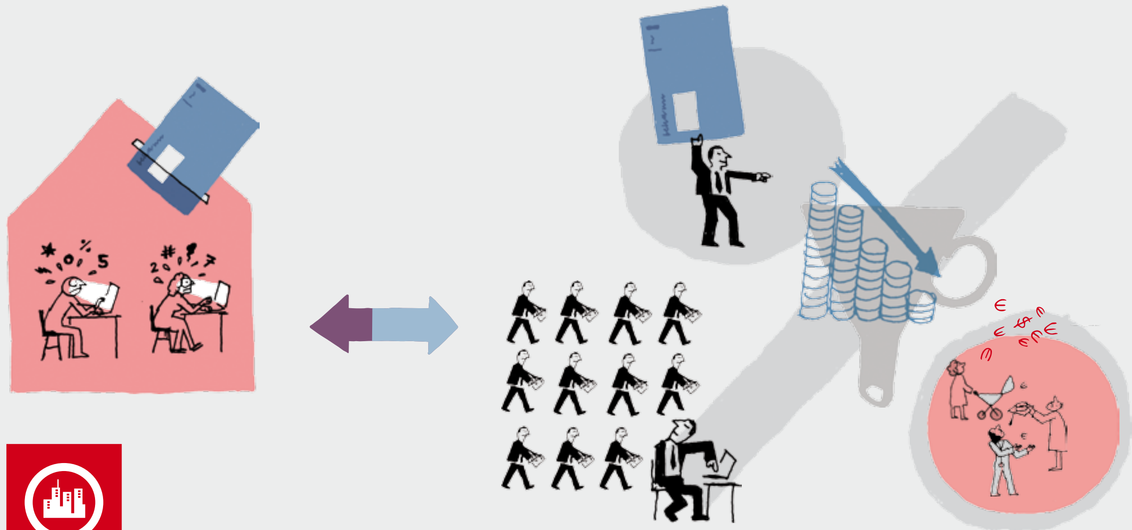

Big Companies, Low Rates

A study of the effective tax rates of large Dutch companies

Summary | March 2016

The report "Grote Bedrijven, Kleine Lasten" (Big Companies, Low Rates) examines the average, effective tax rate for a group of more than 150 large Dutch companies over a period of ten years (2005-2014).[1] This paper is a summary of the full report. You can find a version of the Research Methodology in Annex II of the full report. In recent years, tax avoidance by foreign companies, and role of Dutch tax policy in that, has frequently featured prominent in the media. The report focuses on a group of Dutch companies and the degree to which they have succeeded in reducing their effective tax rates. The effective tax rate expresses the actual tax liability of a company as a percentage of pre-tax profit. It is an indicator of the degree to which companies succeed in reducing their tax liabilities by tax avoidance – shifting of profits through (artificial) constructions which push the boundaries of the law– and by the use of fiscal stimuli offered by governments.

Context: Inequality and harfmul competition

Tax avoidance has existed for centuries, but has increased considerably in recent decades due to the increasing international mobility of capital. Governments make attempts to tackle the large-scale tax avoidance. At the same time, they are entangled in a destructive competition with other countries to attract foreign investors by means of fiscal stimuli. The Dutch government, for example, reduced the statutory tax rate for taxation on company profits (corporate income tax) from 31.5 per cent in 2005 to 25 per cent in 2014.[2] Partly due to this international harmful competition, fiscal inequality – the difference in the degree to which labour (wages) and capital (company profits and capital) are taxed – has become ever greater. Within this context is it also key to examine the fiscal practices of (Dutch) companies.

Conclusions from the study

Effective tax rates of large Dutch companies

- The average effective tax rate of 93 listed Dutch companies which were examined amounted to 21.45 per cent over a decade, from 2005-2014.
- The average effective tax rate of 58 non-listed Dutch companies which were examined amounted to 17.88 per cent over the decade from 2010-2014.
- This means that the company profits were effectively taxed at rates of 21.5 and 18 per cent, respectively. This is lower than the average statutory rate over this same period. This therefore leads to a loss in tax revenues for governments.

In the report, 151 companies were examined: 93 are publically listed 58 are non-listed companies. On the basis of publicly available financial information, data was collected and analysed for all companies in terms of the profits and the fiscal liabilities.

Calculated tax-revenue losses for the Netherlands

- The low effective tax rate leads to tax-revenue losses: an estimated € 3 billion per year in the period from 2005-2014.
- Since approximately half the profits of Dutch companies are made and taxed in the Netherlands itself, the Dutch National Treasury is losing an estimated € 1.5 billion per year, which is more than 10 per cent of the total yield from the corporate income tax that the Dutch government receives annually.

