

## Dutch Treaty Policy Regarding Latin American Countries

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**T**his article examines the international tax treaty policy of the Netherlands regarding income tax treaty negotiations, including the relevant parts of the Memorandum Tax Treaty Policy 2011 (2011 TTP) published by the minister of finance in the Netherlands. It further analyzes the treaties concluded between the Netherlands and Latin American countries, mainly with Argentina, Brazil, Mexico, Panama, and Venezuela.

### I. Introduction

In order to enhance international tax cooperation and tax competition, developing and developed countries are searching for bilateral instruments to exchange information, to promote transparency, and to enhance and protect foreign direct investments. Also, the increased interest of governments to challenge capital flows from developing and developed countries to tax havens and offshore financial centers<sup>1</sup> resulted in political leaders addressing the following in G-8 and G-20 meetings<sup>2</sup>:

- the importance for developing countries to enhance international tax cooperation, including exchange of information among tax administrations and other law enforcement agencies, to counter illicit activities; and
- their willingness to assist developing countries to strengthen their tax systems with the goal of increasing their own tax revenue resources.<sup>3</sup>

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have taxing rights in respect of that income or those assets. Data on revenues lost by developing countries from offshore non compliance is unreliable. Most estimates, however, exceed by some distance the level of aid received by developing countries — around USD 100 billion annually.

OECD, “Promoting Transparency and Exchange of Information for Tax Purposes: A Background Information Brief,” May 10, 2010, at 6.

<sup>2</sup>For instance, in the G-20 summits in Washington, London, and Pittsburgh, and in the G-8 summits in L’Aquila and Lecce (Italy) and Hokkaido (Japan), among others, political leaders expressed their commitment to tackle tax evasion and their willingness to take actions against noncooperative jurisdictions including tax havens, and against those countries that do not meet OECD international standards for transparency and exchange of information.

<sup>3</sup>See Irma Johanna Mosquera Valderrama, “EU and OECD Proposals for International Tax Cooperation: A New Road?” *Tax Notes Int’l*, Aug. 23, 2010, p. 609.

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<sup>1</sup>For the OECD:

offshore financial centers, broadly defined, reduce revenue available to developing countries where they act as a destination for income streams and wealth protected by a lack of transparency and show a refusal or inability to exchange information with revenue authorities who may

(Footnote continued in next column.)

Despite those common objectives, the instruments used by countries vary in accordance to the tax or investment policy of each country and sometimes to the status of some countries as developing countries, offshore financial centers, and tax havens. Those instruments consist of the following:

- bilateral investment treaties;
- income tax treaties following the OECD model;
- income tax treaties following the U.N. model;
- bilateral and multilateral tax information exchange agreements following the OECD Model Agreement on Exchange of Information on Tax Matters; and
- the Multilateral Convention on Mutual Administrative Assistance in Tax Matters jointly developed by the Council of Europe and the OECD.<sup>4</sup>

The objective of this article is to analyze and address:

- the international tax treaty policy of the Netherlands applied to treaties concluded between the Netherlands and Latin American countries; and
- the relevant parts of the Netherlands' 2011 TTP.<sup>5</sup>

Section II describes the main objectives of the Netherlands' policy outlined in the 2011 TTP. Section III examines the most relevant provisions in the treaties concluded by the Netherlands. The relevant provisions addressed in this article concern residence, permanent establishment, dividends, interest, royalties, capital gains, most favored nation clauses, antiabuse clauses, interpretation, and arbitration. Finally, in Section IV, some recommendations are provided regarding the international tax treaty policy of the Netherlands.

## II. Background

### A. Treaty Network

The Netherlands has an extensive network of bilateral tax treaties. Based on the most recent treaty overview (April 2013) as published by the Dutch Ministry of Finance,<sup>6</sup> the Netherlands has concluded 97 treaties. Within Latin America, the Netherlands has concluded treaties with Argentina (1998), Brazil (1991), Mexico (1994 and 2009 protocol), Panama (2011), and Venezuela (1997), and it is negotiating with Colombia (advanced negotiations) and Chile.

<sup>4</sup>This convention provides a multilateral basis for a wide variety of administrative assistance, including information exchange on request, automatic exchange of information, and simultaneous tax examinations; available at <http://www.oecd.org/ctp/exchangeofinformation/conventiononmutualadministrativeassistanceintaxmatters.htm>.

