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# Transfer Pricing and Customs Valuation

## Netherlands

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### Latest Information

This chapter is based on information up to 30 June 2022. Please find below the main changes made to this chapter up to that date:

[A unilateral upward or downward adjustment is required to be in line with arm's length principle.](#)

## 1. Interaction between Transfer Pricing and Customs Valuation

### 1.1. National customs valuation

Within the framework of the World Trade Organization (WTO) and the World Customs Organization (WCO), signatory parties to these organizations – including individual EU Member States and the European Union (EU) on its own account – have signed binding treaties with respect to the customs valuation of imported goods, including the [WTO Customs Valuation Agreement](#).<sup>[1]</sup>

The customs valuation principles set out in the WTO Customs Valuation Agreement are incorporated directly into the EU customs legislation by means of three regulations.<sup>[2]</sup> The customs value of imported products is determined according to rules established at EU level, that is to say:

- the [Union Customs Code \(UCC, Regulation \(EU\) No. 952/2013 of the European Parliament and of the Council\)](#);<sup>[3]</sup>

1. Formally known as the Agreement on Implementation of Article VII of the General Agreement on Tariffs and Trade 1994 (GATT). The WTO Customs Valuation Agreement (WTO CVA) replaced the GATT Valuation Code as a result of the Uruguay Round multilateral trade negotiations which created the WTO in 1994.
2. The [Union Customs Code](#) (UCC) has been structured in accordance with the [Treaty of Lisbon](#), which means that it consists of a basic, a delegated and an implemented regulation. The UCC legal package also includes the Transitional Delegated Act, which, however, is less relevant for determining the customs value of imported goods as it only lays down transitional rules for the customs value particularities in the customs declaration. On 1 December 2009, the [Treaty of Lisbon](#) entered into force, 2 years after its signature by the Member States. The [Treaty of Lisbon](#) (signed on 13 Dec. 2007) entered into force on 1 Dec. 2009. Also known as the Reform Treaty, it amends the Treaty on European Union (Maastricht 1992) and the Treaty Establishing the European Community (Rome 1957). The Treaty of Rome has been renamed the [Treaty on the Functioning of the European Union](#).
3. Regulation (EU) No. 952/2013 of the European Parliament and of the Council of 9 October 2013 laying down the [Union Customs Code](#), OJ L 269 (2013). See arts. 69-76 for the customs valuation provisions.

- its Delegated Act ([UCC DA, Commission Delegated Regulation No. 2015/2446](#));<sup>[4]</sup> and
- its Implementing Act ([UCC IA, Commission Implementing Regulation No. 2015/2447](#));<sup>[5]</sup>

These regulations have direct effect in all Member States, including the Netherlands, and are jointly referred to as the UCC legal package. These regulations became applicable from 1 May 2016.<sup>[6]</sup> Before 1 May 2016, the [Community Customs Code \(CCC\)](#)<sup>[7]</sup> and the CCC Implementing Provisions (CCIP)<sup>[8]</sup> applied.

The Netherlands has its own national customs legislation,<sup>[9]</sup> which is designed to complement EU customs law in order to ensure its correct application. The national legislation provides further details on local customs administration, including the filing and verification of customs declarations, administrative requirements and collection of customs debts. The Dutch national customs legislation does not deviate from the main customs valuation principles laid down in the UCC and the UCC IA.

### European and Dutch soft law and specific circulars

In addition to European and Dutch national customs legislation, there are three further authoritative sources used for establishing and interpreting the customs valuation of goods imported into the Netherlands. These are:

- (a) national and Court of Justice of the European Union (ECJ) case law;
- (b) Compendium of Customs Valuation texts ([EU Customs Valuation Compendium](#)); and
- (c) national interpretative and policy directives – the “Customs Handbook”.

#### Ad (a): National and ECJ case law

Rulings from the Dutch lower courts and the Supreme Court, as well as judgments from the ECJ, on customs valuation issues are applied both by the customs authorities and businesses to interpret and apply EU customs valuation legislation.

#### Ad (b): EU Customs Valuation Compendium

The Customs Expert Group, Valuation Section (CEG VAL), addresses customs valuation issues at an EU level. From time to time, the CEG VAL issues non-binding instruments (i.e. Commentaries and Conclusions) on its interpretation of the UCC legal package. The instruments are intended to ensure a common understanding for both customs authorities and economic operators and provide a tool to facilitate the correct and harmonized application by the EU Member States. The provisions of customs legislation take precedence over the contents of the instruments of the CEG VAL. Even though the instruments are not binding, they clarify the European Commission’s view on how the customs valuation provisions should be applied. However, the authorities of the Member States may interpret or use the instruments in different ways. Furthermore, the instruments may be amended from time to time.

The instruments have been published in the [Customs Valuation Compendium](#) the latest edition of which was released in July 2022.<sup>[10]</sup> The first edition of the Customs Valuation Compendium had been prepared at the time the CCC and CCIP were in force by the EU Customs Code Committee, Valuation Section (the predecessor of the CEG VAL). Since 2018, the Compendium refers solely to UCC provisions. The current edition<sup>[11]</sup> contains a summary of the UCC provisions on and relevant to customs valuation matters, the aforementioned non-binding instruments, a summary of ECJ judgments on customs valuation, the interpretative notes on the WTO CVA provisions and an index of texts of the Technical Committee on Customs Valuation of the WCO. Contrary to the

4. Commission Delegated Regulation (EU) 2015/2446 of 28 July 2015 supplementing Regulation (EU) No. 952/2013 of the European Parliament and of the Council as regards detailed rules concerning certain provisions of the [Union Customs Code](#), OJ L 343 (2015). See art. 71 for the customs valuation provisions.
5. Commission Implementing Regulation (EU) 2015/2447 of 24 November 2015 laying down detailed rules for implementing certain provisions of Regulation (EU) No 952/2013 of the European Parliament and of the Council laying down the [Union Customs Code](#), OJ L 343 (2015). See arts. 127-146 and art. 347 for the customs valuation provisions.
6. Some articles of the UCC became applicable from 30 Oct. 2013, i.e. the articles that confer implementing powers on the Commission (i.e. these articles gave the Commission power to make specific rules which are included in the UCC DA and the UCC IA). However, all substantive provisions became applicable as of 1 May 2016.
7. Council Regulation No 2913/92 of 12 October 1992 establishing the [Community Customs Code](#), OJ L 302 (1992). The customs valuation rules were covered by arts. 28-36.
8. Commission Regulation No 2454/93 of 2 July 1993 laying down provisions for the implementation of Council Regulation (EEC) No 2913/92 establishing the [Community Customs Code](#), OJ L 253 (1993). The customs valuation rules were covered by arts. 141-181a and Annexes 23-29.
9. The national customs legislation consists of the *Douanewet* (Law of 3 Apr. 2008, Staatsblad 111), and the decrees based on this Law, i.e. *Douanebesluit* (Decree of 5 July 2008, Staatsblad 288) and *Douaneregeling* (Decree of 14 July 2008, Staatscourant 145).
10. Most recent update of the Customs Valuation Compendium 2022, available at [https://taxation-customs.ec.europa.eu/document/download/9a13b89e-9e5e-482e-be0b-f593d96bc815\\_en?filename=2022%20EU%20Valuation%20Compendium%20EN.pdf](https://taxation-customs.ec.europa.eu/document/download/9a13b89e-9e5e-482e-be0b-f593d96bc815_en?filename=2022%20EU%20Valuation%20Compendium%20EN.pdf) (accessed 27 July 2022).
11. At the time the substantive provisions of the UCC legal package became applicable on 1 May 2016, the Commission also published another authoritative source, i.e. the Guidance on Customs Valuation, which focused on specific articles of the UCC IA (article 128 on the “last sale for export” rule, and article 136 on dutiability of royalties). Since the release of the latest edition of the Compendium, this Guidance has been incorporated in the Customs Valuation Compendium as Commentary 13.

CCC and CCIP, the interpretative notes on the WTO CVA provisions are laid down in the Compendium instead of the UCC legal package. As a consequence, the interpretative notes are no longer considered legally binding under the UCC.

### Ad (c): Dutch interpretative and policy directives

The Dutch Customs Handbook is a practical guide used by the Dutch customs authorities. The Dutch Customs Handbook provides, amongst other things, instructions and interpretation guidance for the valuation legislation. It also includes decisions and conclusions of the CEG VAL. Although it is not to be regarded as binding customs legislation, it nevertheless clarifies how the customs authorities in the first instance may approach the application and interpretation of customs valuation aspects. It is therefore relevant for customs valuation purposes, though legally not binding.

### Customs valuation methods

The WTO [Customs Valuation Agreement](#) and the UCC (which is directly applicable in the Netherlands) present identical customs valuation methods. These six valuation methods are:<sup>[12]</sup>

- (1) transaction value method;
- (2) transaction value of identical goods;
- (3) transaction value of similar goods;
- (4) deductive value method;
- (5) computed value method; and
- (6) fall-back method.

The six valuation methods must be applied in hierarchical order, with the exception of methods 4 and 5 which can be switched at the request of the importer, but not on the instruction of the customs authorities. In determining the application of one of the valuation methods, the customs authorities are required to consult and consider the views of the importer.

### Transaction value method further defined

Most goods imported into the Netherlands are valued on the basis of the transaction value method. Both the WTO Customs Valuation Agreement<sup>[13]</sup> and the UCC<sup>[14]</sup> define the transaction value as the price actually paid or payable for the goods when sold for export to the country of importation, subject to certain adjustments.<sup>[15]</sup>

The upward adjustments relate to specific elements incurred by the buyer that are not included in the price paid for the imported goods, but which are to be allocated (added) to the goods and thus form a part of the customs value.<sup>[16]</sup> Examples include:

- royalty payments related to the goods being valued which the buyer must pay as a condition of sale;
- assists supplied free of charge or at reduced costs by the buyer for use in connection with the production and sale for export of the imported goods; and
- cost of freight and insurance of the imported goods.

The downward adjustments relate to elements which should not be included in the customs value (deductions), provided that they are shown separately from the price paid or payable.<sup>[17]</sup> Examples include:

- buying commissions;
- transport of products after their arrival at the place of introduction into the EC customs territory; and
- financing costs.

According to the Interpretative Notes on customs valuation to the WTO Customs Valuation Agreement,<sup>[18]</sup> the price actually paid or payable is the total payment made or to be made by the buyer to or for the benefit of the seller for the imported goods. It includes all

<sup>12.</sup> Arts. 70 and 74 UCC (Regulation (EU) No 952/2013 of 9 October 2013).

<sup>13.</sup> Art.1 WTO Customs Valuation Agreement.

<sup>14.</sup> Art. 70(1) UCC (Regulation (EU) No 952/2013 of 9 October 2013).

<sup>15.</sup> Arts. 71-72 UCC (Regulation (EU) No 952/2013 of 9 October 2013), similar to art. 8 WTO Customs Valuation Agreement.

<sup>16.</sup> Art. 71 UCC (Regulation (EU) No 952/2013 of 9 October 2013).

<sup>17.</sup> Art. 72 UCC (Regulation (EU) No 952/2013 of 9 October 2013).

