposal of shares; i.e. the gain realised on the disposal of the shares in an entity is taxed in the country where that entity is established. Under many tax treaties, the right to levy tax on the gain on disposal is, in principle, assigned to the country of residence; that is, the country of the disposing shareholder. “In principle”, because if the source country can apply an anti-abuse provision, the taxing right still belongs to the source country. If the Netherlands is the country of residence, the profit on disposal is exempt from taxation. For this reason, an entity in the Netherlands may have been interposed. To better enable the source country to apply an anti-abuse provision where necessary, the exchange should cover situations where a Netherlands-based entity with little substance disposes of the shares in a foreign company. The assessment of whether there is sufficient substance in the Dutch entity should be based on a nexus.

8.2.3 International

Recommendation 4: Extension of the PPT to the entire tax treaty (if not multilaterally regulated.
The PPT contained in the MLI (applies to all provisions of the applicable tax treaty. Through the MLI (multilateral instrument), the Netherlands aims to make this extended PPT applicable in the treaty relationship with as many countries as possible. Where this is not possible, for example in the relationship with countries that are not parties to the MLI, the Netherlands should approach other countries to include a PPT in the treaty that applies to all treaty provisions.

Recommendation 5: A proactive stance on the forthcoming EU directive proposal
The Committee calls on the Dutch government to adopt a positive attitude towards the European Commission's announced proposal for a directive and, if necessary, to draw attention to a tightening

of the Parent-Subsidiary Directive and the Interest and Royalties Directive to prevent the use of conduit companies.

Recommendation 6: Clear interpretation of the EU anti-abuse principle
Calls at EU level for an unambiguous interpretation of the EU anti-abuse principle, now that combating tax avoidance by 'shell companies' is on the European agenda and a proposal for a directive on the subject has been announced. The Danish judgments offer good starting points for tightening up the Interest and Royalties Directive and the Parent-Subsidiary Directive. Tightening up the Parent-Subsidiary Directive could be aimed, among other things, at depriving intermediate holding companies of tax benefits such as the participation exemption. The proposal for a directive should also aim at a targeted exchange of relevant information on conduit activities between EU Member States.

8.3 Non-fiscal policy options

8.3.1 Transparency and reporting

Recommendation 7: Tighten up the obligations when 'senior management' is designated as UBOs of a legal entity
The Wwft Implementation Decree provides that in the situation where no real UBO has been identified, senior executives may be designated as 'pseudo-UBOs'. Obligate obliged entities in the context of customer due diligence to record the reasons why the pseudo-UBO has been designated, including: i) the steps taken to establish the UBO and the results of these steps; ii) any supporting documentation; iii) why there are no grounds for suspicion; iv) the situation that applies, namely: A) that no UBO has been identified; B) that there is some doubt as to whether an identified person is the UBO. This helps, among other things, to prevent being too quick to fall back on pseudo-UBOs in customer due diligence.

In addition, require legal entities that do not have real UBOs and therefore designate senior management to explain why there are no other UBOs in both their own records and in the registration in the UBO register. This may be because an entity is an association with a social purpose, or because an entity is ultimately owned by at least four natural persons, each with a maximum of 25 per cent ownership and control. Legal entities should be able to provide this explanation because, unlike obliged entities, they are not third parties and have a performance obligation. Therefore, they may only designate the pseudo UBO if they have established that there is indeed no UBO (and not, for example, in case of doubt).

Recommendation 8: Making already public data in the UBO register more searchable
The committee subscribes to the importance of privacy for UBO's but still sees room for improvement of the UBO register without making more data on individual UBOs public or removing the option of shielding data from the public. In this context, the committee recommends that systematic analysis of the UBO register should be made possible for the public (including journalists and other researchers). This consists of two elements. Firstly, make the public part of the UBO register searchable on all public UBO and trade register variables and combinations thereof (e.g. make it possible to search on company characteristics in relation to the name of a certain UBO). This can be done by offering integrated databases or extending the website's search functionality, as in the United Kingdom. In the latter case, also make it possible to download the results of a search in one file. In the case of comprehensive databases and those with extensive search results, safeguards can be put in place to minimise searches by non-professionals, such as the need for special software to access and process the data in an orderly manner. Secondly, make access to the UBO register or the integral databases free of charge, or at least do not charge larger amounts than necessary to break even.