<sup>5</sup>The 2011 TTP was adopted by the Dutch parliament in mid-2012.

<sup>6</sup>See <http://www.government.nl/ministries/fin>. See also <http://www.eoi-tax.org/jurisdictions/NL#agreements>.

Also, the Netherlands has concluded 29 TIEAs, mainly with tax havens and offshore financial centers (for example, the Cayman Islands, the British Virgin Islands, and Bermuda). With Latin American countries, the Netherlands has concluded a TIEA with Costa Rica (in force) and Uruguay (not yet in force).<sup>7</sup> Further, the Netherlands is a signatory to the OECD-Council of Europe Multilateral Convention on Mutual Administrative Assistance in Tax Matters.

### B. The 2011 TTP

On February 11, 2011, the Netherlands published the 2011 TTP, which among other things addressed the goal to enhance international tax cooperation by strengthening "domestic resource mobilization" and by means of enhancing transparency and exchange of information in tax matters.

The first objective results in the Netherlands' willingness to assist in the strengthening of tax administrations of developing countries and to cooperate with the work of the OECD Informal Task Force on Tax and Development. The second objective regards the Netherlands' goal to expand its tax treaty network to an increased number of developing countries. The third objective results in the Netherlands concluding treaties with developing countries containing provisions (that is, article 26 of the OECD model) regarding the exchange of information (on request, automatic, and spontaneous) as well as by concluding TIEAs.

The Netherlands also states in the 2011 TTP that the use of the Dutch standard treaty model is no longer necessary because the Netherlands predominantly concludes its treaties in accordance with the OECD model.<sup>8</sup>

Within the above context, the following paragraphs will deal with the international tax treaty policy of the Netherlands regarding issues that are of relevance when concluding treaties with Latin American countries.

## III. Dutch Tax Treaty Policy

### A. Residency

When concluding treaties, the Netherlands follows the OECD model, stating that the treaty applies to residents of one of the contracting states regardless of their nationality (article 1 of the OECD model). The Netherlands also includes in the definition of resident the requirement that the person must be liable to tax in one of the contracting states (article 4(1) of the OECD model).

Further, under the 2011 TTP, the Netherlands attempts to consider entities that in principle are not

<sup>7</sup>*Id.*

<sup>8</sup>Preface 2011 TTP (*Voorwoord Notitie Fiscaal Vedragsbeleid* 2011), at 9-10.

liable to tax to qualify as residents for tax treaty purposes (exempt entities). This approach follows the OECD commentary to article 4(1) of the OECD model (paragraphs 8.5 and 8.6). As a consequence, under the 2011 TTP, the following entities can be regarded as residents even though they are not liable to tax: pension funds, nonprofit organizations, associations and foundations (without entrepreneurial activities), and exempt investment institutions (*vrijgestelde beleggingsinstelling*).

Based on the above, when negotiating treaties, the Netherlands has a goal of regarding entities liable to tax — if those entities are governed by Dutch law or if their place of central management is in the Netherlands (and further, those entities are considered tax transparent) — to be (deemed) Dutch residents for tax purposes.<sup>9</sup> Nevertheless, in accordance with the aforementioned main objective, when negotiating a treaty, the Netherlands is willing to agree on an exclusion of tax-exempt entities from treaty benefits.

For illustration purposes, in the 2009 protocol amending the Mexico-Netherlands treaty and its 1993 protocol,<sup>10</sup> a new article was introduced stating that the treaty is inapplicable to corporations and other legal persons that are totally or partially exempted from taxes by a special regime or by administrative practice of one of the countries. For this purpose, the special regime should be decided by means of mutual agreement of the tax authorities of both countries.<sup>11</sup>

A less far-reaching provision has been included in the protocol to the Netherlands-Panama treaty concluded in 2011. This protocol states that the competent authorities will decide by means of mutual agreement to what extent a resident of one of the contracting states that is subject to a special regime will not be entitled to the benefits of the treaty.<sup>12</sup> This position provides for a mutual agreement procedure to decide which residents subject to a special regime should be included in the treaty instead of first providing a negative list, as is the case for the treaty with Mexico. It

<sup>9</sup>Following the judgment of the Dutch Supreme Court of Dec. 4, 2009 (HR nr.08/05071, V-N 2009/63.17). In this judgment, the Dutch Supreme Court stated that only the tax-exempt entities that are explicitly mentioned as residents for tax treaty purposes in the treaty are the ones that meet the liability to tax criterion of article 4 of the OECD model. Conversely, the tax-exempt entities not mentioned in the underlying treaty are therefore disregarded as resident for tax purposes.

