

The global problem of tax havens: The case of the Netherlands

SOMO Tax Briefing paper

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*'For centuries, the Netherlands has encouraged entrepreneurial spirit, an international perspective and open market policies. These historical factors, along with the country's secure political and economic climate, make it a near perfect environment for international tax planning. This environment is further enhanced by the Netherlands' network of tax agreements with virtually every significant financial territory in the world, as well as the benefits that can be gained from basing intermediate holding companies within the Netherlands Antilles.'*¹

The harmful effects of tax havens

Tax havens are a global problem. They undermine the interests of poor countries in four major ways:²

- ❑ Secret bank accounts and offshore trusts in tax havens provide wealthy elites and companies with the means to escape their tax obligations.
- ❑ Multinationals' ability to substantially lower their tax burden by routing capital flows through mailbox companies in tax havens provides them with unfair competitive advantages vis-à-vis their – often smaller – competitors in developing countries.
- ❑ Banking secrecy and offshore trusts offered by financial institutions in tax havens make it possible to launder the proceeds of political corruption, illicit arms deals, and other crimes.
- ❑ Tax havens have contributed to the rising incidence of financial crisis that can destroy livelihoods in poor countries.

As a result of tax avoidance and tax evasion, countries both poor and rich fail to collect important tax revenues that could have been used to combat poverty and stimulate development. This affects national and international development efforts, including the achievement of the Millennium Development Goals (MDGs), such as halving extreme poverty and hunger, universal primary education, and halting the spread of infectious diseases worldwide by 2015. The Tax Justice Network (TJN) estimates that as much as US \$255 billion is lost every year to governments around the world because of the low or zero taxation of funds in offshore centres.³ This amount is larger than the estimated cost to halve world poverty by 2015.

The definition of tax havens

There is no such thing as a standard tax haven. One can make the distinction between 'pure' tax havens and countries which exhibit harmful preferential tax regimes. 'Pure' tax havens correspond with the standard image of the offshore tropical island hosting numerous 'brass plate' companies. Assisting tax avoidance or evasion is usually their main source of income. Examples are the Bahamas, Cayman Islands, and Bermuda. The second group consists of countries with a diversified economy and a normal tax system but with certain, often deliberately designed, exceptions for particular activities or types of corporate activities, which can be used by multinationals to substantially lower their overall tax burden. The Netherlands is clearly a tax haven of this second type. ◉

The Netherlands: A tax haven for multinationals

Empirical Evidence

All the empirical evidence indicates that the Netherlands is a tax haven for multinationals. This is because it deliberately offers companies who would not otherwise seek to be resident within its territory the means to reduce their tax charges on interest, royalties, dividends and capital gains income from subsidiary companies.

- Tax planning websites and international trust offices advertise the Netherlands as a historically important offshore and tax planning centre. They offer various constructions involving Dutch subsidiaries that allow multinationals to lower their tax charges in other countries.
- Both the OECD and the EU identified the Netherlands as a country that engages in harmful tax competition.⁴ As a consequence, many of the arrangements created by the Netherlands have been revised in 2001. However, at present the Dutch government is in the process of introducing new and equally disturbing legislation to replace the old practices.
- Many corporations based in the EU or elsewhere have a presence in the Netherlands primarily for fiscal benefits. Examples of companies that have their ultimate or intermediate headquarters in the Netherlands primarily for this reason include IKEA, Mittal Steel, EADS (parent company of Airbus), Nike, Trafigura, and Fujitsu-Siemens.
- The Netherlands hosts nearly 20,000 mailbox companies which do not have a substantial commercial presence.

This number is growing rapidly. In 2006, five new mail companies were established every day on average. Official statistics of the Dutch Central Bank (DNB) count 12,500 Special Financial Institutions (SFIs) in 2002, which are defined as foreign companies present in the Netherlands at least partly for fiscal reasons. In 2003, gross transactions of SFIs amounted to € 3,600 billion – more than eight times the Dutch GNP.

What makes the Netherlands so popular?

The Netherlands facilitates so-called 'conduit structures' which make it possible for internationally operating companies to channel their financial flows through the Netherlands in order to reduce tax charges elsewhere. Usually, such arrangements involve mailbox companies, which are used to reallocate revenues to 'pure' tax havens, where zero or only very little tax has to be paid. Whereas some types of conduit structures may be legitimate, some appear to be quite harmful for other countries.

Out of the 42,072 financial holding companies registered in the Netherlands for which information on the (ultimate) parent was available, 5,830 are mailbox companies, managed by trust offices. Of these companies, 43% have a parent in a tax haven jurisdiction such as the Netherlands Antilles, Switzerland, Cyprus, the British Virgin Islands or the Cayman Islands. Hence there is a clear link to tax havens for conduit structures (also see figure).

The Dutch group financing (CFM) regime, which will be abolished by 2011 following pressure from the EU, is slightly different. It is one of the most harmful tax policies and may result in lost tax revenues in other countries, both poor and rich. The Dutch government is currently replacing the CFM regime by the so-called 'group interest box', which will be



The Netherlands - tax haven link

Location of (ultimate) parent company of mailbox companies in the Netherlands managed by trust offices. The figure only depicts a subsample of the total number of mailbox companies.

Controversial fiscal affairs with link to the Netherlands

Parmalat (Italy) borrowed six billion Euro - now missing - using a Dutch mailbox company. The head office of **Trafigura** (Switzerland) - the company involved in the Ivory Coast toxic waste disaster - is nothing more than a mailbox company in the Netherlands. **Enron** (USA) used mailbox companies in the Netherlands to cover up fraude. The children of former dictator **Suharto** (Indonesia) used Dutch mailbox companies to raise investment capital for their enterprises.