Recommendation 9: International introduction of UBO registers with public data
The worldwide introduction of UBO registers with public information (as in EU countries) is an important step in promoting transparency. The more countries that adopt it, the more effectively investigations can be carried out, both privately and publicly, into cross-border concealment structures. The Netherlands should therefore strive for the global introduction of UBO registers with public data.

8.3.2 Financial Statements

Recommendation 10: Deletion of exceptions in Section 2:403 of the Dutch Civil Code
Delete the exceptions in Article 2:403 of the Dutch Civil Code to prepare and present the financial statements, the management report, the other information, the report on payments to public authorities[147], the audit, and the publication of these documents. Individual entities that are part of group are then no longer exempted from the usual reporting requirements under certain conditions. This increases the possibility of systematic investigations, making it more difficult to use Dutch conduit companies for concealment purposes and uncover socially undesirable conduit practices sooner.

Recommendation 11: When defining the size of a company, always include data from participations and, if relevant, financial income
Delete the last sentence in the second paragraph in Sections 2:395a-397 of the Dutch Civil Code so that the assets, net turnover and employees of participations are always counted when determining the size of the company. This is only relevant for conduit companies that are themselves holding companies. In addition, the committee recommends adding a provision to these articles to the effect that for legal entities with primarily financial income[148] the threshold for net turnover is applied to another income concept[149] that includes financial income, because net turnover is not relevant in that case. This is particularly relevant for conduit companies with financing activities and for entities through which dividends flow.

8.3.3 Monitoring and Investigation

Recommendation 12: Commitment to tackling illegal trust services
Give higher priority - and if necessary allocate more resources - to tackling illegal trust services more rigorously. Do this throughout the chain where necessary, both in monitoring and detection. The extent of illegal trust service provision in the Netherlands, which is estimated to be substantial, is worrying and poses significant integrity risks. Some of the conduit activities therefore evade supervision of, among other things, customer due diligence.

Recommendation 13: Follow-up investigation into money laundering and conduit activities
Let the FEC further research the role of conduit activities in the money laundering problem , and make the necessary capacity and resources available for this. Due to their nature, illegal conduit activities are difficult to detect; existing research on them is limited and obtaining the data needed for proper

[147] The report on payments to governments is only applicable to companies in the extractive industry.

[148] Financial income may refer to the result from participating interests, income from (other) securities and receivables included in fixed assets, other interest income and similar income and (to the extent that the balance is positive) changes in the value of financial fixed assets and securities included in current assets. “Primarily” means that the financial income is at least 70 per cent of the total of the net turnover plus the financial income.

[149] Instead of net turnover, net turnover plus the above-mentioned financial income, or only financial income, may be used as income.

analysis is complex. A partnership of authorities is likely to be able to examine this issue in greater depth than the commission, using the information available to different authorities.

Recommendation 14: Commitment to international cooperation in combating criminal conduit activities
Criminals abuse national borders for (disguising) money laundering constructions and to obstruct local authorities. Therefore, the Netherlands should be committed to strengthening international cooperation in the fight against criminal conduit activities. This can be done by focusing on improved cooperation and information sharing in an international context, and giving national resources and priority to combating criminal conduit activities, including those involving persons residing outside the Netherlands.

8.3.4 bilateral investment treaties

Recommendation 15: Deny conduit companies access to bilateral investment treaties.
The Committee advises the Netherlands to make efforts in a multilateral context to exclude conduit companies from bilateral investment treaties. If this cannot be done (in the short term), the committee recommends renegotiating existing bilateral investment treaties and doing so in the short term. For additional renegotiations, permission should be requested from the European Commission. The committee believes that an international or European approach whereby as many bilateral investment treaties as possible are modified, as in the case of the MLI, would be an effective way to impede access to bilateral investment treaties by conduit companies. To monitor progress, a periodic report to the House on adjusting the Dutch bilateral investment treaties and arbitration cases is recommended.