<sup>18.</sup> [Interpretative Note to art. 1 WTO Customs Valuation Agreement](#) (accessed 18 July 2022). This used to be included also in Annex 23 of the CCIP.

payments made as a condition of sale of the imported goods by the buyer to the seller, or by the buyer to a third party, to satisfy an obligation of the seller.

In order to apply the transaction value as the customs value, all of the following conditions must be fulfilled:

- There are no restrictions as to the disposal or use of the goods by the buyer, other than restrictions which:
  - are imposed or required by law in the country of importation;
  - are limited to the geographic area in which the goods may be resold; or
  - do not substantially affect the value of the goods.
- The sale or price must not be subject to conditions or considerations for which a value cannot be determined with respect to the goods being valued.
- No part of the proceeds of any subsequent resale, disposal or use of the goods by the buyer will accrue directly or indirectly to the seller, unless adjustment can be made in accordance with the provisions in articles 71 and 72 of the UCC.<sup>[19]</sup>
- The buyer and seller are not related persons. However, where the buyer and seller are related, the use of the transaction value is still acceptable if the importer demonstrates that:
  - the relationship did not influence the price; or
  - the transaction value closely approximates a test value.

The customs aspects and difficulties surrounding this last element – the relationship between the buyer and the seller – will be addressed in further detail in section 3. Next we address some specific (practical) approaches with respect to applying the transaction value method in the Netherlands.

### Specific approaches when applying the transaction value method

In the past there have been a number of cases where the particular application of the valuation rules in the [Community Customs Code \(CCC\)](#) and Custom Code Implementing Provisions (CCIP) by the customs authorities have resulted in what can be considered a more “developed” approach to customs valuation. The customs authorities have also made public their view on the application of the new EU customs valuation rules.<sup>[20]</sup> These approaches should always be considered when considering the customs value of goods to be imported into the Netherlands. They can be summarized as follows:

- (a) applying the “last sale for export doctrine”;<sup>[21]</sup>
- (b) consignment manufacturing; and
- (c) dutiability of intangibles, in particular royalty payments.

#### Ad (a): Interpretation of sale for export

Under the UCC, the “last sale for export” doctrine applies.<sup>[22]</sup> This means that the transaction value of the goods should be determined on the basis of the sale occurring immediately before the goods were brought into the customs territory of the European Union.<sup>[23]</sup>

In the Netherlands, there has been some discussion on the question of what can be considered a “sale” in this respect.<sup>[24]</sup> Commentary 13 in the Customs Valuation Compendium states that “the basis of the customs value under Art. 70 UCC takes the form of an actual sale, with an actual buyer and seller. In other words, it must be established whether the parties to a transaction can be regarded as buyer and seller and thus whether the transaction constitutes a sale in legal terms as well as in a commercial sense”.<sup>[25]</sup> Commentary 13 also states: “Art. 128 UCC-IA does not introduce changes in the scope of what can be deemed a

19. This is embedded in art. 8 WTO Customs Valuation Agreement.

20. The UCC version of the “Customs Handbook” is available on the website of the Dutch customs authorities, [https://www.belastingdienst.nl/wps/wcm/connect/bldcontentnl/belastingdienst/douane\\_voor\\_bedrijven/naslagwerken\\_en\\_overige\\_informatie/handboeken\\_douane/handboek\\_douane/handboek\\_douane](https://www.belastingdienst.nl/wps/wcm/connect/bldcontentnl/belastingdienst/douane_voor_bedrijven/naslagwerken_en_overige_informatie/handboeken_douane/handboek_douane/handboek_douane) (accessed 10 July 2022).

21. Under the old customs legislation, the “first sale for export rule” applied. This is one of the most important changes in terms of customs valuation of the UCC.

22. Under the CCC, the “first sale of export” applied. Since the introduction of the UCC, this methodology was abolished and a grandfathering clause was applicable until 31 Dec. 2017.

23. Art. 128(1) UCC IA.

24. This question relates to the situation where purchase orders are placed with the importer (or with another party such as the exporter in the exporting country) by the final customer, prior to import of the goods. The question arose whether such a purchase order could be considered as a “sale for export”.

25. See sec. 2.1, point 10 of Commentary 13.

sale of goods for customs valuation purposes. Based on the guidelines, the meaning (and concept) of what constitutes a sale is not altered".<sup>[26]</sup> In Commentary 13, the CEG VAL gives examples of transactions (not an exhaustive list) that do not qualify as a "sale".<sup>[27]</sup> These examples are: import on consignment, goods imported by branches of the same company which are not separate legal entities and goods imported under a hire or leasing contract. In these cases, the transaction value method cannot be applied if no other transaction took place with respect to the goods prior to the entry of the goods in the EU customs territory.

Apart from the question whether a specific transaction qualifies as a "sale", there is also some debate about which sale qualifies as the "last sale for export" in specific transaction chains. One example in this respect is provided below:

Example: Which sale qualifies as the "last sale for export"?

Invoice flow:

- US Manufacturer sells goods to EU established dealer (invoice 1);
- EU Dealer sells to EU Buyer (invoice 2);
- EU Buyer sells to EU Distributor (invoice 3).

Goods flow:

- US Manufacturer delivers the goods directly to the EU Buyer.

Customs formalities:

- EU Buyer acts as importer.

The question is which sale is the "last sale for export" and should function as a basis to determine the customs value of the imported goods.

The initial version of the Guidance on Customs Valuation (which is now incorporated as Commentary 13 of the Compendium Customs Valuation) stated that a domestic sale did not qualify as a sale for export to the European Union. A domestic sale was defined as a sale where the buyer and seller are established in the European Union.<sup>[28]</sup> As a result, invoice 3 was considered a domestic sale (between two EU-established companies) and could not be the last sale for export.

A new version of the Guidance on Customs Valuation was published on 25 September 2020 (it is backdated to 17 September 2020). The "domestic sale" concept had been removed from the Guidance at the time. As a result, a sale between two EU-established entities can be considered the "last sale for export", which should be used as a basis to determine the customs value of the imported goods. As a result, in the above example, the purchase price of the EU Buyer (the importer), i.e. invoice 2, may qualify as the transaction value. However, depending on the facts and circumstances, the *sales price* of the EU Buyer to the EU Distributor (invoice 3) may qualify as the transaction value. This can be the case if that sale has already been concluded before the goods are brought to the European Union (i.e. that sale qualifies as the "sale for export to the EU"). In some cases, even a purchase order placed by an EU customer can qualify as a "sale" and as the "sale for export", even though the invoice is not yet issued to that customer at the moment of import. This is possible if the purchase order is accepted/confirmed by the seller according to Commentary 13.<sup>[29]</sup> The Dutch customs authorities do, however, tend to apply example 5 of Commentary 13 in back-to-back order situations, meaning that the sale to the importer is regarded as the relevant sale for export purposes, even if, in a later chain, an (accepted) purchase order has been raised before the moment of import.

Where importers are uncertain about which sale in the supply chain qualifies as the "last sale for export", the importers can reach out to the Dutch customs authorities to obtain confirmation.

### Ad (b): Transaction value with consignment manufacturing

In more complicated transactions for export, the question arises as to whether transactions relating to toll manufacturing or contract manufacturing can also be considered as the starting point for defining the sale for export to the European Union. The answer to this question has been positive in the Netherlands; nevertheless, these export/import scenarios are carefully examined by the Dutch customs authorities prior to approval.

<sup>26.</sup> See sec. 2.1, point 9 of Commentary 13.

<sup>27.</sup> See sec. 2.1, point 10 of Commentary 13.

<sup>28.</sup> See sec. 2.1, point 9 Guidance on Customs Valuation. Note that the exact text in the former Guidance on Customs Valuation is "buyer and seller in EU".

<sup>29.</sup> See 2.1, point 10 of Commentary 13.



On the basis of Commentary 1 of the Customs Valuation Compendium, it is generally accepted that a processing fee (provided that the costs of raw materials are added to the customs value as an assist) can be used to determine the transaction value for customs valuation purposes. Commentary 1 states:<sup>[30]</sup>

2. Article 70(1)(b) of the UCC is applicable in cases where:

- the customs value of the imported goods is determined under Article 70 of that Regulation even where the contract is only for working or processing of goods, and
- the buyer of the imported goods has supplied certain goods or services (referred to as “assists”) either free of charge or at reduced cost, for use in connection with the production and sale for export of those imported goods.

From the *Christodoulou* case (Case C-116/12) (12 December 2013), it can be derived that the ECJ confirms this interpretation. This interpretation also follows from WCO TCCV Advisory Opinion 1.1, which states: “[T]he WTO [Customs Valuation] Agreement does not contain a definition of ‘sale’, but for reasons of uniformity of interpretation and applicable, it is important that the term ‘sale’ is taken ‘in the widest sense’ so that the customs value of the imported goods can be determined under the transaction value method as often as possible. This means that all transactions that economically and legally qualify as sales should, to the greatest extent possible, be used for customs valuation purposes to make sure that the valuation of the goods reflects as close as possible their actual market value”.

### Ad (c): Dutiability of intangibles (royalties)

The transaction value of the imported goods can include certain elements incurred by the buyer that are not included in the price paid for the imported goods but which are to be allocated to the goods and thus form a part of the customs value.<sup>[31]</sup> Royalties, which payments consist of payments for intangible rights such as patents, trademarks and copyrights, are an example of such a specific element which can be included in the customs value.

The EU implementation of the royalty concept, as laid down in article 71(1)(c) of the UCC,<sup>[32]</sup> requires that, in applying the transaction value method, royalties and licence fees shall be included in the customs value if:

“The royalties are related to the goods being valued”. This means that the royalties must relate to the products imported into the European Union by the buyer.

“The buyer must pay the royalties directly or indirectly as a condition for sale of the goods being valued”. This means that the buyer must pay the royalties, directly or indirectly, to the seller and that this payment is a condition stipulated by the seller to sell the goods to the buyer. So, only if the buyer pays the royalties (in)directly to the seller, is the seller prepared to sell the goods to the buyer.

Both requirements must be satisfied separately. If one of the conditions laid down in article 71(1)(c) of the UCC is not met, royalties and/or licence fees should not be a part of the customs value.

Article 136 of the UCC IA gives further directions as to whether or not royalties are to be added to the customs value of goods. However, it can be questioned whether, in the situation that there is no ground for including royalty payments in the transaction value on the basis of article 70 of the UCC, these payments can still be considered dutiable on the basis of any provisions in the UCC IA. This question is based on the concept that the UCC in principle takes precedence over the UCC IA.<sup>[33]</sup> Therefore, the argument could be raised that the UCC IA – which clarifies the legal framework of the UCC – should be interpreted in the light of article 71(1)(c) of the UCC and can therefore potentially not provide for stricter rules than the UCC.

Under the old EU customs legislation, a distinction was made between royalties paid in respect of the right to use a trademark, as opposed to royalties paid for the use of other types of intellectual property.<sup>[34]</sup> There was also a specific provision for the situation

30. See the most recent update of the Customs Valuation Compendium 2022, available at [https://taxation-customs.ec.europa.eu/document/download/9a13b89e-9e5e-482e-be0b-f593d96bc815\\_en?filename=2022%20EU%20Valuation%20Compendium%20EN.pdf](https://taxation-customs.ec.europa.eu/document/download/9a13b89e-9e5e-482e-be0b-f593d96bc815_en?filename=2022%20EU%20Valuation%20Compendium%20EN.pdf) (accessed 27 July 2022).