A comparison between a worldwide statutory tax rate and the effective tax rate of the group of large Dutch companies leads to this estimate of lost tax revenues for governments. Given that Dutch companies also make profits abroad, which are subsequently taxed there, a worldwide statutory rate was calculated. In other countries, after all, different tax rates apply. According to data from the Dutch Centraal Bureau voor de Statistiek (Central Bureau for Statistics – CBS), approximately half of the total profits made by Dutch companies are generated abroad. On the basis of this relationship between domestic and foreign profits, it is estimated that the Netherlands is losing € 1.5 billion per year in tax revenues. The same applies to those foreign governments where the subsidiaries of Dutch companies are generating profit.

Tax avoidance and fiscal policies

There are a number of reasons for the lower effective tax rates of companies.

- Firstly, a lower effective tax rate can be a result of tax avoidance. The shifting of profits, from countries with high tax rates where profits are actually generated, to countries with low tax rates, is in fact reflected by an effective tax rate. However, tax avoidance involves more than the shifting of profits. Various other forms of tax avoidance have not been measured in this study, which means that the actual tax revenue loss due to tax

Table 1: Effective tax rate of 93 listed Dutch companies and the resulting estimated tax foregone for governments, 2005-2014 (in million EUR)[3]

	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	Total	Annual average
Pre-tax income	31,850	36,052	41,159	10,634	10,130	28,881	24,580	17,987	24,802	23,560	249,633	24,963
Income tax expense	6,906	6,989	6,039	3,699	1,185	6,277	5,969	5,467	5,518	5,510	53,558	5,356
Effective tax rate (in %)	21.68	19.39	14.67	34.79	11.69	21.74	24.28	30.39	22.29	23.39	n.b.	21.45
Tax expense according to statutory tax rate	10,480	11,328	11,975	3,071	2,855	8,238	6,865	5,094	7,029	6,550	73,485	7,349
Tax foregone estimate	3,574	4,340	5,936	-629	1,670	1,960	897	-372	1,512	1,040	19,928	1,993
Tax foregone attributable to foreign countries	1,764	1,850	2,581	-331	753	1,032	438	-217	903	577	9,348	935
Tax foregone attributable to the Netherlands	1,810	2,490	3,355	-298	917	928	459	-155	609	463	10,579	1,058

Table 1 shows the results of the research into the effective tax rates of 93 large, listed Dutch companies.

Table 2: Differences in average effective tax rates of listed companies, divided into five categories, 2005-2014[4]

Effective tax rate	0 - 10%	10 - 20%	20 - 30%	30 - 40%	Outliers	Total
Number of companies	14	15	27	7	30	93
Pre-tax income of category as percentage of total pre-tax income (93 companies)	11%	38%	44%	3%	4%	100%

Table 2 shows that, on average in the period 2005-2014, almost half of the profits of the group of 93 listed companies was effectively taxed with a rate between 0-20 per cent.

Table 3: Effective tax rate of 58 unlisted Dutch companies and the resulting estimated tax foregone for governments, 2010-2014 (in million EUR)

	2010	2011	2012	2013	2014	Total	Annual average
Pre-tax income	9,933	10,354	9,055	10,418	8,866	48,626	9,725
Income tax expense	1,880	2,079	1,697	1,710	1,326	8,692	1,739
Effective tax rate (in %)	18,92	20,08	18,74	15,78	14,31	n,b,	17,88
Tax expense according to statutory tax rate	2,833	2,892	2,565	2,953	2,465	13,707	2,741
Tax foregone estimate	954	813	867	1,242	1,139	5,015	1,003
Tax foregone attributable to foreign countries	502	397	506	742	632	2,778	556
Tax foregone attributable to the Netherlands	452	416	361	500	507	2,236	447

Table 3 shows the results of the research into the effective tax rates of 58 large, unlisted Dutch companies (family-owned companies and cooperatives).

Table 4: Differences in average effective tax rates of unlisted companies, divided in five categories, 2010-2014

Effective tax rate	0 - 10%	10 - 20%	20 - 30%	30 - 40%	Outliers	Total
Number of companies	8	7	34	4	5	58
Pre-tax income of category as percentage of total pre-tax income (58 companies)	24%	58%	17%	2%	0%	100%

Table 4 shows that, on average in the period 2010-2014, over 80 per cent of all profits of the unlisted companies was subject to an effective tax rate of 20 per cent or lower.

evasion and avoidance will in reality be greater than the € 3 billion estimated in this study.[5]

- Secondly, the Dutch government justifies its tax policies based on the notion of stimulating economic activity and the intention of preventing double taxation. In the study, we have attempted to minimise the effect of fiscal policies by, amongst other things, researching a long time period and by taking account of profits made abroad. In addition, the effectiveness and justice of these fiscal policies are brought into question.

Avoidance strategies of large Dutch companies

A quartet of well-known strategies which companies use in order to avoid taxation are scrutinised in this study. Amongst other things, interest, royalties and dividend payments between subsidiary companies of the same corporate group are often employed in order to shift profits around.