Enclosures

Annex 1: External input

The Chairman of the Committee invited the following organisations to express their views on the phenomenon of conduit companies.

- Anti Money Laundering Centre (AMLC)
- Tax and Customs Administration/Foreign Investors Contact Point
- Tax and Customs Administration/APA-ATR team
- De Nederlandsche Bank (DNB)
- Financial Intelligence Unit-the Netherlands (FIU-NL)
- Fiscal Intelligence and Investigation Service (FIOD)
- Offshore Kenniscentrum
- Holland Quaestor
- Royal Dutch Notarial Association (KNB)
- Dutch Association of Tax Advisers (NOB)
- Netherlands Foreign Investment Agency (NFIA)
- Public Prosecution Service (PPS)
- TaxJustice NL
- Transparency International
- Representative of a multinational with various companies in the Netherlands

In addition, the Committee received written input from the following organisations.

- De Nederlandsche Bank (DNB)
- TaxJustice NL
- Dutch Association of Tax Advisers (NOB)
- Transparency International
- Holland Quaestor

The Committee obtained external research or support from the following organisations.

- Statistics Netherlands
- Anti Money Laundering Centre (AMLC)
- infobox Criminal and unexplained assets (iCOV)
- PwC Tax Advisors
- International Bureau for Fiscal Documentation (IBFD)

Annex 2: Composition of the committee

Composition of the committee

- Dr B. (Bernard) ter Haar (Chairman) (ABDTOPconsult)
- M. (Marin) Bergwerff (independent international tax consultant to international organisations and others)
- Dr A. (Anja) de Haan (Tax and Customs Administration)
- P.M. (Pieter) Moore MSc (De Nederlandsche Bank)
- Prof. H. (Henk) Vording (Leiden University)
- Dr F. (Francis) Weyzig (Central Planning Bureau)

Secretariat

The Committee was supported by the administrative secretariat.

- N. (Nadia) Ganga (Ministry of Finance)
- D.W. (Daan) de Leeuw MSc (Ministry of Finance)
- B.J.W. (Bart) van Raaij (Ministry of Finance)
- B.E. (Ben) Tichelaar (Ministry of Finance)

Annex 3: Country classification used

Table 8 summarises the country classification for the statistics used in this report, where:

- An LTJ is defined as a jurisdiction that does not subject bodies to tax on profits or to a statutory rate of less than 9 per cent or a jurisdiction included in the EU list of non-cooperative jurisdictions for tax purposes. This definition is also used in the context of conditional withholding taxes on interest and royalties.
- An offshore financial centre, or OFC, is defined as a "country or jurisdiction that provides financial services to non-residents on a scale not commensurate with the size and funding of its domestic economy. This definition is in line with the country classification used by the government to monitor the effects of the approach to tax avoidance.[150]
- Emerging markets are defined as countries that are in the process of growing from a developing country to an economically developed country. Often these countries have a high economic growth and the infrastructure is already much better than in developing countries.

Annex Table 8: *Number of countries by country group and breakdown OFCs, LTJs and emerging markets*

Country group	Number of	Offshore financial centres	Low-tax jurisdictions	Emerging economies
Rest of the World	153	Panama	United Arab Emirates	Brazil
Ireland	1	Seychelles	Cayman Islands	China
Emerging markets	7	Philippines	Bermuda	Mexico
United States	1	Singapore	British Virgin Islands	Malaysia
LTJ	23	Hong Kong	American Samoa	Turkey
Switzerland	1	Andorra	Seychelles	Kazakhstan
United Kingdom	1	Aruba	Barbados	Equatorial Guinea
Luxembourg	1	Curacao	Bahrain	
OFC excl LTJ	25	Gibraltar	Guernsey	
The Netherlands	0	Lebanon	Man	
EMU excl. IE and LU*	16	Saint Lucia	Jersey	
		Liberia	Trinidad and Tobago	
		Marshall Islands	US Virgin Islands	
		Mauritius	Anguilla	
		Bonaire, St. Eustatius and Saba (BES)	Turkmenistan	
		Belize	Fiji	
		Liechtenstein	Guam	
		Sint Maarten (Dutch part)	Palau	
		Saint Vincent and the Grenadines	Vanuatu	
		Dominica	Samoa	
		Antigua and Barbuda	Turks and Caicos Islands	
		Cook Islands	Bahamas	
		Grenada	Panama	
		Saint Kitts and Nevis		
		Nauru		