31. Art. 70(1) UCC read in conjunction with art. 71(1)(c) UCC.

32. Art. 71(1)(c) UCC is equal to art. 8(1)(c) WTO Customs Valuation Agreement.

33. See also ECJ cases NL: ECJ, 13 Dec. 2001, *Case C-317/99, Kloosterboer Rotterdam B.V.*, Case Law IBFD; BE/DE: ECJ, 4 Feb. 1997, *Joined Cases C-9/95, C-23/95, C-156/95, Belgium and Germany v. Commission*, and E2: ECJ, 11 Nov. 1999, *Case C-48/98, Firma Söhl & Söhlke v. Hauptzollamt Bremen*, Case Law IBFD, according to which an indication is given that it follows from the case law of the Court that the Commission is authorized to adopt all the measures which are necessary or appropriate for the implementation of the basic legislation, provided that they are not contrary to such legislation or to the implementing legislation adopted by the Council.

34. This was included in art. 159 CCIP. Based on this article, a royalty or a licence fee in respect of the right to use a trademark was only to be added to the transaction value where:

- the royalty or licence fee refers to goods which are resold in the same state or which are subject only to minor processing after importation;
- the goods are marketed under the trademark, affixed before or after importation, for which the royalty or licence fee is paid; and

where a royalty is paid to a third party (i.e. not the manufacturer of the goods).<sup>[35]</sup> As a result of these provisions, it was less likely for royalties or licence fees to be dutiable for customs purposes where a royalty payment was related to the right to use a trademark or where royalties were paid to third persons. Under the UCC, it is more likely that the royalties will be payable in these circumstances. The aforementioned provisions were EU specific, because in the respective situations, the WTO Customs Valuation Agreement only constitutes the “condition of sale” rule (also the position under the UCC).

Based on article 136(4) of the UCC IA, royalties and licence fees are considered to be paid as a condition of sale for the imported goods when any of the following conditions are met:<sup>[36]</sup>

- the seller or a person related to the seller requires the buyer to make the royalty payment;
- the payment by the buyer is made to satisfy an obligation of the seller, in accordance with contractual obligations; or
- the goods cannot be sold to, or purchased by, the buyer without payment of the royalties or licence fees to a licensor.

Under the UCC, the “condition of sale” determination has been broadened which can result in a more frequent inclusion of royalty payments in the customs value.

As an example of broadening the scope for inclusion, the third criterion above could imply that even in the situation where the buyer, the seller and licensor are all unrelated parties, the royalty paid by the buyer is dutiable. This position was not that obvious under the old EU customs legislation. However, Commentary 13 of the Compendium Customs Valuation states that the condition of sale test may not be directly applicable when royalty payments are paid to a third party, because the commercial arrangement between buyer and seller may not really create such a condition for the buyer.<sup>[37]</sup>

Some EU Member States may consider the third condition of article 136(4) of the UCC IA a catch-all clause. Commentary 13 states however that article 136 of the UCC IA does not indicate an assumption that royalties and licence fees are to be automatically included in the customs value, and that the article does not state that the conditions for dutiability are automatically met unless the declarant demonstrates the contrary.<sup>[38]</sup> With respect to determining whether a royalty payment constitutes a condition of sale of the imported goods, Commentary 13 refers to WCO Commentary 25.1, which provides for a (non-exhaustive) list of factors that can be taken into account. In line with Commentary 13, the Dutch customs authorities tend to use Commentary 25.1 for determining whether a royalty payment is a condition of sale.

The following observations can be made with respect to the position of the Dutch customs authorities regarding royalty payments. The Dutch customs authorities have a knowledgeable national customs valuation team which critically examines the reasons for which the royalty payments are made, in order to establish whether the royalty is partly or fully dutiable or not dutiable at all. Some of the considerations in this regard include whether the royalty relate to payments for dutiable elements only, or whether the royalty also relates to non-dutiable elements. The Dutch customs authorities critically assess the “build up” of the royalty payments and examine the dutiable versus non-dutiable elements. The Dutch customs authorities will generally ask for copies of royalty/licence fee agreements in order to determine whether or not a royalty payment is dutiable for customs purposes. In order to determine whether a royalty payment constitutes a condition of sale of the imported goods, the Dutch customs authorities will generally use WCO Commentary 25.1. In this respect, the Dutch customs authorities often not only ask for copies of royalty/licence fee agreements, but also ask for copies of the sales agreements between the buyer/importer and the manufacturer.

## 1.2. Interaction between TP and customs rules

### 1.2.1. National Transfer Pricing

#### 1.2.1.1. Netherlands legislative and regulatory transfer pricing framework

The arm’s length principle was incorporated into the Corporate Income Tax Law of 1969 (*Vpb*) on 1 January 2002. Article 8b of the *Vpb* introduced an arm’s length provision that closely mirrored article 9 of the OECD Model Tax Convention on Income and on Capital (OECD Model).<sup>[39]</sup> This legislation formally required Dutch enterprises to prepare transfer pricing documentation if they are involved in transactions with associated enterprises.

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- the buyer is not free to obtain such goods from other suppliers unrelated to the seller.

35. This was included in art. 160 CCIP. This article reads as follows: “When the buyer pays royalties or license fees to a third party, the conditions provided for in Article 157(2) [the condition of sale] shall not be considered as met unless the seller or a person related to him requires the buyer to make that payment”.

36. Art. 136(4) UCC IA.

37. See section 3.7, point 2 Commentary 13.

38. See section 3.7, point 8-10 Commentary 13.

39. OECD, *OECD Model Tax Convention on Income and on Capital*, art. 9 (21 Nov. 2017), Treaties & Models IBFD.



Prior to the introduction of article 8b of the Vpb, the State Secretary of Finance issued two transfer pricing Decrees<sup>[40]</sup> that provided specific guidance on the treatment of transfer pricing issues and clarified the Dutch interpretation of the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations (OECD Guidelines).<sup>[41]</sup> These Decrees were replaced by Decree No. IFZ 2013/184M of 14 November 2013, which was a completely revised and updated transfer pricing Decree and provided important insights and guidance on particular transfer pricing issues.<sup>[42]</sup>

On 11 May 2018, the Dutch State Secretary of Finance (the Finance Secretary) published transfer pricing Decree No. 2018-6865 of 22 Apr. 2018.<sup>[43]</sup> This decree has replaced Decree No. IFZ 2013/184M of 14 November 2013.<sup>[44]</sup> It contains a number of new sections and changes in light of the amendments to the OECD Guidelines as a result of the OECD BEPS Project (more specifically BEPS Actions 8-10 “Aligning Transfer Pricing Outcomes with Value Creation” and BEPS Action 13 “Guidance on Transfer Pricing Documentation and Country-by-Country Reporting”) and specific developments in Dutch case law. Decree No. 2018-6865 provides a further interpretation of the arm’s length principle where the OECD Guidelines leave room for interpretation or where there is ambiguity.

The Finance Secretary is of the opinion that, insofar as the changes in the OECD Guidelines are a further clarification of the application of the arm’s length principle, such changes are also applicable to years in which the changes were not yet published. Decree No. 2018-6865 does not specify which changes are considered a mere clarification. However, based on earlier communication by the Finance Secretary,<sup>[45]</sup> one may derive that the amended guidance on the following matters is not considered a mere clarification: documentation requirements, intangibles, intra-group services, commodity transactions, and cost contribution arrangements.

With respect to transfer pricing documentation, the Netherlands has implemented a three-tiered approach for transfer pricing documentation in line with the final report of Action 13<sup>[46]</sup> of the OECD’s BEPS Project (see section 4.) as currently incorporated in Chapter V of the OECD Guidelines. In this chapter, “the old EU customs legislation” is used to refer to the legislation that was in place prior to 1 May 2016, i.e. prior to the Union [Customs Code](#) (UCC) becoming effective (see section 1.1.).

### 1.2.1.2. Transfer pricing methods

Consistent with the original guidance that was applicable since 2001, [Decree No. 2018-6865](#) still confirms that all OECD transfer pricing methods are acceptable in the Netherlands.<sup>[47]</sup>

The traditional transaction transfer pricing methods are as follows:

- the comparable uncontrolled price (CUP) method;
- the resale price method (RPM); and
- the cost-plus method.

In addition, there are also the so-called transactional profit transfer pricing methods, namely:

- the transactional net margin method (TNMM); and
- the profit split method.

It is important to note that Decree No. 2018-6865 continues to confirm that the tax authorities, in case of a transfer pricing investigation, should use the method that was applied by the taxpayer to set its prices.<sup>[48]</sup>

The Dutch authorities do not favour the “best method rule”. However, despite the absence of a best method rule, the taxpayer should be able to substantiate the choice of a certain transfer pricing method. Moreover, Decree No. 2018-6865 continues to acknowledge that several methods could also be used in conjunction.

40. Decree of 30 Mar. 2001, IFZ2001/295M, which was subsequently updated by (amongst others) the Decree of 21 August 2004, IFZ2004/680M and its revised version of 26 Nov. 2016.

41. Following the OECD’s Base Erosion and Profit Shifting (BEPS) Project, the OECD issued a new version of the *OECD Guidelines* in January 2022. See *OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations* (OECD 2022), Primary Sources IBFD [hereinafter *OECD Guidelines*].

42. Decree of 14 Nov. 2013, No. IFZ2013/184M, available at <https://zoek.officielebekendmakingen.nl/stcrt-2013-32854.html> (accessed 20 July 2022).

43. Decree of 22 Apr. 2018, No. 2018-6865, available at <https://zoek.officielebekendmakingen.nl/stcrt-2018-26874.html> (accessed 20 July 2022). Decree of 22 Apr. 2018, No. 2018-6865 is aligned with the July 2017 version of the OECD Guidelines.

44. Decree of 14 Nov. 2013, No. IFZ2013/184M, available at <https://zoek.officielebekendmakingen.nl/stcrt-2013-32854.html> (accessed 18 July 2022).

45. Finance Secretary’s letter to Dutch Parliament dated 5 Oct. 2015, p. 18; and the letter to Dutch Parliament dated 2 Feb. 2016, p. 17.

46. OECD/G20, *Transfer Pricing Documentation and Country-by-Country Reporting – Action 13: 2015 Final Report* (OECD 2015), Primary Sources IBFD.

47. Decree of 22 Apr. 2018, No. 2018-6865 art. 3.1, available at <https://zoek.officielebekendmakingen.nl/stcrt-2018-26874.html> (accessed 18 July 2022).

48. Decree of 22 Apr. 2018, No. 2018-6865 art. 3.1, available at <https://zoek.officielebekendmakingen.nl/stcrt-2018-26874.html> (accessed 18 July 2022).