<sup>10</sup>This 2009 protocol amending the Mexico-Netherlands treaty was signed on December 11, 2008, and it is in force as of December 31, 2009. This 2009 protocol replaces the 1993 protocol.

<sup>11</sup>Article 9 of the 2009 protocol to the Mexico-Netherlands treaty.

<sup>12</sup>Ad 1 protocol modifying article 1 of the Netherlands-Panama treaty.

could reasonably be expected that this provision will also be used in future treaties concluded by the Netherlands.

Further, the Netherlands follows the tiebreaker rule of the OECD model to determine residence in case of dual residency of qualifying persons. For individuals, residence is determined by the following criteria: permanent home, habitual abode, nationality, or by means of mutual agreement (article 4.2). Those criteria are to be applied in hierarchical order. For corporations and other legal persons, the decisive criterion is the place of effective management (article 4.3).

More specifically, the 2009 protocol amending the Mexico-Netherlands treaty states that if the corporation or legal person has a dual residence, residence will be determined by means of mutual agreement between the tax authorities of both countries, taking into account the place of effective management, place of incorporation, or any other relevant criteria.<sup>13</sup> However, if no agreement can be reached, then the tax treaty benefits will be inapplicable to this corporation or legal person. There is, nevertheless, a possibility of obtaining the treaty benefits by means of the application of the Mexico-Netherlands treaty articles regarding nondiscrimination (article 23) or mutual agreement (article 24).

## B. Permanent Establishment

The Netherlands follows the definition of PE according to article 5(1) and article 5(2) of the OECD model. The definition does not include activities of a preparatory and auxiliary character, which is in accordance with article 5(4) of the OECD model.

Further, in the 2011 TTP, the Netherlands states that it does not prefer an expansion of the PE concept but that expansion could nevertheless be accepted by the Netherlands if it is part of the tax treaty policy of the other country.<sup>14</sup>

The first issue in which the Netherlands may deviate from the OECD model definition and approach of PE is regarding article 5(3) of the OECD model. The Netherlands in the 2011 TTP recognizes differences in the approach toward PE both from the U.N. and from the OECD regarding a building site, a construction assembly or installation project, or related supervisory activities that are being carried out in the source country. For the U.N. model, those activities are considered a PE if performed for a period longer than six months (article 5(3)a of the U.N. model), whereas in the OECD model (article 5(3)) that period is 12 months.

The Netherlands states that for developing countries, in principle it is willing to follow the approach of the U.N. model (that is, six months) if that criterion has

<sup>13</sup>Ad 3 protocol replacing article 4(3) of the Mexico-Netherlands treaty.

<sup>14</sup>2011 TTP (*Notitie Fiscaal Vedragsbeleid* 2011), at 40.

been established as part of the international treaty policy of the developing country. However, this approach may be changed if the total outcome of the treaty negotiations is unacceptable for the Netherlands. The decisive criteria regarding what is acceptable in this respect are not further explained in the 2011 TTP. Therefore, the Netherlands always will unilaterally decide what is acceptable and for which developing countries the period of six months will be followed.

The 2011 TTP states that in order to accept the six months, the Netherlands may require additional conditions regarding the calculation of the attribution of profits to PEs.<sup>15</sup> It is unclear from the text of the 2011 TTP what additional conditions must be fulfilled. Also, Dutch treaties concluded previously that contain a six-month period have not introduced any additional conditions. Generally, the Netherlands has accepted this term of six months in its treaties with Latin American countries (for example, in the treaties with Argentina, Brazil, Mexico, and Panama, although with another criterion (which is that the activities should be performed for more than 183 days in a 12-month period)). However, in the treaty with Venezuela, a 12-month period has been included.