**NL is not included in the figures*

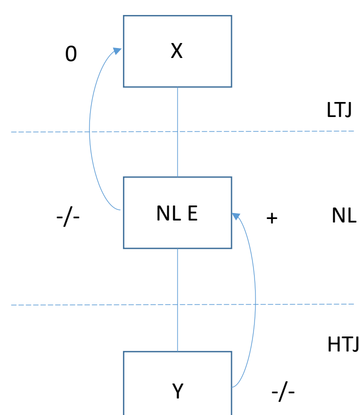
[150] See Monitoring Letter (2020); Parliamentary Papers II 2019/2020, 25087, No. 259.

Annex 4: Examples of tax conduit structures

This Annex provides an overview of a number of common tax-driven conduit structures using some simplified, stylized examples. The legislator has deemed some of these structures undesirable and has already taken (targeted) measures against them or announced that it will do so.[151] This is not the case, or to a lesser extent, for other structures.

Structure 1 (Interest or royalty flow through to LTJ)
Company Y is located in an HTJ. A high-tax jurisdiction here means a jurisdiction that is not designated as an LTJ. Y pays interest or a royalty to Dutch entity E (NL E). NL E passes it on to company X, established in an LTJ. Under the tax treaty between HTJ and the Netherlands, there is no (or a reduced) withholding tax between HTJ and the Netherlands. Until 1 January 2021, there was no withholding tax on interest or royalty payments to an LTJ. In this structure, the group uses the tax treaty between HTJ and the Netherlands and the absence of any withholding tax in the Netherlands on the outgoing interest or royalty payment.

***Annex example** structure 1*



HTJ has a tax treaty with the Netherlands.

It is this type of structure that was also part of the “double Irish with a Dutch sandwich” construction that has been obsolete for some time. Y was in that set up an Irish company that paid royalties to a Dutch entity. In turn, the Dutch entity paid the royalties to a company incorporated under Irish law and domiciled in Bermuda (an LTJ) and therefore deemed to be resident (for tax purposes) there. The Dutch entity was interposed to avoid Irish withholding tax on royalties.

The recent SOMO report “Keep watching” on the tax avoidance structures of ViacomCBS also mentions such a structure, whereby between 2005 and 2010 royalties from various countries were channelled via the Netherlands to Bermuda.[152]

Because the Netherlands does not have a low corporate income tax rate[153], it is desirable from a group perspective to limit the tax burden, i.e. to ensure that payments received are offset by outgoing payments. The Dutch entity E can be (relatively) a shell company or an (existing) operating company. In both cases there is a conduit situation. Only in common parlance is the second case not referred