Decree No. 2018-6865 provides for a specific consideration in relation to the application of the CUP method. It specifically acknowledges that it is very difficult to apply this method in practice since in most cases there are hardly any CUP references that can be used to apply it (and adhere to the comparability standards) in a reliable manner. For this reason, Decree No. 2018-6865 acknowledges that, in practice, the TNMM often needs to be applied instead as the most appropriate transfer pricing method.<sup>[49]</sup> In relation to applying the TNMM, Decree No. 2018-6865 also specifically explains that the TNMM should only be applied to the least complex entity and that this will typically not be the party that is entitled to the return on intangible assets considering the division of functions, assets and risks. In practice, this approach has always been followed in the Netherlands but it is certainly helpful that this is specifically acknowledged in Decree No. 2018-6865 in light of the broader discussions around the applicability of the TNMM in certain cases. Important to note here is that it is essential to consider the broader value chain perspective by not merely looking at individual transactions in isolation, as well as the possible aggregation aspects. Under this approach, the Dutch perspective on a (factual) two-sided analysis has always been a multi-sided perspective with full recognition of the broader set of arrangements that can be interlinked.

Furthermore, there is a specific section in Decree No. 2018-6865 around the remuneration for using intangible assets.<sup>[50]</sup> Specifically, in the context of intangible assets, Decree No. 2018-6865 emphasizes that the tax authorities are very critical of external CUP analyses through database studies since there is typically no sufficient reliable information to assess whether comparability standards can be met. Decree No. 2018-6865 also explains that one-sided methods, like the TNMM, can be applied to indirectly determine an arm's length result for the intangible asset by first determining the remuneration for the tested party. This can be done in cases whereby the residual profit can be allocated to the intangible asset and the associated functions in relation to this asset. More specifically, if a Dutch entity is performing routine activities and the key functions in relation to foreign-owned IP are also performed outside the Netherlands, the TNMM may be used to indirectly determine the value of the foreign-owned IP. A key condition under this approach is that all other functions, assets and risks are adequately compensated. Again, this policy has been in place since 1998 but has not yet been described in this level of detail in any administrative decree. Since there are many cases whereby there are (i) no internal CUPs in relation to intangible assets; and (ii) no external CUPs that are sufficiently comparable (or with sufficient data to validate the comparability standards), it is crucial that indirect approaches accounting for the arm's length remuneration of the other functions can be used for substantiating the residual profit that can be allocated to intangible assets (and the underlying functions associated with these intangible assets). The broader value chain approach is also clearly described in the current OECD Guidelines in paragraph 6.32 which states that "other members of the legal intangible owner's MNE group may have performed functions, used assets, or assumed risks that are expected to contribute to the value of the intangible". This is further echoed in paragraph 6.42:<sup>[51]</sup> "The return ultimately retained by or attributed to the legal owner depends upon the functions it performs, the assets it uses, and the risks it assumes, and upon the contributions made by other MNE group members through their functions performed, assets used, and risks assumed."

Decree No. 2018-6865 also provides important guidance around cost-based profit level indicators (PLIs).<sup>[52]</sup> If a third party would not realize a profit on certain costs, such costs should also not be included in the context of intercompany transactions. A specific example is provided in relation to intermediary roles (with a reference to paragraph 7.34 of the OECD Guidelines) that clarifies that in such cases the cost base on which a mark-up should be applied needs to be limited to the costs for which the company contributes through its own functions, risks and assets but not in relation to services supplied by third parties. Decree No. 2018-6865 continues to refer to costs with a "disbursement nature" that should not be included in the cost base. However, it also contains a helpful example that illustrates that this may also pertain to services/activities provided by other group companies and that the underlying costs should therefore not be included in the cost base. The actual example pertains to a manufacturer whereby the manufacturing affiliate is engaged in processing raw materials but that, in light of its functions, does not incur any risks in relation to these raw materials. The relevant functions in relation to raw materials are performed by other (group) companies. In such cases, the relevant cost base for applying a mark-up should be limited to the cost base that can be associated with the affiliated manufacturer's own functions, risks and assets but not the underlying raw materials. Consistent with the broader Dutch focus on economic substance, this example clarifies that the legal arrangement or the underlying administrative arrangements are not leading for characterization of a transaction. The underlying (functional) characterization of the transaction should be based on the relevant facts and circumstances whereby the mere legal title is not decisive but the underlying functions, risks and assets drive the characterization.

Another example provided by Decree No. 2018-6865 pertains to legal buy-sell arrangements whereby the underlying functional contribution is limited to an administrative contribution to a sales transaction (and the sales function is performed elsewhere in or outside the group).<sup>[53]</sup> In this example, a Dutch affiliate may engage in a legal buy-sell arrangement and therefore record revenue on its books but it does not perform any sales or revenue-generating functions. Consistent with paragraph 2.39 of the OECD

49. Decree of 22 Apr. 2018, No. 2018-6865 art. 3.1, available at <https://zoek.officielebekendmakingen.nl/stcrt-2018-26874.html> (accessed 18 July 2022).

50. Decree of 22 Apr. 2018, No. 2018-6865 sec. 5, available at <https://zoek.officielebekendmakingen.nl/stcrt-2018-26874.html> (accessed 18 July 2022).

51. Para. 6.42 *OECD Guidelines*.

52. Decree of 22 Apr. 2018, No. 2018-6865 art. 3.2, available at <https://zoek.officielebekendmakingen.nl/stcrt-2018-26874.html> (accessed 18 July 2022).

53. Decree of 22 Apr. 2018, No. 2018-6865 art. 3.2, available at <https://zoek.officielebekendmakingen.nl/stcrt-2018-26874.html> (accessed 18 July 2022).

Guidelines, the intermediary company in such a case is not considered to add any value to the actual sales activity (not does it incur any risk) and should therefore also not be entitled to sales-related return. More specifically, this means that a revenue-based remuneration would not be appropriate but instead a cost-based profit level indicator should be applied that accounts for the relevant operating costs of the intermediary company. This approach recognizes that the revenue that is recorded in the profit and loss statement of such an intermediary is not leading for the underlying characterization if the functional contribution does not include a sales function but a mere administrative function. Given the geographic position of the Netherlands and its role in logistics and warehousing, it is relevant to note that there are many logistics facilities based in the Netherlands whereby, for the sake of administrative simplicity, the revenue is often legally recorded in their books. In all these cases where there is a mere logistics activity without any sales functionality, the arm's length remuneration should be based on the relevant operating costs instead of the revenue that is booked/administrated in their profit and loss statements. Historically, many companies have obtained formal advance certainty on this mark-up on operating costs approach through the Dutch APA program.

### 1.2.1.3. Use of comparables

The use of arm's length ranges, based on comparable data, is addressed in the Dutch TP regulations and clarifications. The application of a transfer pricing method will most likely provide a range of prices or results rather than one single arm's length price. An arm's length range comprises the lowest and highest figure that is identified. These figures pertain to information on prices or relevant profit level indicators, as derived from comparable transactions and/or companies. The OECD Guidelines<sup>[54]</sup> do not specifically state which of the figures within that range would be relevant as a basis for a potential adjustment, if the transfer price does not fall within that range. Furthermore, a distinction should be made between a range that comprises comparable transactions with a relatively high level of comparability (high reliability) and a range that comprises comparable transactions with a relatively low level of comparability (lower reliability). In the latter situation, it may be necessary to apply statistical approaches (e.g. the use of an interquartile range) in order to increase the reliability of the range.

Once a range is established, it needs to be determined to what extent the transaction under review falls within the range. If the transfer price in the transaction under review is within the range, there is no need for an adjustment. If the transfer price is outside of the range and the taxpayer is not able to justify such a result, the tax authorities would apply an adjustment to the transfer price. The Dutch TP practice follows the OECD Guidelines, and the OECD Guidelines indicate that "where the range comprises results of relatively equal and high reliability, it could be argued that any point in the range satisfies the arm's length principle".<sup>[55]</sup> The OECD Guidelines further indicate that if there are still comparability defects, it may be appropriate to use measures of central tendency (e.g. the median of the benchmark) to select this point (to which the adjustment should be made). In this light, the tax authorities also would apply an adjustment on the basis of the median observation within the arm's length range.<sup>[56]</sup>

In certain cases, enterprises apply amendments within the arm's length range by adjusting the transfer prices either upwards or downwards. However, if a taxpayer makes such a change within the arm's length range, the taxpayer should be able to demonstrate a change in the circumstances that would justify such a price change. If there are no changed circumstances, the Dutch authorities would assume that such amendments within the range are motivated by tax reasons and would not accept such price changes. Furthermore, such amendments would only be allowed if they were contractually agreed upon and if the changes in the range are actually charged between the group companies. This specific clause goes beyond the general framework of the OECD Guidelines. Thus, in order to ensure that such price changes within the range will be accepted by the tax authorities, a taxpayer needs to be able to show that:

- a change in circumstances justifies a price change;
- there are contractual arrangements between the controlled enterprises that provide for the possibility to adjust prices; and
- the change in the arm's length range is actually charged between the controlled enterprises (i.e. the parties actually implemented the price change).

One of the important aspects to consider relates to the potential benefits of using multiple-year data. Including multiple-year data could help avoid adjustments from the tax authorities in a certain year if the transfer price were to fall within a multiple-year range. It is recognized that the OECD Guidelines do not approve of the use of hindsight.<sup>[57]</sup> Consequently, the use of a multiple-year range should be restricted to the year under review and prior years. The selection of the number of years should depend on the life cycle of the product in question and other relevant factors. The tax authorities have adopted a peculiar way of applying a multiple-year range, however. In the case of a transfer pricing audit and/or review, the range should be applied as follows:

<sup>54.</sup> Paras. 3.55-3.66 *OECD Guidelines*.

<sup>55.</sup> Paras. 3.61-3.62 *OECD Guidelines*.

<sup>56.</sup> If necessary, the Dutch authorities would be willing to negotiate this with other authorities in a mutual agreement procedure upon request of the taxpayer.

<sup>57.</sup> This argument is not emphasized in the section that provides guidance on the valuation of intangible property that is also discussed in this chapter.

- determine whether the result of an intercompany transaction falls within a 1-year arm's length range (there is no need for an adjustment if the result falls within the 1-year range); and
- if outside of the range, determine whether the result of the transaction falls within a multiple-year range (there is no need for an adjustment if the result falls within the multiple-year range).

If the result is outside of the range, the considerations mentioned above for applying adjustments come into play. This way of using multiple-year ranges provides the taxpayer with the flexibility to always initially use 1-year ranges and only use multiple-year ranges if necessary. Because it appears that there is no specific "consistency" condition, this may mean that one can use a multiple-year range for 1 year and a 1-year range for another.

Transfer pricing adjustments may influence the customs value of goods that have already been imported. See section 2.

### 1.2.1.4. Valuation approaches and asset transfers

There are some specific approaches to the application of the arm's length principle in the Netherlands. Decree No. 2018-6865 acknowledges that the applicable valuation methods as discussed under the OECD Guidelines<sup>[58]</sup> are applicable in the Netherlands.<sup>[59]</sup> However, it also emphasizes that valuations should account for the perspective of all parties involved. In other words, both the buyer and seller perspective should be accounted for. It is important to note that under the Dutch approach it is expected that the buyer perspective reflects a higher price as compared to the seller perspective and that the two-sided approach would typically reflect a value that falls within the range established by the buyer versus seller perspective.