The second issue in which the Netherlands may deviate from the definition and approach of PE in the OECD model is regarding article 5(6) of the OECD model. In principle, the Netherlands follows the introduction of independent personal services in the concept of PE. For instance, in the treaty with Panama, independent personal services are included in the PE article (article 5(7)). However, in the treaty with Mexico,<sup>16</sup> the Netherlands has deviated from the OECD model and has accepted the use of article 14 of the U.N. model for independent personal services. The objective of article 14 of the U.N. model is to remove the limitation imposed on the source state to only tax income from independent personal services if the income is derived from a fixed base.

### C. Dividends

Regarding substantial participations (5 percent or more for Dutch standards) the Netherlands' goal is for exclusive taxation in the country of residence of the recipient of the dividends. The main reason for this approach is the application of capital import neutrality to active foreign investments. The Netherlands applies the participation exemption under which dividends received from qualifying shareholdings (that is, in general shareholdings of at least 5 percent not held as portfolio investments) are exempt at the level of the corporate shareholder. If the source country levies a dividend (withholding) tax, this will result in an additional tax

burden for the recipient of the dividends since any foreign withholding tax cannot be credited against Dutch corporate income tax. Therefore, in order to improve the competitive position of Dutch resident companies, the Netherlands hopes to reduce those withholding taxes as much as possible under tax treaties.

The Netherlands follows this approach regardless of:

- the source country being a developing or a developed country; or
- the withholding tax percentages for substantial participations in the OECD model or the U.N. model.

Unlike the discussion above on PEs, the Netherlands does not address in its tax treaty policy the differences between the U.N. and the OECD models.

However, with Latin American countries, dividend withholding tax has been agreed as follows:

- *with Argentina*: 10 percent if substantial shareholding (more than 25 percent) and 15 percent for portfolio investments;
- *with Brazil*: 15 percent for all investments;
- *with Mexico*: 5 percent if substantial shareholding (more than 10 percent) and 15 percent for portfolio investments;
- *with Panama*: 0 percent if substantial shareholding (more than 15 percent) and 15 percent for portfolio investments; and
- *with Venezuela*: 0 percent if substantial shareholding (more than 25 percent) and 10 percent for portfolio investments.

The following paragraphs address the international tax treaty policy in the Netherlands regarding interest and royalties.

### D. Interest and Royalties

Similar to dividends, the Netherlands seeks in its treaties to agree on exclusive taxation of interest and royalties by the country of residence. No reference to the approach of the U.N. model has been made in the 2011 TTP.<sup>17</sup>

However, the approach in the treaties concluded by the Netherlands with Latin American countries may vary regarding the percentages of the interest and royalty withholding tax depending on the type of interest or royalty income. Those percentages are provided below:

- *with Argentina*: interest 12 percent and royalty 3 percent, 5 percent, 10 percent, and 15 percent (depending on the type of royalty);

<sup>15</sup>*Id.*

<sup>16</sup>This approach was left unchanged despite the introduction of the 2009 protocol.

<sup>17</sup>The U.N. approach is in favor of source taxation on interest and royalties. The OECD model provides for source taxation only on interest and exclusive residence taxation on royalties.

- *with Brazil*: interest 10 percent (loans more than 7 years) and 15 percent in other cases, and royalty 25 percent and 15 percent;
- *with Mexico*: interest 5 percent and 10 percent, and royalty 10 percent;
- *with Panama*: interest 5 percent and royalty 5 percent; and
- *with Venezuela*: interest 5 percent and royalty 5 percent, 7 percent, and 10 percent.

### 1. Interest

The Netherlands has negotiated in its treaties with Latin American countries reduced rates and exemptions that differ among treaties. For interest income, the treaty with Argentina introduces a 12 percent withholding tax at source with specific exemptions; the treaty with Brazil introduces a 10 percent or a 15 percent rate and specific exemptions; the treaty with Mexico and the 2009 protocol introduce a 5 percent or 10 percent rate<sup>18</sup>; and the treaties with Panama and with Venezuela introduce a 5 percent rate with specific exemptions.