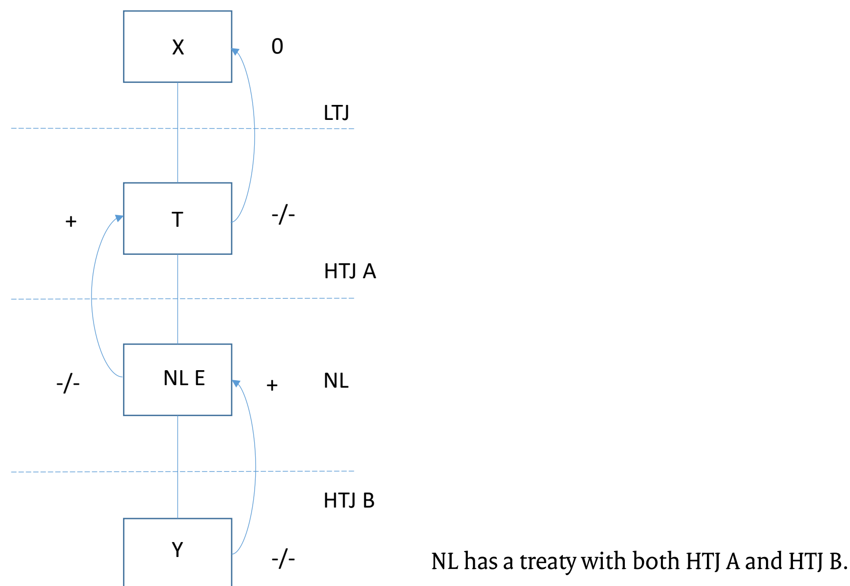
[151] See also paragraph 4.3.
[152] https://www.somo.nl/keep-watching
[153] In 2021, the low rate is 15 per cent and the high rate is 25 per cent.

to as a conduit company or letterbox company. Indeed, on the basis of existing statistical inventories and systems, it is not possible to identify purely conduit activities of non-financial entities.

For the conditional withholding tax on interest and royalties that has been in force since 1 January 2021, it is irrelevant whether the interest or royalty is paid by a shell or active company in the Netherlands. Also, based on the law, whether a shell or an active company receives the payment is irrelevant. If a tax treaty applies between the Netherlands and the LTJ, the rate of conditional withholding tax may be reduced under that treaty.[154]

Structure 2 (Interest or royalty stream with intermediary)
Y pays interest or royalties to NL E. NL E passes it on to the intermediate holding company T. T then pays this to X. There is no (or a reduced) withholding tax between HTJ B and the Netherlands. In affiliated relationships, there is no withholding tax on the payment to the intermediate holding company T in HTJ A if T meets the substance requirements and it cannot be proven that there is an abusive situation.

Annex example *structure 2*



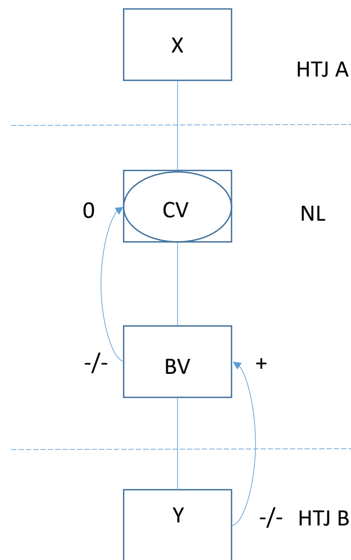
If T satisfies the substance requirements of Article 2 of the 2021 Netherlands Regulations on Withholding Taxes, it is assumed that there is no situation of abuse, unless the Tax and Customs Administration can make a case to that effect.

This structure may have been put in place because the HTJ A-HTJ B relationship is not subject to a reduced rate of withholding tax or the withholding tax that would be levied by HTJ B would not be fully offsettable at T in HTJ A. However, it is possible for HTJ B to levy withholding tax on the payment to NL E using the PPT. The PPT prevents the improper use of the tax treaty between HTJ B and the Netherlands.

[154] In the 2020 Tax Treaty Policy Memorandum, the State Secretary of Finance indicated that he will renegotiate the treaties with LTJs.

Structure 3 (CV-BV construction)
Y pays interest or royalties to BV. BV pays this on to the limited partnership. There is no (or reduced) withholding tax between HTJ B and the Netherlands. The Netherlands considers the limited partnership to be fiscally transparent and therefore not liable to tax. The payment would then have to be taxed at the HTJ A level. However, because HTJ A views the limited partnership as a fiscally non-transparent entity, that does not happen.