Specifically in relation to both tangible and (even more so) intangible assets, Decree No. 2018-6865 continues to apply the condition that a transfer of such an asset to an affiliated company will not meet the arm's length standard if the acquiring company is not able to enhance the value of this asset because the underlying functionality is not there and the underlying risks cannot be actively managed. Further to the aforementioned "fiction" around the buyer and seller perspective, Decree No. 2018-6865 explicitly states that if the overall profit of the multinational enterprise does not increase as part of the asset transaction, the transaction will not be recognized under the application of the arm's length standard. It will be very important to carefully consider this guidance since the tax authorities are very determined to follow this guidance in particular in outbound transactions whereby the tax authorities suspect that the foreign buyer's functionality is limited.

Furthermore, Decree No. 2018-6865 acknowledges the importance of DEMPE (i.e. development, enhancement, maintenance, protection and exploitation of intangibles) (control) functions. It specifically states that the "development" and "enhancement" function will be assigned a higher weight in measuring the relative importance of the different DEMPE contributions in relation to intangible assets.

With regard to intangible property, there is significant focus on the uncertainty that may exist about the underlying value of intangible property when engaging in an intercompany licence transfer. Decree No. 2018-6865 continues to emphasize the Dutch preference for including a price adjustment clause in situations in which the valuation is highly uncertain at the time of the transaction. The underlying rationale is that independent enterprises would not be willing to enter into a fixed arrangement when the valuation is highly uncertain. In particular, this is required in a so-called round trip transaction, whereby the owner of intangible assets transfers these assets and subsequently (partially) licenses them back. In the authors' experience, the tax authorities are typically quite reluctant to accept a CUP analysis for intercompany licences if such a CUP analysis is based on external comparables. In view of the fact that the CUP method requires a high degree of comparability, and a typical CUP analysis based on licence agreements between third parties may not entail sufficient comparability with the intercompany licence, the tax authorities typically expect other (corroborating) methodologies to substantiate the arm's length nature. Such other methodology could for example be the profit split or the transactional net margin method (the latter method would be useful to demonstrate that the licensee's overall remuneration after paying royalties can be considered reasonable).

The OECD guidance around hard-to-value intangibles introduces a new concept under the Dutch regulatory framework that entails the adoption of (effectively) using hindsight. If there are significant deviations between the actual results and the forecasted results that formed the basis for the original valuation, the tax authorities can make adjustments. The State Secretary of Finance has stated in this case that a deviation of more than 20%, which materializes in the first 5 years after the transfer, will be considered a significant deviation that can justify an adjustment to the original established arm's length value on the basis of the valuation.

Furthermore, the tax authorities will scrutinize (immaterial) asset transactions whereby the buyer does not have the required substance to add value to the acquired asset. Another transaction that requires specific attention entails centralized purchasing activities. Although the pricing of such activities is often based on a percentage of expenditure (or "value-based" fee), the tax authorities, in principle, take the position that a cost-plus methodology is the most appropriate methodology for these types of

<sup>58</sup>. Ch. 2 *OECD Guidelines*.

<sup>59</sup>. Decree of 22 Apr. 2018, No. 2018-6865 art. 3.1, available at <https://zoek.officielebekendmakingen.nl/stcrt-2018-26874.html> (accessed 18 July 2022).



activities. This approach is not only based on a Supreme Court case<sup>60</sup> but also hinges on the notion that most purchasing benefits entail so-called “volume rebates” that should be shared amongst affiliated companies in the viewpoint of the tax authorities.

There are also some specific approaches to intercompany services, financing arrangements and cost contribution arrangements, but these are arguably less important from a customs perspective.

There are no particular approaches for specific industries, but due to the facts and circumstances of specific industries, certain methods are more common than others. To illustrate, within the automotive industry it is quite common that local country importers/distributors very much perform routine functions and therefore the transactional net margin method is typically the right method to establish arm’s length remuneration for such routine functions. Within the pharmaceutical industry, however, the division of roles and responsibilities can be much more complex and therefore justify different methodologies. To illustrate, it is not uncommon to enter into co-promotion agreements within the pharmaceutical industry. These types of arrangements are typically set-up between third parties based on profit split considerations. Thus, the application of the profit split may be the most appropriate model for such specific arrangements within the pharmaceutical industry. Nonetheless, within the Netherlands there are certainly no “default transfer pricing methods” for specific industries. The analysis of specific facts and circumstances, the entire value chain and respective contributions of the related parties in terms of functions, risks and assets is the crucial element in assessing the most appropriate transfer pricing methodology.

### 1.2.2. Comparison of valuation methods

Certain valuation methods used for transfer pricing and customs purposes are not identical, but do have strong similarities.

	OECD (transfer pricing)	UCC (customs)
1		Transaction value
2	CUP	Identical goods; and Similar goods
3	Resale price method (RPM)	Deductive value
4	Cost plus method	Computed value
5		Fall-back method

Customs valuation methods 2 (transaction value of identical goods) and 3 (transaction value of similar goods) have great similarities with the CUP method for transfer pricing. Further, customs valuation method 4 (deductive value) is similar to the RPM. Finally, both the computed value (method 5) for customs purposes and the Cost plus for transfer pricing are based on the same principles in order to arrive at an acceptable price level. We note however that where a transfer price is determined (regardless of the method that is used), that transfer price can generally serve as a basis to determine the customs value of imported goods, according to the transaction value method. From a customs perspective, one could therefore also say that the CUP, and the transfer price based on a cost plus method or RPM, constitute the transaction value as long as the requirement can be satisfied that this value is also at arm’s length from a customs valuation perspective. See section 4. for more information regarding the use of transfer pricing documentation for customs purposes.

Although these methods show great similarities and would result in similar and acceptable prices for both the tax and customs authorities, none of these valuation methods are frequently applied in practice. For transfer pricing purposes, the CUP method and the “pure” application of the cost plus and RPM are rarely used. In fact, for transfer pricing it is quite common to use the transactional net margin method (TNMM) on an aggregated level which makes the “translation” to one of the accepted customs methods on an actual transaction level rather difficult. Although it is possible to apply “pro rata” approaches to ensure that the margins established under the TNMM are effectively similar across all products, this does entail an additional level of analysis that is important for customs purposes, but not necessarily relevant for corporate income tax purposes. For customs purposes, the most frequently used valuation method in international trade, including imports into the Netherlands, is the transaction value of the imported goods (method 1). The transaction value, i.e. the price actually paid or payable for the goods when sold for export, is the preferred valuation method based on the legal customs framework, and further is easier to use in practice compared to the other methods since it is based on the actual sales transaction information and documentation (e.g. the sales invoice for the goods).

The alternate customs valuation methods can (or must) only be used if the transaction value method cannot be applied. To start with, this can occur in the absence of a sales transaction (for example transfer and imports of own goods into the Netherlands). However, in the context of comparing the two tax areas, a more relevant ground to reject the use of the transaction value arises with related party transactions, where the relationship between the seller and the buyer has influenced the price.

60. NL: HR, 23 Apr. 2004, No. 39 542, VN 2004/27.17.

The use of the transaction value method for related party transactions can be summarized as follows. Based on article [134\(1\) of the UCC IA](#), the fact that the buyer and the seller are related shall not in itself be grounds for regarding the transaction value as unacceptable. However, Customs can examine the circumstances surrounding the sale and should accept the transaction value provided that the relationship did not influence the price. This basically introduces and recognizes for customs purposes the “at arm’s length principle” which is also known in the transfer pricing methodologies.

Under the old EU customs legislation, Annex 23 to the CCIP clarified that it was not intended that there should be an examination of the circumstances surrounding the sale in all cases where the buyer and the seller were related. Such examination was only required where there were doubts about the acceptability of the price. Where Customs had no such doubts, the price was to be accepted without requesting further information from the importer. There is no equivalent of the legally binding Annex 23 to the CCIP in the UCC legal package, although this “rule” can be found in the legally non-binding Section B of the Compendium Customs Valuation. Article [134\(1\) of the UCC IA](#) even states that where the buyer and the seller are related, in order to determine whether such relationship has not had an influence on the price, the circumstances surrounding the sale *shall* be examined as may be necessary. This means that where Customs is unable to accept the transaction value without further inquiry, it must give the importer an opportunity to supply such further detailed information as may be necessary to enable it to examine the circumstances surrounding the sale.

Where the circumstances of sales test is conducted, Customs should be prepared to examine relevant aspects of the transaction, including the way in which the buyer and seller organize their commercial relations and the way in which the price in question was arrived at, in order to determine whether the relationship influenced the price. Where it can be shown that the buyer and seller, although related for customs purposes, buy from and sell to each other as if they were not related, this would demonstrate that the price had not been influenced by the relationship and the transaction value method should be accepted by Customs.

In the following paragraph a more detailed analysis is given on the possibility to use transfer pricing documentation in the context of satisfying the circumstances of sales test for Customs. However, for the sake of completeness, it is relevant to also indicate that this test method is not the only available instrument for an importer to justify, and avoid rejection of, the transaction value based on its sales invoices. Article [134\(2\) of the UCC IA](#) gives importers the right to demand that the value should be accepted when they demonstrate that the value closely approximates one of the following test values occurring at or about the same time:

- (a) the transaction value in sales, between buyers and sellers who are not related in any particular case, of identical or similar goods for export to the customs territory of the European Union;
- (b) the customs value of identical or similar goods as determined under the deductive value (method 4);
- (c) the customs value of identical or similar goods as determined under the computed value (method 5).

To conclude, for customs purposes the transaction value is used in the majority of imports into the Netherlands. As this method is not directly comparable to one of the valuation methods for transfer pricing, it is therefore more often than not the situation that the customs value is based on a different valuation method than a similar equivalent for transfer pricing (and vice versa).

### Circulars on transfer pricing and customs valuation

The interaction between customs methods and transfer pricing is, from a customs perspective, laid down in the Dutch interpretative and policy directives (the Dutch “Customs Handbook” referred to in section [1.1.1](#)). This is an instruction manual with interpretations on the valuation legislation for the Dutch customs authorities. It is not to be considered as binding customs legislation; nevertheless, it does make clear how the customs authorities in first instance will look at the definition and interpretation of customs valuation aspects.

In the Dutch Customs Handbook, it is explicitly stated that the arm’s length principle used in the OECD context for transfer pricing can also be used for assessing import duties. The policy directive specifically refers to the OECD transfer pricing methods. It indicates that the traditional transaction methods are preferred over the transactional profit methods. The Dutch Customs Handbook mentions that the OECD methods and customs valuation methods show many similarities, but are isolated methods and should be considered and used as such.