For illustration purposes, the reduced rate of 5 percent (treaty with Mexico and 2009 protocol) or an exemption (treaties with Brazil, Argentina, Panama, and Venezuela) applies to interest paid to a bank of a contracting state, any of its political subdivision or local entities, and the interest paid to other entities or bodies (including financial institutions) as a result of financing provided by those institutions. The treaty with Panama also exempts the interest paid regarding the sale on credit of merchandise or equipment to an enterprise of a contracting state. Further, the treaty with Brazil provides a 10 percent reduced rate for the interest paid for loans with a term of more than seven years, whereas the treaty with Argentina exempts from withholding tax the interest paid for loans with a term of more than three years.

### 2. Royalties

Regarding royalty income, the withholding tax percentage may vary among treaties depending on the type of royalty. For instance, the treaty with Argentina introduces several percentages of royalty withholding tax (that is, 3 percent, 5 percent, and 10 percent) for specific types of royalty income, and 15 percent in other cases. The treaty with Venezuela also introduces several percentages (5 percent, 7 percent, and 10 percent) and in other cases, the law of the source state may determine the percentage. The treaty with Brazil introduces 25 percent (for example, trademark) or 15 percent withholding tax in other cases. Other treaties introduce a single withholding tax rate for all royalty income, such as the treaty with Mexico (that is, 10 per-

cent, amended by the 2009 protocol<sup>19</sup>) and the treaty with Panama (that is, 5 percent).

## E. Capital Gains

The Netherlands has the goal in its treaties of agreeing on exclusive taxation of capital gains by the country of residence in situations that are not explicitly excluded in article 13 of the OECD model. According to article 13, the source country may only tax capital gains from the alienation of immovable property situated in the source state (article 13(1)), gains from the movable property forming part of the business property of a PE of an enterprise (article 13(2)), gains from the alienation of a ship/aircraft (article 13(3)), and gains from the alienation of shares deriving more than 50 percent of their value directly or indirectly from the immovable property situated in the source state (article 13(4)). In other cases, the country of residence will have the exclusive right to tax capital gains (article 13(5)).

The Netherlands follows to a great extent article 13 of the OECD model, but regarding article 13(4) its goal is to introduce two deviations. The first one is a higher percentage than 50 percent; more specifically a percentage between 70 and 90 percent has been introduced in treaties concluded by the Netherlands.<sup>20</sup> The second change is to limit taxation at source state of capital gains obtained from shares from listed companies, small participations, business immovable assets, participations held by pension funds, and gains obtained as a result of reorganizations within a group of enterprises.<sup>21</sup>

For instance, article 13(6) of the treaty with Panama states that gains from the alienation of shares deriving more than 90 percent of their value from immovable property are taxed in the source country. However, those gains will be taxed in the residence country only when:

- the resident owned less than 10 percent of the shares or other comparable interests before the first alienation;
- the gain is derived in the course of a corporate reorganization, amalgamation, division, or similar transaction; or
- the resident is a pension fund that is recognized and controlled according to the statutory provisions of a contracting state, provided that the gain is not derived from the carrying on of a business, directly or indirectly, by that pension fund.

<sup>18</sup>The prior percentage was 15 percent, and now it is 5 percent for loans from bank institutions and 10 percent in other cases.

<sup>19</sup>Before the 2009 protocol, the treaty with Mexico had a withholding tax rate of 15 percent for royalty income.

<sup>20</sup>2011 TTP (*Notitie Fiscaal Vedragsbeleid* 2011), at n.47.

<sup>21</sup>*Id.* at 49.

No other changes have been implemented in the treaties concluded by the Netherlands with Argentina, Brazil, Mexico, or Venezuela.

Also, the Netherlands strives for exclusive taxation in the country of residence of the seller regarding gains realized on the alienation of shares (other than shares of article 13(4) in a company, or of securities, bonds, debentures, and the like). The main reason is that the Netherlands' policy is to avoid economic double taxation on those gains as long as they qualify under the Dutch participation exemption (*deelnemingswinsten*).

Nevertheless, in some situations the Netherlands has agreed to source taxation on the capital gain derived from the alienation of shares, for instance, if the source country deems this to be consistent with its wish to apply a withholding tax on dividends.<sup>22</sup> With Latin American countries, the Netherlands has agreed on that with Argentina and Mexico.