***Annex example** structure 3*



In this way, long-term tax deferral could be achieved. However, as a result of the Act Implementing the Second EU Directive against tax avoidance (ATAD2)[155], the payment by the BV has not been deductible since 2020, making this structure no longer fiscally attractive.[156] In addition, hybrid entities are subject to taxation under the Dutch Withholding Tax Act 2021, so that interest and royalties paid to such an entity will, in principle, be subject to withholding tax as from 1 January 2021. It is important to note that this limited partnership (CV private limited company (BV) structure was also used in non-conduit situations where BV was an operating company in the Netherlands.

The CV-BV structure was mainly used by American groups, which could thus defer taxation on the non-US portion of their worldwide earnings (sometimes for a very long time). Only if the limited partnership were to pass on or distribute its income to the American participant in the limited partnership would tax be due on that income in the United States. Until 2018, this type of structure was allowed by the US legislature.[157]

[155] Council Directive (EU) 2017/952 of 29 May 2017 amending Directive (EU) 2016/1164 as regards hybrid mismatches with third countries (OJEU 2017, L 144/1).

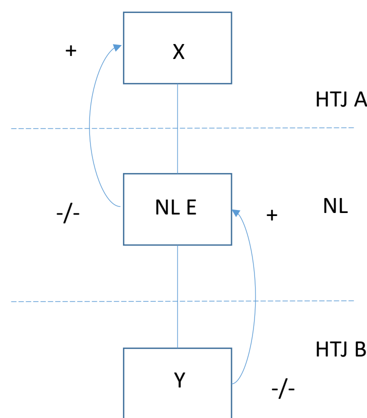
[156] When implementing ATAD2, the Netherlands made use of the option to postpone the entry into force of the tax liability measure for reverse hybrid entities until 1 January 2022. A bill to this end has been introduced as part of the Tax Package 2022. ATAD2 had already eliminated the tax advantages of the CV-BV structure. The bill's purpose is to further prevent hybrid mismatches due to a difference in the classification of partnerships.

[157] As part of the US tax overhaul, a fundamental change was made to the taxation of multinational corporations: from a global to a territorial system. Until this change, all profits (domestic and foreign) were taxed at the time those profits were repatriated to the US.

There have been several investigations into the taxation of US multinationals which have shown that they used the CV-BV structure to defer taxation. The recent SOMO report "Keep watching" on the tax avoidance structures of ViacomCBS also mentions such a structure in the Netherlands between 2016 and 2019.[158]

Structure 4 (Interest or royalty conduit to HTJ)
Y located in HTJ B pays interest or royalties to the Dutch entity E (NL E). NL E passes it on to X established in HTJ A. Under the tax treaty between HTJ B and the Netherlands, there is no (or a reduced) withholding tax between HTJ B and NL. No tax treaty is applicable between HTJ A and HTJ B. There is no withholding tax on the payment from NL E to X in HTJ A. Indeed, X is not located in an LTJ, nor is it an intermediary between NL E and an entity in an LTJ.

Annex example *structure 4*



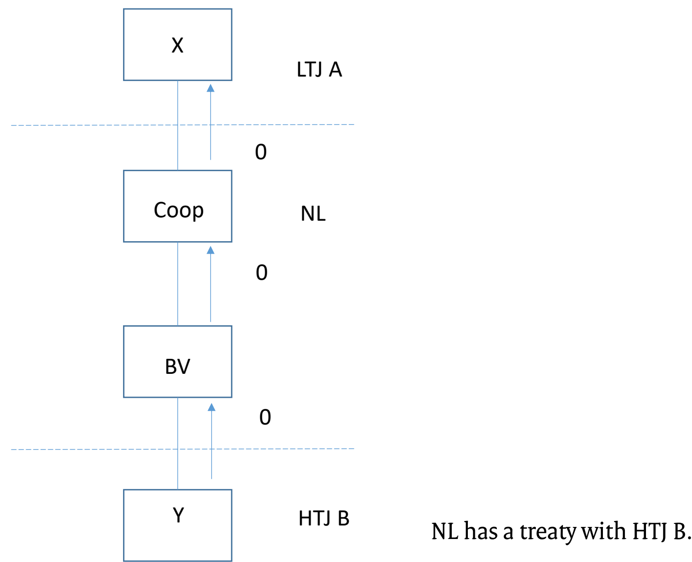
NL has a tax treaty with both HTJ A and HTJ B.