In this context it is relevant to mention that the Dutch Customs Handbook explicitly refers to Dutch case law from the Dutch Tariff Commission with respect to the interdependency between corporate tax and customs legislation. The Handbook indicates that the Dutch Tariff Commission (*Tariefcommissie*) has considered that establishing the customs value should be done in accordance with customs legislation. A value established for taxes other than for customs purposes is not decisive. The issue of “influence” for



corporate tax purposes does not – because customs legislation does not specifically refer to this – need to be taken into account in deciding on a dispute on establishing the customs value.<sup>[61]</sup>

## 2. Practical Impact of TP and Customs Adjustments

Where a transfer price is used as the basis for determining the customs value of imported goods based on the transaction value method, and such a transfer price is adjusted, such an adjustment may impact the customs value that was initially reported. A transfer pricing adjustment has an impact on the customs value of imported goods, if:

- it concerns a retroactive/prospective transfer pricing adjustment; and
- the transfer pricing adjustment relates to the imported goods.

This follows from the fact that the transaction value is the price actually paid or payable, consisting of the total payment made or to be made by the buyer to the seller (or to a third party for the benefit of the seller) for the imported goods. This price should include all payments made or to be made as a condition of sale of the imported goods ([article 70\(2\) of the UCC](#)).

The Dutch government also implemented legislation intended to avoid double non-taxation resulting from the unilateral application of the arm's length principle in the Netherlands as of 1 January 2022.<sup>[62]</sup> The Dutch transfer pricing rules require a unilateral upward or downward correction of the commercially applied transfer prices between related parties to ensure the recognition of an arm's length profit for Dutch tax purposes.

If a transaction between a Dutch corporate taxpayer and a foreign related party is not at arm's length, the legislation denies a downward adjustment of the taxable income of the Dutch taxpayer (either as a payor or payee) to the extent a corresponding upward adjustment is not included in the taxable basis of a profit tax in the country of the foreign counterparty. The burden of proof for such inclusion lies with the Dutch taxpayer. The documentation to demonstrate this is in principle form free.

### 2.1. TP adjustments resulting in an increase in price paid by importers

Both downward (leading to a lower customs value) and upward (leading to a higher customs value) retroactive transfer pricing adjustments have an impact on the customs value of imported goods as initially reported. We note however that the customs authorities of some EU Member States may be willing to accept upward adjustments of the customs value, but may reject downward adjustments.

The Dutch customs authorities accept upward adjustments of the customs value (as a result of transfer pricing adjustments) provided that at the moment of the initial import entry there was an agreement in place which explains that prices can be adjusted (price review clauses).

### 2.2. TP adjustments resulting in a decrease in price paid by importers

The Dutch customs authorities accept downward adjustments of the customs value (as a result of TP adjustments), provided that, at the moment of the initial import entry, there was an agreement in place which explains that prices can be adjusted (price review clauses).

### 2.3. Other implications for customs due to TP adjustments

There are several ways in which transfer pricing adjustments can be taken into account for customs valuation purposes. The first option is submitting simplified declarations ([article 166 of the UCC](#)). Once the actual customs value is known (i.e. after the transfer pricing adjustments have taken place), the import declarations would have to be completed. The regular use of simplified declarations is subject to an authorization from the customs authorities ([article 166\(2\) of the UCC](#)). This method is burdensome, as each single customs declaration would have to be corrected once the transfer pricing adjustment is known. Also, as the transfer pricing adjustment is generally a global adjustment which pertains to a large number of transactions, it is often difficult and burdensome to allocate the transfer pricing adjustment to each of the transactions.

Another option to take transfer pricing adjustments into account for customs valuation purposes, is applying for a licence under article 73 of the UCC. This licence allows amounts which are to be included in the customs value in accordance with article 70(2) of the UCC and the amounts referred to in articles 71 and 72 of the UCC, to be determined on the basis of specific criteria, where

<sup>61</sup>. Reference is made to Tariefcommissie Nos. 12986, 12988, 12989 and 13049 of 21 Dec. 1994. See also Tariefcommissie Nos. 88/95 to 90/95, 118/95 to 122/95, 131/95 to 155/95 and 10/96 of 25 Nov. 1997.

<sup>62</sup>. Dutch Corporate Income Tax Act (*Vpb*), art. 8ba.

they are not quantifiable on the date on which the customs declaration is accepted. Based on this licence, the importer should determine a fixed percentage to account for transfer pricing adjustments. This fixed percentage would be applied to every import transaction. The fixed percentage is subject to change. Therefore, each period (usually a year) it has to be determined what the transfer pricing adjustment will be and how that adjustment can be reflected as a percentage of the value of the imported goods. This may be a challenging exercise for many companies, because generally it is not known whether there will be an upward or downward transfer pricing adjustment and to which extent this can be foreseen at the beginning of the year. Most companies will therefore apply a fixed percentage on the basis of the adjustments made in the previous year. This could be disadvantageous, as the imported volumes are subject to changes over the years. The conditions for applying for such licence are stated in article 71 of the UCC DA.

The Dutch customs authorities also accept – at their discretion – an approach with respect to the amendment of the customs value as a result of retroactive transfer pricing adjustments in which they allowed companies to submit periodical (often yearly) adjustments, once the transfer pricing adjustment is known. The weighted average import duty rate would be calculated for that period, and would be applied to the transfer pricing adjustment, resulting in the payable amount or the amount to be refunded. This approach is also advocated by the International Chamber of Commerce, although one can argue that a clear legislative basis in the UCC is absent and this approach is not in line with the ECJ's ruling in the *Hamamatsu* case (see below).<sup>[63]</sup> However, to apply such a practical approach, a ruling should be obtained from the Dutch Customs' Valuation Team.

In some cases, the Dutch customs authorities take the position that agreements between importers and the customs authorities regarding customs valuation should be included in the format of the article 73 licence. In that case, a fixed percentage is applied to each import transaction, under the licence of article 73 of the UCC. In other cases, the Dutch customs authorities recognize that specific circumstances can make it difficult to apply for such a licence. Therefore, the Dutch customs authorities still respond to ruling requests where the importer requests an annual adjustment of the reported customs value, although a legal basis seems to be lacking and the approach may not be in line with the ECJ ruling in the *Hamamatsu* case (see below). Especially in situations where the conditions for the use of the simplification of article 73 of the UCC are not met, the Dutch customs authorities may still take requests for annual adjustments into consideration. One of the conditions for the use of the simplification is for instance that the customs value determined will not significantly differ from that determined in the absence of an authorization (article 71(1)(b) of the UCC DA). As mentioned above, applying a fixed percentage to account for transfer pricing adjustments can be disadvantageous where imported volumes fluctuate over the years (as the fixed percentage is determined on volumes imported in the previous year and the transfer pricing adjustment of the previous year).

### **Hamamatsu case**

Since the ECJ ruled in the *Hamamatsu Photonics* case (20 December 2017, [Case C-529/16](#)),<sup>[64]</sup> there has been some uncertainty regarding the influence of retroactive transfer pricing adjustments on the customs value of imported goods for imports into the European Union. The *Hamamatsu* case concerns a customs duty refund request submitted by Hamamatsu Photonics Deutschland GmbH in Germany. Hamamatsu Photonics was a subsidiary of Hamamatsu Photonics Japan. The Japanese entity sold products to Hamamatsu Photonics. An advance pricing agreement covered the transactions between the two entities. The transfer price was adjusted at year-end, based on the “residual profit split method”, to ensure that the transfer price meets the arm's length standard range.

Hamamatsu Photonics imported goods in Germany and paid import duties. In 2010, the transfer price was retroactively adjusted downwards. Following the adjustment, Hamamatsu submitted a request with the German customs authorities, for repayment of the overpaid import duties. The amount of the refund was calculated based on the difference between the initial customs value and the adjusted value, multiplied by a weighted average duty rate. The German customs authorities rejected the refund request, because it did not allow the method by which the refund was calculated. The Court of Munich was of the view that the final transfer price (after adjustments) between the parties is based on the arm's length principle of the OECD, but that the price declared at the time of import was provisional. Therefore, the initially declared price is fictitious and cannot be used as the transaction value. The German court therefore referred the following preliminary questions to the ECJ:

- (1) Do the provisions of Article 28 et seq. of [the Customs Code] permit an agreed transfer price, which is composed of an amount initially invoiced and declared and a flat-rate adjustment made after the end of the accounting period, to form the basis for the customs value, using an allocation key, regardless of whether a subsequent debit charge or credit is made to the declarant at the end of the accounting period?
- (2) If so:

<sup>63</sup>. WCO *Guide to Customs Valuation and Transfer Pricing*, pp. 61 and 71 (WCO 2018), available at <http://www.wcoomd.org/-/media/wco/public/global/pdf/topics/key-issues/revenue-package/wco-guide-to-customs-valuation-and-transfer-pricing.pdf?la=en> (accessed 10 July 2022).

<sup>64</sup>. DE: ECJ, 20 Dec. 2017, [Case C-529/16](#), *Hamamatsu Photonics Deutschland GmbH v. Hauptzollamt München*, Case Law IBFD.

May the customs value be reviewed and/or determined using simplified approaches where the effects of subsequent transfer pricing adjustments (both upward and downward) can be recognised?

The ECJ ruled that:

1. Articles 28 to 31 [of the CCC] must be interpreted as meaning that they do not permit an agreed transaction value, composed of an amount initially invoiced and declared and a flat-rate adjustment made after the end of the accounting period, to form the basis for the customs value, without it being possible to know at the end of the accounting period whether that adjustment would be made up or down.<sup>2</sup>

The *Hamamatsu* judgment is subject to different interpretations.<sup>65</sup> Some are of the opinion that where transfer prices are used which can potentially be adjusted retroactively, the transaction value method cannot be applied. As many companies deal with transfer pricing and transfer pricing agreements often include the possibility to retroactively adjust prices, this interpretation would have far-reaching consequences for businesses. These businesses would then have to use one of the other customs valuation methods to determine the customs value of the imported goods. Furthermore, this interpretation would be contrary with the view of the WCO expressed in the “guide to customs valuation and transfer pricing”.

Others are of the opinion that the *Hamamatsu* judgment implies that the initially reported customs value is the transaction value, and that retroactive transfer pricing adjustments should not be taken into account at all for customs valuation purposes (i.e. both upward and downward adjustments of the customs value are not allowed).

The current internal policy of the Dutch customs authorities is that adjustments agreed upon in a licence (article 73 of the UCC), as explained before, can still be applied. However, ruling requests can also still be submitted. Depending on the facts and circumstances, the Dutch customs authorities may – at their discretion – grant a ruling allowing year-end adjustments of the customs value. However, any such rulings are granted without prejudice to any further guidance issued by the EC on the interpretation of the *Hamamatsu* judgment. This guidance is expected to be published once the German Federal Financial Court decides in the *Hamamatsu* case. While the Court informed Hamamatsu Photonics Deutschland GmbH, during a verbal hearing in June 2022, that it will rule in favour of the German customs authorities (i.e. rejecting the refund request), the considerations of the ruling have not yet been made public. Until such time, no guidance is to be expected from the European Commission.

### TP adjustments resulting in a decrease or increase of the export price

In the export declaration, the statistical value should be reported. The statistical value is determined based on the UCC provisions regarding customs valuation. Formally, a correct customs value has to be reported upon export of the goods. When it comes to TP adjustments and their impact on the customs value, in practice, we only see a focus on the value reported on import. If exporters want to be complete, they can choose to discuss this with the Dutch customs authorities.