For instance, with Mexico the provision states that gains from the alienation of shares on a participation of more than 25 percent will be subject to taxation by the source country; however, the tax to be charged is limited to a rate of 10 percent.<sup>23</sup> This article does not apply if the gains are obtained as a result of reorganization, merger, splitting, or any other similar operation.<sup>24</sup> The treaty between the Netherlands and Argentina introduces two percentages for a tax at source — 10 percent if there is a substantial (that is, 25 percent) shareholding participation, or 15 percent in any other cases (article 14(5) of the treaty with Argentina).

## F. Most Favored Nation Treatment Clause

In the 2011 TTP, the Netherlands reaffirms the EU approach that treaties are the result of negotiations between two parties and therefore the Netherlands is unwilling to agree on a most favored nation treatment clause that can be applied to other (third) parties than the treaty contracting parties. Further, the Netherlands argues that the introduction of a most favored nation treatment clause may result in the countries being reduced in their margin (scope) for negotiation.

For countries outside the European Union, the same argument is being followed, and therefore the Netherlands states its reluctance to agree on most favored nation treatment clauses in its treaties. The Netherlands currently has not introduced those types of clauses in the treaties concluded with Latin American countries.

## G. Treaty Antiabuse Clauses

### 1. Antiabuse Clauses

The Netherlands Supreme Court has a reserved approach to domestic antiabuse clauses, such as *fraus legis*,

*gis*,<sup>25</sup> to prevent treaty abuse. As a consequence, the Netherlands is willing to include antiabuse provisions in treaty negotiations and is willing to agree on reasonable antiabuse provisions if there is a real risk of treaty abuse given the interaction between the relevant tax systems.<sup>26</sup>

Further, the Netherlands commits to agree on reasonable antiabuse provisions following treaty negotiations and upon request of the treaty partner.

The first type of treaty antiabuse clause is the beneficial ownership provision that is designed to prevent abuse by means of treaty shopping. The treaties concluded with Argentina, Brazil, Mexico, Panama, and Venezuela have introduced the concept of beneficial ownership for dividends, interest, and royalties.

The second type of treaty antiabuse clause is the limitation on benefits provision that is directed toward the activities of the person entitled to the element of income. This clause is generally found in the treaties concluded by the Netherlands, for instance in its treaty with the United States. The third type of treaty antiabuse clause is the main purpose test applicable to transactions carried out with the goal of obtaining a treaty benefit unintended by the parties when concluding the treaty. The main purpose test is, for instance, found in the treaty with Qatar (protocol).<sup>27</sup> Those clauses have not yet been found in the treaties with Latin American countries.

Finally, with the goal of safeguarding legal certainty, the Netherlands applies a reserved approach. The approach is to apply the LOB and the main purpose test

<sup>25</sup>The antiavoidance doctrine of fraud of law (*fraus legis*) has been introduced by the judiciary in the Netherlands. By means of this doctrine, the taxpayer can carry out transactions targeting tax benefits but the taxpayer's focus should not be only those tax benefits. This doctrine is used as *ultimum remedium* that "can only be considered after interpretation and characterisation according to the normal interpretation methods have been fully utilized without this leading to an outcome that can be regarded as consistent with the purpose and intent of the law." R.L. Yzerman, "Report for the Netherlands, Form, and Substance in Tax Law," *Cahiers de droit Fiscal Int'l*, International Fiscal Association, vol. 87a, SDU Uitgevers, the Netherlands, 2002, at 452 and 455.

<sup>26</sup>2011 TTP (*Notitie Fiscaal Vedragsbeleid* 2011) at 48.

<sup>27</sup>According to the Dutch reporters to the IFA Congress 2010, the purpose of the main substance test is "that treaty benefits are not granted if the relevant structure is set up with the sole or predominant reason of gaining the treaty benefits. Most of those provisions are found in the articles concerning dividends, interest and royalties, but main purpose tests are also used to counter mala fide emigration of corporations" (see Protocol III to article 4(4) of the Netherlands-Qatar 2008 treaty and article 34(2) of the tax arrangement for the Kingdom of the Netherlands). F. Peters and A. Roelofsen, the Netherlands, "Tax Treaties and Tax Avoidance: Application of Anti-Avoidance Provisions," *Cahiers de droit Fiscal Int'l*, IFA, vol. 95A, IBFD, 2010, at 573.

<sup>22</sup>*Id.* at 48.