The advantage of this structure is that no withholding tax is levied on the payment by Y. It may be the case that the withholding tax that would otherwise be levied by HTJ B would not be (fully) offsettable at X. There is a conduit in this structure, but this form of conduit does not fall within the scope of the conditional withholding tax on interest and royalties (assuming that X is not a hybrid entity). This is because the Withholding Tax Act 2021 aligns payments to LTJs. However, HTJ B may levy withholding tax on the payment to BV using the PPT. The PPT prevents the improper use of the Dutch treaty network. In addition, pursuant to Article 8c of the 1969 Corporate Income Tax Act, any withholding tax levied on the payment from Y to BV is not offsettable at BV.
Although this structure uses the Netherlands as a jurisdiction to avoid withholding tax in HTJ B, it is HTJ B's responsibility to take measures against this and apply them, just as it is the Netherlands' responsibility to take measures against the avoidance of Dutch dividend tax on dividends paid to LTJs or in abusive situations. If there is insufficient substance, the Netherlands will provide information about NL E to HTJ B, as provided for in Article 3a of the Income Tax Act.

[158] https://www.somo.nl/keep-watching.

Structure 5 (Dividend payment to LTJ)
Y pays a dividend to NL E and NL E passes it on to X via a cooperative. The dividend is paid to NL E without withholding tax. The dividend is subject to the participation exemption in NL E. NL E passes dividend to a cooperative without withholding tax. If the cooperative is a holding cooperative, it will have to withhold dividend tax on the dividend payment to X (unless stipulated otherwise by a treaty). In other cases, a cooperative is not subject to withholding tax on dividends.

***Annex example** structure 5*

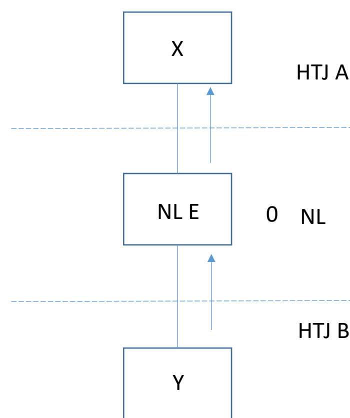


NL has a treaty with HTJ B.

This structure is therefore advantageous only if the cooperative does not qualify as a holding cooperative. In affiliated situations, dividend payments by all cooperatives to LTJs will be subject to withholding tax as of 2024 pursuant to the bill to introduce a conditional withholding tax on dividends.

Structure 6 (dividend payment by intermediate holding company)
Y pays a dividend to NL E and NL E passes it on to X. The dividend is paid without withholding tax to the Netherlands under the tax treaty between the Netherlands and HTJ B. At NL E, the dividend falls under the participation exemption. No dividend withholding tax is levied on the dividend payment from NL to HTJ A under the tax treaty between NL and HTJ A or the Parent-Subsidiary Directive. The participation exemption also covers the dividend received by HTJ A.

Annex example *structure 6*



NL has a treaty with both HTJ A and HTJ B.

A motive for this structure may be the avoidance of dividend tax by HTJ B, for example, if there is no treaty between HTJ A and HTJ B. HTJ B may still be able to levy withholding tax on the payment to NL E using the PPT. The PPT prevents the improper use of the Dutch treaty between HTJ B and the Netherlands.

Although in this structure too, the Netherlands can be used as a jurisdiction to avoid withholding tax in HTJ B, here too it is the responsibility of HTJ B to take measures against this and to apply them, just as it is up to the Netherlands to take measures against the avoidance of Dutch dividend tax on dividends paid to LTJs or in abusive situations.