### Penalties and interest

In the Netherlands, not taking into account TP adjustments in the customs value of imported goods may be considered as the reporting of an incorrect customs value and, thus, the filing of an incorrect customs declaration. Based on Dutch legislation, the filing of an incorrect customs declaration is considered a criminal offence and will be punishable by a maximum of 6 months' detention or a monetary penalty in the third category (i.e. EUR 9,000 in 2022). Deliberately submitting an inaccurate or incomplete customs declaration that results in undercharging duties imposed at import will be punishable by a maximum of 6 years' imprisonment or a monetary penalty in the fifth category (i.e. EUR 90,000 in 2022), or no more than the undercharged duties imposed at import, whichever amount is higher.

Whether or not, in practice, a penalty will be issued depends on several factors, one of which is the way the infringement was detected (e.g. in an audit or through a voluntary disclosure). The applicable penalties depend on the severity of the offense:

- I. In case the customs authorities consider the infringement as a less serious infringement (offence), the penalty is often set at 10% of the payable customs debt.
- II. If the customs authorities believe the infringement was more serious (generally, when the infringement was committed intentionally), they will regard it as a crime and will issue a fiscal penalty decision determining that. A fiscal penalty decision for a crime may have serious consequences for both the legal entity and the people involved.

Crimes, severe offences or repeated less severe offences may result in the revocation of the companies' customs licenses.

<sup>65</sup> M.L. Schippers & M. Friedhoff, [EU Court of Justice's judgment in Hamamatsu: An Abrupt End to Interaction Between Transfer Pricing and Customs Valuation?](#), *EC Tax Review*, Volume 28(1), pp. 32-42.

If the customs authorities issue a customs assessment for additional payable import duties (e.g. in relation to upward TP adjustments), late payment interest will become payable. The interest rate is based on the interest operated by the European Central Bank on the first day of the month in which the customs debt became due, increased by 2 percentage points. The payable interest is calculated based on the following formula:

$$((A \times P + A \times P \text{ etc.}) \times \text{payable amount}) / 36,000 = \text{late payment interest}$$

A = the number of days for which late payment interest is payable

the number of days for which late payment interest is payable

P = the applicable interest percentage

the applicable interest percentage

## 2.4. Impact of changes in customs value on TP

If the customs value is changed, there is not necessarily an automatic impact on transfer prices for corporate income tax purposes. However, there could be particular changes that may directly have an influence on the transfer prices for corporate income tax purposes. The clearest example would be the transaction value. If the transaction value for custom duties changes, and if this indeed reflects different values that are included in the statutory accounts, then (in principle) this should also be the starting point for corporate income tax purposes unless there is an element of informal capital or deemed dividend that should be eliminated. For other changes, it is less clear what the impact could be on transfer prices as such. However, if the customs value changes due to a price derived from identical or similar goods then this should trigger an assessment of the CUP method for transfer pricing purposes as well. Although the CUP method requires a (very) high degree of comparability, it is likely that the use of identical goods or similar goods for customs purposes could trigger a different/new transfer pricing assessment as well.

## 3. Cooperation between Competent Authorities

### 3.1. Competent authorities

The Dutch customs authorities are the competent authorities for levying customs duties. The Dutch tax authorities are the competent authorities for transfer pricing.

### 3.2. Exchange of information

The Netherlands has partially integrated customs and tax authorities, as well as pursuing joint examinations. In Rotterdam (Oil & Gas team) and Amsterdam (International Trade) there are two combined teams of customs and transfer pricing specialists. These teams also conduct joint tax audits. The emerging movement towards joint customs and transfer pricing enforcement is likely to impact upon current approaches to transfer pricing, and customs compliance and examination approach in the (near) future.

This joint teaming at the level of the Dutch customs and tax authorities is seen as an example of best practice cooperation.

### 3.3. Use of APAs and tax rulings

Within the Netherlands, there continues to be an increasing interaction between the tax and customs authorities. To illustrate, they have integrated customs and tax authorities' teams which conduct joined audits. Furthermore, it is also known that advance pricing agreements (APAs) can be concluded with the authorities that cover both transfer pricing and customs aspects. The tax authorities offer the possibilities to apply for such advance agreements. It is expected that the popularity of these types of APAs will rise in the future. In view of the integrated teams conducting audits, it is also not unreasonable to expect more future controversy if companies have not aligned their transfer pricing and customs positions.

APAs can be used for custom valuation purposes, just like TP documentation can be used for customs valuation purposes (see section 4.). Depending on the information included in the APA, the APA can be used to prove that the price charged between the related entities (which is reported as the transaction value) is at arm's length.

## 4. Use of TP Documentation for Customs Purposes

The Netherlands has two types of transfer pricing documentation requirements. The first is the Dutch primary transfer pricing documentation requirements as described in the third paragraph of article 8b of the Vpb. This paragraph stipulates that taxpayers are required to include information in their accounting records showing how their transfer prices have been established.

Furthermore, such information should enable the Dutch authorities to assess whether the taxpayer's transfer prices were concluded under arm's length conditions. The article refers to two main requirements:

- information that shows how transfer prices have been established; and
- information that is sufficient to assess whether the transfer prices were concluded under arm's length conditions.

The documentation requirements that are described in the third paragraph of article 8b of the Vpb specifically refer to a taxpayer's "accounting records". The State Secretary of Finance made reference to the OECD Guidelines for additional guidance on what should be included in transfer pricing documentation. He indicated that the following elements may be included in transfer pricing documentation:

- the characteristics of the goods and services;
- analysis of activities performed (including assets used and risks incurred);
- contractual terms and conditions; and
- economic circumstances and company strategies.

The second type of transfer pricing documentation requirements relates to the Final Report on Action 13 of the OECD's BEPS Project (i.e. the three-tiered approach). The three-tiered approach consists of the country-by-country (CbC) report, the master file and the local file. The requirements are applicable for qualifying multinational enterprises (MNEs) for fiscal years starting on or after 1 January 2016. MNEs with a consolidated turnover of EUR 750 million or more should prepare a CbC report. The (consolidated) turnover threshold for the master file and local file requirement is EUR 50 million.

The three-tiered approach has been codified in articles 29b-29h of the Vpb. In addition, the State Secretary for Finance issued a Ministerial Regulation<sup>[66]</sup> providing further rules regarding the form and content of the CbC report, Master File and Local File. Generally speaking, articles 29b-29h of the Vpb and the Ministerial Regulation provide supplementary requirements, in addition to article 8b of the Vpb.

Decree No. 2018-6865 offers some additional insight into the Dutch transfer pricing documentation requirements.<sup>[67]</sup> In particular, it clarifies that if a Dutch taxpayer prepares documentation in accordance with article 29g of the Vpb, the taxpayer will have to also comply with the (original) Dutch transfer pricing documentation requirements from article 8b of the Vpb. It is noted that the original documentation requirements have a broader reach, covering both cross-border and domestic transactions. For instance, the new requirements under article 29 for qualifying taxpayers pertain to cross-border transactions and the allocation of profits to permanent establishments.

The transfer pricing documentation for corporate income tax purposes can in principle be applied for customs purposes as well. As indicated in the previous paragraph, transfer pricing documentation is used in practice in the Netherlands when justifying the acceptability of the transaction value method by demonstrating that the "circumstances of sale test" is met. In other words, when there are grounds for considering that the relationship influenced the price, the relevant aspects of the transaction have to be examined, including the way in which the parties organize their commercial relations and the way in which the price in question was arrived at, in order to determine whether the relationship influenced the price.

Where it can be shown that the related parties buy from and sell to each other as if they were not related, this would demonstrate that the price had not been influenced by the relationship and Customs needs to accept the transaction value method.

In this context it is relevant that the customs regulations give some examples of how it can be demonstrated that the pricing has not been influenced by the relationship:

- the price is settled in a manner consistent with the normal pricing practices of the industry in question; and/or
- the price is adequate to ensure recovery of all costs plus a profit which is representative of the firm's overall profit realized over a representative period of time in sales of goods of the same class or kind.

When referring to the first example, the arguments to demonstrate that the circumstances of sales test is satisfied can be further supported with transfer price documentation. This would be done in order to indicate that the prices between the seller and buyer (importer of the goods) are settled in a manner consistent with the normal pricing practices of the industry in question. For example:

<sup>66</sup>. Regulation of the Under Minister of Finance of 30 Dec. 2015, No. DB/DB/2015/463 M, Regulation supplementary documentation requirements transfer pricing.

<sup>67</sup>. Decree of 22 Apr. 2018, No. 2018-6865 art. 13, available at <https://zoek.officielebekendmakingen.nl/stcrt-2018-26874.html> (accessed 18 July 2022).



- Based on the transfer pricing documentation it could be indicated that, if applicable, the seller operates a consistent transfer pricing policy for its products to set its prices on an arm's length basis to satisfy the OECD Guidelines. These Guidelines state that the transactions between related parties satisfy the arm's length standard when they take place under the same conditions, and at the same price, that would apply if the parties were unrelated.
- A transfer price study could be conducted as a basis for the pricing policy in place to compare the companies' transfer pricing policy with situations in the industry in question involving independent parties that engage in comparable transactions on substantially the same terms.
- It could be demonstrated that the pricing agreements between the seller and the buyer are made in conformity with the transfer pricing policy, which means that the transactions between the seller and buyer take place in such a way that would also apply if these parties were unrelated.

Where transfer pricing documentation for corporate income tax purposes is often analysed and used for customs purposes to examine the circumstances of sales test, this approach can in particular be successful, to the extent that such transfer pricing documentation really covers specific individual transactions/product types. However, the transfer pricing regulatory framework for corporate income tax purposes recognizes that it may not always be possible to apply the arm's length principle on a transaction-by-transaction basis. Sometimes, there may be a need for aggregating transactions in specific circumstances, for instance when an enterprise is engaged in a large number of rather similar transactions. An evaluation on a transaction-by-transaction basis could be difficult to apply and this may justify an evaluation on the basis of combined transactions.

The OECD Guidelines also specifically address the issue of whether separate or combined transactions need to be evaluated. Although it is stated that the arm's length principle should ideally be applied on a transaction-by-transaction basis, it is recognized that certain transactions are so closely linked "that they cannot be evaluated on a separate basis".<sup>[68]</sup> For this purpose, the OECD Guidelines provide the example of pricing a range of closely linked products (e.g. in a product line) when it is impractical to determine pricing for each individual product or transaction.<sup>[69]</sup> Furthermore, "such transactions should be evaluated together using the most appropriate arm's length method or methods".<sup>[70]</sup> The OECD Guidelines also recognize the fact that the price for tangible property may cover some accompanying services.<sup>[71]</sup> Generally speaking, tangible property transactions could be evaluated on a combined basis with service transactions, if the products and services are so closely linked that it would be impractical to price them separately. The products and services should then be intertwined from a commercial and economic perspective.