<sup>23</sup>Ad 6 protocol modifying article 13(4) of the Mexico-Netherlands treaty.

<sup>24</sup>See article 13(4) of the Mexico-Netherlands treaty in conjunction with 2009 protocol Ad. 15.

not as general clauses but as specific clauses, for instance by specifically mentioning the type of transaction to which each can be applicable.<sup>28</sup>

## 2. Antiabuse Clause

In the recent treaty between the Netherlands and Panama<sup>29</sup> a new article has been included (article 27) that provides for the contracting parties to apply any domestic law and measure to prevent, discourage, avoid, or counteract the effect of any transaction, arrangement, or practice that results in improper use of the treaty. Article 27 also states that “the contracting states shall designate by mutual agreement the domestic law and measures concerned.”<sup>30</sup>

This clause follows, to some extent, the clause introduced in the tax agreement with Hong Kong.<sup>31</sup> The result could be that the contracting parties, and in this case the Netherlands, may introduce new domestic measures to counteract the effect of the improper use of the treaty, which can also result in treaty override.<sup>32</sup>

<sup>28</sup>2011 TTP (*Notitie Fiscaal Vedragsbeleid* 2011), at 70 and 71.

<sup>29</sup>Signed October 2010 and in force as of December 1, 2012.

<sup>30</sup>Article 27 of the Netherlands-Panama treaty states:

Nothing in this Convention shall prejudice the right of each Contracting Party to apply any of its domestic laws and measures for preventing, discouraging, avoiding or counteracting the effect of any transaction, arrangement, or practice that has the purpose or effect of improperly conferring a tax benefit to any person. The Contracting States shall designate by mutual agreement the domestic laws and measures concerned.

<sup>31</sup>Article 27 of the Hong Kong-Netherlands treaty also includes that clause, although it is a little more extensive than the one in the treaty with Panama and states that:

1. Nothing in this Agreement shall prejudice the right of each Contracting Party to apply its domestic laws and measures concerning tax avoidance, whether or not described as such.
2. For the purposes of this Article, “laws and measures concerning tax avoidance” includes laws and measures for preventing, discouraging, avoiding, or counteracting the effect of any transaction, arrangement, or practice that has the purpose or effect of conferring a tax benefit on any person.
3. For the purposes of this Article, “laws and measures concerning tax avoidance” includes for the Netherlands in any case: Article 17, paragraph 3, subparagraph b, in connection with article 17a, paragraph 1, subparagraph c, of the Corporate Income Tax Act 1969, or any identical or substantially similar provisions replacing these Articles.

Article 27 of the Hong Kong-Netherlands treaty, signed March 2010 and in force as of October 24, 2011.

<sup>32</sup>By means of treaty override, a tax treaty concluded by the country has equal force as domestic law and thus the most recent prevails. The result is that a conflict between a bilateral tax convention and a domestic law is solved by applying the provision introduced later in time. In other words, for a tax issue if domestic law is later in time, the bilateral tax convention is no longer applicable.

## H. Interpretation of Treaty and Arbitration

The Netherlands in general follows a dynamic interpretation of the tax treaty articles following the developments in the OECD commentary. This may give rise to problems for the application of treaties with countries that follow a static approach. In order to solve the differences between those approaches, the Netherlands stated in its 2011 TTP to agree during treaty negotiations on the application of the recent or future changes in the OECD model and OECD commentary and the application of those changes to the current treaties. Alternatively, a general clause (*kapstok bepaling*) can be agreed on that delegates simple implementation of new provisions or interpretation methods by mutual agreement between the competent authorities.<sup>33</sup>

Also, the Netherlands tries to introduce the wording of article 25(5) of the OECD model in its treaties.<sup>34</sup> This article provides for a mutual agreement procedure, and in case this agreement is not successful within two years, it provides for (binding) arbitration upon request of the taxpayer. The possibility to request arbitration by a taxpayer changes the policy of the Netherlands before the 1990s (in the past a request for arbitration could be made only by the competent authorities). Finally, in case the outcome of an arbitration procedure deviates from a prior judgment in the treaty partner’s country, and its legal system, like the Netherlands’, provides for such a deviation, then the limitation to only submit unresolved issues to arbitration can be removed from the text of the treaty that will be concluded.<sup>35</sup>

The treaty with Panama does not include a clause similar to article 25(5) of the OECD model mentioned above, but it does state in article 23(5) the following:

<sup>33</sup>2011 TTP (*Notitie Fiscaal Vedragsbeleid* 2011), at 24-25.