USA 691

Bermuda 23

British Virgin Islands 49

Cayman Islands 38

Netherlands Antilles 1430

UK 331
Belgium 331
Luxembourg 409

France 140

Switzerland 62

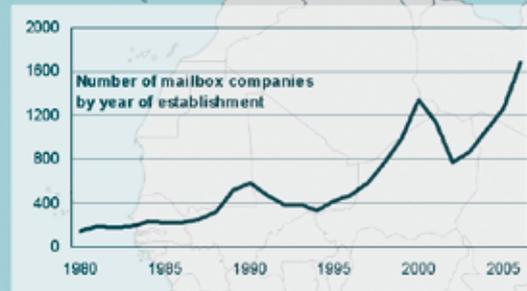
Italy 163

Sweden 111

Germany 51

Cyprus 54

Israel 109



offering tax rates as low as 5% on interest income. This might mean that the Netherlands will be offering the lowest tax rates on financial flows in the developed world.

One of the main factors which make the Netherlands so attractive for conduit and group financing structures is the extensive Double Taxation Treaty (DTT) network, which allows for multinationals to substantially reduce withholding taxes on dividend, interest and royalty payments on financial flows to and from other countries and tax havens via the Netherlands.

Positive and negative effects

The Netherlands mainly benefits from attracting financial flows to its territory by increasing the tax yield it enjoys from corporate income and from employment generated in the trust and tax consultancy sector. It has been estimated that the activities of the 12,500 SFIs generate some 2,500 direct jobs and a total direct revenue for the Dutch state of € 1.7 billion. It is expected that measures such as the new 'group interest box' will not generate substantial new employment in the Netherlands.

However, these benefits do not outweigh the negative consequences for other countries. It affects both the capacity of developing country governments to supply essential

services to their populations and the capacity of developed country governments to provide finance for development in the form of debt relief and Official Development Assistance (ODA). Hence, the Dutch tax policy is clearly inconsistent with the policy on development cooperation. Furthermore, it results in a shift of the tax burden to other sources of income such as labour and reduces possibilities for smaller companies to compete with multinational corporations. The tax haven features of the Netherlands also facilitate money laundering and attract companies with a dubious reputation.

Recommendations

In order to promote a fair and just global economic system in which tax avoidance by multinational corporations is minimised, SOMO presents the following recommendations.

- The Netherlands must put an end to harmful tax policies and stop being a bridge between tax havens and other countries as soon as possible.
- However, tax havens are a global problem which requires a global solution, and the Netherlands putting an end to its harmful tax policies is a necessary but not sufficient step. Hence it is important that the Netherlands also actively puts pressure on other OECD countries to follow suit.

- The Dutch government should commission an official research on the Netherlands as a tax haven. This SOMO report is the first comprehensive report on this issue and a more detailed study, including a more quantitative analysis, would be desirable.
- The Dutch Central Bank (DNB) should regularly publish statistical information on SFIs.
- To support transparency, a new mandatory International Accounting Standard should be adopted that requires multinationals to provide detailed financial information on subsidiaries.⁵
- All relevant actors, including corporations, government, civil society organisations, consultants, and analysts, should recognise refraining from tax avoidance as a core element of Corporate Social Responsibility (CSR).

About SOMO

SOMO (Centre for Research on Multinational Corporations) is a Dutch non-profit research and advisory bureau that investigates the consequences of multinational corporations' policies and the internationalisation of business worldwide.

Recognising that it is a core responsibility of multinational corporations to pay their fair share of taxes, SOMO aims to incorporate this topic in all its regular activities. Occasionally SOMO also initiates tax-related research projects with Southern partners. Currently we are working with a Southern organisation to investigate financial flows from African-based subsidiaries of multinationals via the Netherlands.

At present, SOMO, together with other Dutch organisations, is establishing the Tax Justice Network Netherlands (TJN-NL). TJN-NL will coordinate activities and carry out lobby and research on harmful tax competition, tax havens, and related topics, such as innovative resources for financing development and environmental taxes. The launch of the TJN-NL is planned for Spring 2007.

As explained above, many multinationals use Dutch Limited Liability Companies (BVs) for group financing purposes or to route financial flows from subsidiaries to other countries (including 'pure' tax havens). As part of its research strategy, SOMO is continuously looking for information on such structures, in particular those which may negatively affect developing countries. We welcome any relevant information on the issue. In case you are aware of potential cases of tax avoidance that might merit further investigation, or are interested to learn how to conduct such research, please contact us.

Endnotes

- 1 Deutsche Bank - Offshore Group, "An introduction to the Netherlands," <<http://www.dboffshore.com/offshore/html/location/netherlands.shtml>> (Aug 2006).
- 2 TJN, 'Tax Us If You Can', The Tax Justice Network, London, 2005, available as a download from www.taxjustice.net.
- 3 TJN, 'Tax Us If You Can', *ibid*.
- 4 Primarolo Group, "Code of Conduct (Business Taxation)," 29 Nov 2000, <<http://www.uv.es/cde/TEXTOS/primaloro.html>> (Sep 2006); OECD, "Towards Global Tax Co-operation: Progress in Identifying and Eliminating Harmful Tax Practices," 2000, <<http://www.oecd.org/dataoecd/9/61/2090192.pdf#search=%22towards%20global%20tax-cooperation%22>> (Sep 2006)
- 5 R. Murphy, "Reporting Turnover and Tax by Location: A Proposed International Accounting Standard," AABA, 2003, <http://www.taxjustice.net/cms/upload/pdf/new_int_Account_Standard.pdf> (Nov 2006).
- 6 http://www.somo.nl/html/paginas/pdf/netherlands_tax_haven_2006_NL.pdf

Colophon

This briefing paper is based on the research report:
M. van Dijk, F. Weyzig and R. Murphy, 'The Netherlands:
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