- **At least seven parent companies of the 93 listed Dutch companies examined are partially financed with loans from subsidiary companies.**
  Shifting profits through interest payments. Misuse of intra-group financing – group entities within a corporate group which finance each other – is a well-known evasion strategy. The interest which must be paid on the intra-company loan by the borrowing subsidiary can reduce the taxable profits in the one country (with high tax rates) and, on the contrary, increase profits in the other country (which has low rates) where the lending subsidiary is based. Companies provide very little insight into these types of transactions between group entities. The research findings are therefore limited: it is therefore very likely that intra-group financing takes place on a much larger scale.

- **At least seven of the 151 companies examined appear to make use of the Belgium route.**
  The Belgium route: Belgium has the so-called notional interest deduction, which offers companies the possibility of determining a notional interest on its own equity and then subsequently deducting that interest from the taxable income. This is similar to the tax deductibility of interest on loans or debt owed. This study shows that at least seven of the 151 Dutch companies appear to make use of the Belgium route, although only a small sample from the entire group was investigated. In some cases, the Belgian subsidiary company is instrumental in the firm's overall corporate structure, when 20 to as much as 75 per cent of their global equity is deposited in Belgium.

- **Switzerland is the most popular location of choice for intellectual property rights.**
  Shifting profits through royalties: Reimbursement must be made for the use of the company's intellectual property (IP) rights, such as patents and trademarks: royalties. By inflating these royalty payments, profits can be shifted just as is the case with interest payments. The location of the intellectual property rights is therefore important. Of the 151 companies in the study, 105 companies have subsidiaries with patents and/or trademarks. Looking solely at the letter box companies – the subsidiaries with a very small number of employees – Switzerland turns out to be the most popular destination for intellectual property rights followed by the Netherlands, due to (amongst other things) the lack of withholding taxes on royalties in both countries.

- **Switzerland is also the most popular tax haven among the Dutch companies.**
  Presence in tax havens: This study found that the Dutch companies in the sample have, at least 388 subsidiaries in tax havens. Of the 151 companies investigated, 58 have subsidiaries in tax havens. Nearly 80 per cent of the total number of tax haven subsidiaries is established in Switzerland, Singapore, Hong Kong, Ireland and Luxembourg, all notorious tax havens.

Suggestions for further research

The report offers new insights with regards to the effective tax rate of large Dutch companies, and the associated lost tax revenues as well as the possible tax avoidance strategies used by some of the biggest Dutch companies. One important limitation of this study is the lack of sufficient publicly available financial data, specifically with regards to what takes place within a corporate group – thus, between subsidiaries. Due to this limitation, this study is only able to estimate and identify indicators (red flags) of tax avoidance. Further investigation into specific companies at the individual level is needed in order to obtain more insight and evidence with regards to losses in tax revenue for governments.

Recommendations

On the basis of the above findings, the following recommendations are made to the Dutch government:

Ensure a fair tax policy in which multinational companies

- make their contribution to society by paying the profits tax that they ought to pay:
- The statutory tax rate must be guiding, and be in a fair proportion to the tax rates imposed on the incomes of workers.
- The participation exemption must be limited, so that profits made abroad are taxed at a minimum rate of 25 per cent.
- The innovation box must be abolished; in place thereof, innovation could be stimulated via targeted subsidy schemes.

Take action against international tax competition and profit shifting:

- Unilateral action: intra-group payments to tax havens must be taxed in the Netherlands by means of a withholding tax with a statutory rate of 25 per cent.
- European action: a uniform European taxation playing field must come into being, which is based on uniform principles, uniform depreciation periods and uniform treatment of interest and royalty payments.
- International action: in addition to the implementation of recent agreements which have been made within the OECD for the purpose of tackling international tax evasion and avoidance, the Netherlands must promote a structural reform of the international taxation system, in which economic activity is the guiding principle rather than legal presence (unitary taxation).

Create greater financial transparency so that citizens and organisations can call both companies and governments to account for taxation practices and policy.

- Governments must oblige companies to make public financial reports per country. This so-called country-by-country reporting makes it possible to assess where companies have (genuine economic) activities, how much profit they generate in different countries and where they pay taxes.
- The country-by-country reporting must also provide insight into transactions which take place within the corporate group – thus, between group entities – because it is here that the greatest avoidance takes place.

Endnotes

1 Some of the biggest Dutch companies including Shell and HEMA were not included in this study. The complete list of companies is included in the Dutch report Grote Bedrijven, Kleine Lasten (Annex I).

2 The statutory rate for corporate income tax in the Netherlands is the legally-prescribed tax rate that is used for taxation of company profits.

3 The effective tax rate is the income tax expense as percentage of pre-tax income. In this research, it is calculated by dividing the consolidated income tax expense by the total consolidated pre-tax income, as reported by companies in their annual financial statements in the years 2005-2014.

4 Outliers are companies with effective tax rates above 40 per cent, or negative effective tax rates.

5 Moreover, tax evasion and avoidance possibly also take place among companies that were not examined – including both large companies like Shell and HEMA which were not included in this study, and smaller companies.

Colophon

This paper is a translated summary of the report 'Grote Bedrijven, Kleine Lasten' (Big Companies, Low Rates)

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