Dutch Court Case on the Transfer Pricing Aspects of Business Restructurings

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This court case concerns a Dutch taxpayer (part of a multinational enterprise group) that is engaged in the exploitation of a zinc smelter. The case underlines that transfer pricing is dependent on facts and the taxpayer's actual conduct as reflected in documentation, annual accounts, tax returns, other documents and communication with the tax authorities.

In this case, a worldwide restructuring of a multinational enterprise ("**MNE**") group on 1 July 2010 led to a transfer of part of the business of a Dutch group entity to a Swiss group entity. Due to the business restructuring, the Dutch entity received a conversion fee of EUR 28,351,364 based on the remaining duration of the contract of one year. Moreover, the MNE group agreed on a cost-plus remuneration based on the Transactional Net Margin Method for the post-restructuring activities performed by the Dutch entity. The remuneration has been based on the argumentation that the Dutch entity should be considered as a toll manufacturer performing routine activities after the core activities had been transferred to the Swiss entity. The Dutch tax authorities disagreed on the above considerations and calculated an exit charge of EUR 184,627,000. The Dutch tax authorities believed that the Dutch entity was still performing core activities and therefore could not be regarded as a toll manufacturer. As a result, the Dutch tax authorities also did not agree with the cost-plus 10% remuneration for the post-restructuring activities performed by the Dutch entity.

The main dispute at issue is whether the received compensation payment of EUR 28,351,364 is at arm's length. Another dispute regards whether the cost-plus remuneration is an arm's length remuneration for the post-restructuring activities of the taxpayer (after 1 July 2010).

The Dutch taxpayer won the case in the lower court of Zeeland-West-Brabant ("**Lower Court**"),[1] which decided that the Dutch taxpayer can be considered as a toll manufacturer performing routine activities after the restructuring on 1 July 2010. Therefore, the cost-plus remuneration was an appropriate remuneration for the activities performed by the Dutch entity. In addition, the Lower Court decided that the conversion fee was at arm's length because the Dutch entity started transferring core activities to other affiliated entities already in the years prior to 2010 so that there is no reason anymore to consider this in 2010 in determining the conversion fee. The Dutch tax authorities disagreed and appealed against the Lower Court's decision.

During a hearing before the court of 's-Hertogenbosch ("**Appeals Court**") ,[2] the Appeals Court provisionally considered that the Dutch taxpayer should be held to its own conduct until June 2010, which means that the Dutch taxpayer is an entrepreneur and profit beneficiary until and including June 2010. This implies that what has been transferred as of 1 July 2010 by the Dutch taxpayer to a Swiss group entity can be attributed a value and that the functions of the Dutch taxpayer after 1 July 2010 exceed that of a limited risk toll manufacturer. After the Appeals Court hearing, the Dutch taxpayer and the Dutch tax authorities reached a compromise. The decision of the Appeals Court was based on what was agreed between the Dutch taxpayer and the Dutch tax authorities. The key points of the compromise include :

- Firstly, the remaining activities performed by the Dutch entity are regarded to constitute more than pure toll manufacturing activities. The most appropriate transfer pricing

[1] Court of Zeeland-West-Brabant, BRE 15/5683, data of ruling: 19 September 2017, date of publication: 27 October 2017.
[2] Court of 's-Hertogenbosch, 17/00714, Date of ruling: 13 March 2020, date of publication: 16 April 2020.

method to remunerate the remaining activities of the Dutch entity after the restructuring is the profit split method instead of the cost-plus method. Under the agreed application of the profit split method, the Dutch taxpayer is entitled to 72% of the total profits obtained through the joint smelting activities of the Dutch taxpayer and the related party.

- Secondly, based on the profit split remuneration of 72%, 28% of the total enterprise value prior to the transfer on 1 July 2010 should be considered by the Dutch taxpayer as conversion payment for the transferred part of its business.
  Based on the above, the profit split remuneration of the Dutch taxpayer for the period 1 July 2010 – year-end 2010 and the conversion payment lead to a taxable amount of EUR 121,973,435 for 2010 rather than the taxpayer's position of EUR 42,7641,089 or the taxable amount of EUR 188, 342,906 initially argued by the Dutch tax authorities.

The State Secretary for Finance felt the need to explain the Appeals Court ruling in a separate note on 30 April 2020. The State Secretary for Finance regards it of importance for the Appeals Court to point out that the taxpayer should be held to its own conduct until and including June 2010, which means that the taxpayer is an entrepreneur and profit beneficiary until and including June 2010. He stresses that if, for example, in its own transfer pricing documentation, annual accounts and tax returns, a taxpayer has always presented itself as a residual profit-making beneficiary, it cannot successfully assert later in time that there has been no de facto entitlement to the residual profit, since core functions would have been transferred gradually in previous years. In addition, the State Secretary for Finance highlights the importance of a compensation payment reflecting the value of the transferred functions and risks and the associated profit generating capacity. Finally, the State Secretary for Finance emphasizes that when there is a partial transfer of functions and risks, the remaining entity could still be entitled to a part of the residual profits.

This case shows the importance of considering the transfer pricing aspects of business restructurings taking into account the correct facts and circumstances.