<sup>34</sup>Article 25(5) paragraph 5 of the OECD model states:

Where, a) under paragraph 1, a person has presented a case to the competent authority of a Contracting State on the basis that the actions of one or both of the Contracting States have resulted for that person in taxation not in accordance with the provisions of this Convention, and b) the competent authorities are unable to reach an agreement to resolve that case pursuant to paragraph 2 within two years from the presentation of the case to the competent authority of the other Contracting State, any unresolved issues arising from the case shall be submitted to arbitration if the person so requests. These unresolved issues shall not, however, be submitted to arbitration if a decision on these issues has already been rendered by a court or administrative tribunal of either State. Unless a person directly affected by the case does not accept the mutual agreement that implements the arbitration decision, that decision shall be binding on both Contracting States and shall be implemented notwithstanding any time limits in the domestic laws of these States. The competent authorities of the Contracting States shall by mutual agreement settle the mode of application of this paragraph.

<sup>35</sup>2011 TPP (*Notitie Fiscaal Vedragsbeleid* 2011), at 66.

the competent authorities may also agree on other forms of resolution when a mutual agreement can not be reached.

Thus, one may argue that on the basis of this article 23(5), it should be possible to make use of alternative dispute resolution methods such as binding arbitration if the mutual agreement is unsuccessful.<sup>36</sup>

#### IV. Summary and Recommendations

The Netherlands no longer makes use of the Dutch model tax treaty but instead follows the OECD model. Regarding Latin American countries, the Netherlands in principle is willing to follow the U.N. model provisions for the minimum period during which specific activities should be carried out in order to constitute a PE (that is, a period longer than six months instead of the regular 12 months). For dividends, interest, and royalties, the Netherlands in principle follows the OECD model. Consequently, the Netherlands has a goal of a 0 percent dividend withholding tax rate for non-portfolio substantial shareholdings and no tax at source on interest and royalty payments.

The 2011 TTP contains open concepts that allow for changes in the relationship of the Netherlands with other countries when negotiating treaties. For instance, in the case of the attribution of profits to PEs, the 2011 TTP states that further conditions may be required by the Netherlands, but it does not address the content of those possible conditions.

<sup>36</sup>This was also stated in the explanatory memorandum to the treaty with Panama. *Memorie van Toelichting 8 september 2011: 32 907. Verdrag tussen het Koninkrijk der Nederlanden en de Republiek Panama tot het vermijden van dubbele belasting en het voorkomen van het ontgaan van belasting met betrekking tot belastingen naar het inkomen, met Protocol; 's-Gravenhage, 6 oktober 2010.*

Also, the inclusion of antiabuse provisions in the treaty in principle is limited to reasonable antiabuse provisions, which has the goal of providing for legal certainty. Therefore, the Netherlands is reserved in agreeing on provisions such as a LOB clause or a main purpose test in treaties based on the nondefined criterion of reasonable provisions. It does not explain what is meant by the term “reasonable,” and there are no examples of situations on which those provisions can be agreed.

The MOF during the Parliamentary discussions on the 2011 TTP stated that technical notes regarding the 2011 TTP are unnecessary given that the Parliamentary documents, the previous tax treaty policy memorandums, and the explanatory note to the treaties should be sufficient to clarify international tax issues not completely specified in the 2011 TTP.<sup>37</sup>

Even with the above, I believe that the policy adopted in the 2011 TTP is theoretical and it leaves too much room for interpretation of the Netherlands’ objectives in its tax treaty policy. Taking into account that the Dutch model treaty is no longer applicable, the 2011 TTP is the only guidance to determine the policy of the Netherlands regarding other countries for negotiating new treaties. In order to better understand the Netherlands’ policy for foreign new treaty partners, it is recommended to provide a full English translation of the 2011 TTP document as well as an overview of examples from current, in-force treaties or current international tax practices in which additional justifications or “reasonable” antiabuse provisions have been included. ◆

<sup>37</sup>*Kamerstukken II 25087, 2010-2011, Annex I, June 24, 2011, at 2.*