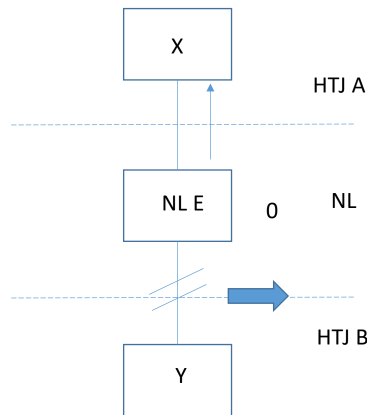
In the Annex to the government's response to the report of the Advisory Committee on Taxation of Multinationals, it was announced that regulations will be introduced as of 2022 that will provide for the possibility of exchanging information with foreign countries for conduit companies (flow of dividends) that have insufficient substance (within the meaning of Article 3a(7) of the Income Tax Act).

Another motive may be that, at the level of HTJ A, the participation exemption applies in the relationship between HTJ A and the Netherlands (e.g. based on the Parent-Subsidiary Directive), but not in the relationship between HTJ A and HTJ B. The intermediation of an entity in the Netherlands in this type of situation could explain the large number of conduit companies in the Netherlands.

There are many holding companies in the Netherlands. This includes active holding companies of foreign concerns with qualified personnel in the Netherlands. Taxation (in particular the participation exemption and the treaty network) is a factor in the choice of the Netherlands as a 'holding country', but company law and infrastructure are also important factors.

Structure 7 (Disposal by intermediate holding company)
NL E disposes of the shareholding in HTJ B. The gain on disposal falls under the participation exemption. NL E distributes the profit to HTJ A untaxed (without withholding tax).

***Annex example** structure 7*



NL has a treaty with both HTJ A and HTJ B.

The motive for setting up the structure may be that gains on disposal are not exempt in HTJ A or that in HTJ B a withholding tax would apply to the gains on disposal if X had directly disposed of the shares in Y; the treaty between the Netherlands and HTJ B prevents that if NL E disposes of the shares in Y.

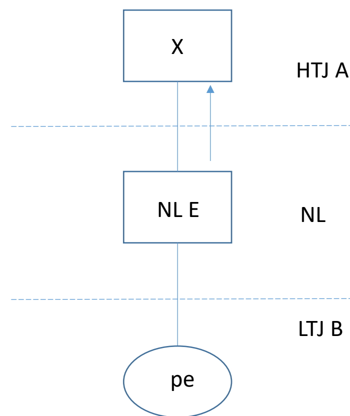
HTJ B may still be able to levy withholding tax on the gain on disposal using the PPT. The PPT prevents the improper use of the tax treaty between HTJ B and the Netherlands. The Netherlands could also apply the PPT in case of improper use of the tax treaty between the Netherlands and HTJ A. It is also possible that HTJ A may nevertheless tax the gains on disposal of the Y 3 shares by using the PPT in the treaty with the Netherlands.

For the rest, Dutch legislation and regulations do not provide for measures against this type of (holding) structure.

In a variant of this structure, not the shares in Y but the shares in NL E are disposed of. In that case, nothing flows through NL but NL E is used as a vehicle to possibly avoid tax on the disposal of Y in HTJ B or Y's assets.

Structure 8 (permanent establishment in LTJ)
In this structure, there is a permanent establishment (PE) in LTJ B. The PE's profits were not taxed or were taxed at a low level in B. The PE profit is not taxed at NL E level in the Netherlands because of the object exemption. This is different when it comes to passive income. If so, the Netherlands will not apply the object exemption under certain conditions. NL E distributes its profits (including the part attributable to the PE) to X in HTJ A.

***Annex example** structure 8*



The tax benefit could be that if X had had a PE in LTJ B, that PE profit would not have been exempt in X, but a credit would 'only' have been given in HTJ A for the tax paid in LTJ on the PE profit. Since NL E's profits are passed on to X, there is a conduit situation.

This is a publication of:

Ministry of Finance
PO Box 20201 | 2500 EE The Hague
T 070 342 80 00 (Monday till Friday 8.00 – 20.00 hour)

October 2021