Customs authorities can have objections to using combined transactions (or profit-based transfer pricing methods) since this may not distinguish or sufficiently demonstrate the at arm's length pricing of the individual product categories/types. This is based on the concept that there are many different import duty rates which are product specific. This could imply that the evaluation of a transfer pricing policy and agreement for a range of linked products in a product line can be satisfactory ("at arm's length") for corporate income tax purposes. However, on an individual product level the customs authorities may argue – for example, based on the customs value of comparable imported products in the industry or high margins on certain products – that the price of some (low-taxed) products is too high and the price of other (high-taxed) products is too low from a customs perspective, in the absence of further clarifications on the transfer pricing policy for the individual products.

This means that transfer pricing documentation for corporate income tax purposes can probably best be used for customs purposes if transactions are analysed on a stand-alone basis, instead of an aggregated basis. This does not take away the fact that the customs authorities normally give the transfer pricing documentation careful consideration in their examination of the circumstances surrounding the sale. Nonetheless, there still is some lack of clarity and consensus regarding the alignment of customs and transfer pricing values and documentation requirements.

In June 2011, the WCO Council approved Commentary 23.1: Examination of the expression "circumstances surrounding the sale" under article 1.2 (a)<sup>[72]</sup> in relation to the use of transfer pricing studies. This Commentary endorses the use of transfer pricing studies to support customs valuation of transactions between related parties. It seeks to provide guidance on how importers can use this transfer pricing documentation, prepared in accordance with the OECD Guidelines, as a basis for examining the circumstances surrounding the sale for customs valuation purposes. As such, Commentary 23.1 allows for certain economic principles used by the OECD to support the application of the transaction value.

The Commentaries from the TCCV are not binding on any jurisdiction, but the pronouncements from the TCCV are regularly cited by customs authorities worldwide. The Dutch customs authorities are known to make careful considerations in their valuation

<sup>68.</sup> Para. 3.9 *OECD Guidelines*.

<sup>69.</sup> Para. 3.9 *OECD Guidelines*.

<sup>70.</sup> Para. 3.9 *OECD Guidelines*.

<sup>71.</sup> Para. 3.11 *OECD Guidelines*.

<sup>72.</sup> Art.1.2 (a) WTO Customs Valuation Agreement is equivalent to art. 134(1) UCC as applied in the Netherlands.



analysis and take into account principles laid down by the WTO Customs Valuation Agreement and valuation commentaries when making their assessments.

In practice, the Dutch customs authorities often allow transfer pricing documentation to be used as part of the substantiation of the customs value. The Dutch customs authorities are aware of the interdependencies between transfer pricing and customs valuation and thus normally take this into consideration. In particular the traditional transaction transfer pricing methods can be applied more directly for this purpose. Where there is insufficient information available, the Dutch Customs Handbook indicates that in these situations the transactional profit-based transfer pricing methods are also relevant to take into consideration in assessing the correct customs value. More specifically, there is an obvious preference for a true transactional approach like the CUP method, but it is recognized that in practice the TNMM is often used. In this sense, the Dutch authorities were already operating in line with Commentary 23.1 even before this was officially approved in 2011. Nevertheless, in more complicated cases it is advisable to seek prior approval with the customs authorities.

## 5. Use of Customs Documentation for Transfer Pricing Purposes

It is not common practice for the Dutch tax authorities to examine customs documentation. The most likely review (or joint review) would take place as part of the joint teams that the authorities have in both Amsterdam and Rotterdam. However, since the Dutch transfer pricing documentation requirements are extensive and in line with the OECD requirements, there is no particular need or incentive to review customs documentation. However, if there are particular concerns (e.g. a disparity between a rejection of the CUP versus applying an identical/similar goods approach for customs purposes), then there could be a reason to review the customs documentation files. Thus, in practice, the most likely scenarios for a review of customs documentation would be triggered by scrutiny around the selection of the most appropriate transfer pricing method as part of a tax audit.

## 6. VAT or GST Treatment of Transfer Pricing

### 6.1. Open market value or arm's length price

Article 72 of the VAT Directive introduces the "open market value". This open market value reflects the amount that a customer would have to pay for a good or a service, under conditions of fair competition, to a supplier at arm's length. In order to prevent tax evasion or avoidance, EU Member States may determine that the taxable amount for VAT purposes is the open market value, in respect of supplies of goods or services involving related entities. This open market value principle was not adopted by the Netherlands. In the Netherlands, the taxable amount is the price that has been agreed between two parties (also if those parties are related to each other).

### 6.2. Impact of adjustments

The VAT implications of TP adjustments have not been defined in EU/Dutch VAT legislation. In principle, the general rules as regards the supply of goods or services apply. For VAT purposes, the taxable amount for the supply of goods or services is based on the consideration actually received by the supplier. In order for an adjustment to have VAT implications, it must constitute a consideration in exchange for a taxable supply of goods or services that was made. If this is the case, the adjustment leads to a decrease or increase in the VAT taxable amount of that transaction, which may have an impact on initially filed VAT returns. The TP adjustment is, as such, regarded as an adjustment to the price already paid in exchange for a supply of goods or services. If there is no link between the adjustment and a specific supply of goods or services, there are arguments to say that the adjustment has no impact for VAT purposes at all. This, however, strongly depends on the actual facts and circumstances and the possibility to link the adjustments to a specific number of transactions.

For imports into the European Union, for the levying of import VAT, the taxable amount is based on the customs value. To determine the VAT impact of TP adjustments made in respect of imported goods, the question should be raised whether the adjustment leads to a decrease or increase in the customs value of the imported goods. The import VAT treatment will follow that customs valuation treatment.

### 6.3. Cooperation between competent authorities

For import VAT, the Dutch customs authorities are the competent authorities, while, regarding VAT, the Dutch tax authorities are the competent authorities. As import VAT is levied by the Dutch customs authorities, when an audit covers TP adjustments and the impact on the customs value, the impact on the import VAT will also be taken into account.

Within the Netherlands, there continues to be increasing interaction between the tax and customs authorities (see section 3.3.). However, there is no publicly available information about whether or not there is an exchange of information between the two authorities and between the different departments of the tax authorities.

## 7. Case Studies

### 7.1. Case Study 1

#### Facts

Assume the following scenario. Exquisite Cosmetics is a US group. The companies in this group develop, manufacture and distribute cosmetics. One of their products is an anti-wrinkle cream registered under the trademark Pure Magic. LocalCo is a company resident in the Netherlands, and a distributor of Pure Magic. LocalCo purchased Pure Magic from ForeignCo, a related company in Country X. LocalCo furthermore distributes a product called Simply Magical, which is also an anti-wrinkle cream and was purchased from a non-related party in Country X.

LocalCo performs the same functions in respect of Pure Magic and Simply Magical. The gross profit margins of LocalCo on both products were 25%.

ForeignCo owns a trademark on Pure Magic. On the importation of Pure Magic, LocalCo makes a payment to ForeignCo. The payment is specified to be 25 cents per unit. ForeignCo licensed the trademark to four unrelated licensees in Countries A, B, C and D. The licensees of Countries A and B paid a fee of 25 cents per unit. The licensees of Country C paid 30 cents per unit. LocalCo's transfer pricing documentation shows that the trademark fee is based on the comparable uncontrolled price (CUP) method.

#### Questions and answers

1. *Based on the above facts, would the RPM be acceptable for transfer pricing purposes, and why? What factors are critical in making this judgement? Would the CUP method used in the above scenario be acceptable?*

The RPM may be applicable in the Netherlands to establish the arm's length nature of the transfer prices between ForeignCo and LocalCo for the supply of Pure Magic. However, there is an important comparability difference in the sense that LocalCo needs to pay royalties for the Pure Magic product. This may either mean that the RPM is not applicable (or the comparables should be adjusted) and that the transactional net margin method is more applicable, or it may question the arm's length nature of the royalty payments. After all, LocalCo is a mere buy-sell distributor which typically does not pay royalties. The CUP method on the product supplies would most likely not be possible if Pure Magic and Simply Magical have different prices on the market.

2. *If there were to be a tax audit, would the tax authorities in the Netherlands make an adjustment? And if so, why and based on what?*

Further to the above question, denying deductibility on the royalty payments could be a potential adjustment scenario in the Netherlands. Alternatively, the gross margin could be adjusted in such a way that it would be increased to compensate for the royalty payment.

3. *Based on the above facts, which valuation method would be acceptable for customs purposes, and why? Which customs method would be used, and which factors are critical in making this judgment?*

The transaction value method of article 70 of the UCC<sup>[73]</sup> is the preferred customs valuation method. In this situation the transaction value method is in principle the appropriate starting point for establishing the customs value of both products (Pure Magic and Simply Magical).

Simply Magical is purchased from an unrelated vendor and assuming that a sale for export to the Netherlands is made by the third-party vendor to LocalCo, there would in principle not be any reason to reject the application of the transaction value method.

With respect to the purchases of Pure Magic, an additional consideration to take into account when applying the transaction value method is that LocalCo buys the product from a related seller, i.e. ForeignCo. Based on article 134(1) of the UCC IA,<sup>[74]</sup> the declarant should be given an opportunity to supply further detailed information regarding the circumstances surrounding the sale; for the customs authorities to be able to determine whether the relationship between LocalCo and ForeignCo influenced the price. The circumstances of sale test or alternate test values mentioned in article 134(2) can be used to demonstrate that LocalCo and ForeignCo buy from and sell to each other as if they were not related. This would demonstrate that the price had not been influenced by the relationship and the transaction value method should be accepted by Customs.

73. Regulation (EU) No 952/2013 of 9 October 2013.

74. UCC IA.

Further, the trademark payment made by LocalCo to ForeignCo on the importation of Pure Magic will in principle be considered dutiable when the customs value is determined under the transaction value method. Based on article 71(1)(c) of the UCC, separate royalty or licence fee payments of 25 cents per unit shall be added to the price actually paid or payable when these payments relate to the goods being valued and if LocalCo must pay them as a condition of sale.<sup>[75]</sup> This seems to apply to the transactions between ForeignCo and LocalCo.

Under the old EU customs legislation, a specific provision applied in determining whether trademark payments should form part of the customs value.<sup>[76]</sup> The UCC does not contain an equivalent of that provision. This means that under the UCC, no distinction is made with respect to the specific right (i.e. trademark or other) for which the royalty payment is made. The provisions of the UCC regarding the dutiability of royalties are more in line with those of the GATT which only constitute the condition of sale rule. As a result, it needs to be tested whether the trademark royalty is considered a condition of sale for the imported goods. Article 136(1) (4) of the UCC IA gives three circumstances in which the condition of sale is met:

- the seller or a person related to the seller requires the buyer to make the payment;
- the payment by the buyer is made to satisfy an obligation of the seller, in accordance with contractual obligations; or
- the goods cannot be sold to, or purchased by, the buyer without payment of the royalties or licence fees to a licensor.

In order to determine whether one of these conditions is met, the royalty agreement between ForeignCo and LocalCo must be examined. It is likely that the royalty payment constitutes a condition of sale and therefore should be included in the customs value of the imported goods.

*4. Would the answers to the above questions be different if LocalCo were to be paid on a resale minus or a cost-plus basis?*

From a customs perspective, the answers given to the above question would not be different if LocalCo were to be paid on a resale minus or cost-plus basis. The transaction value method will still be the preferred customs valuation method for the purchases of Simply Magical and Pure Magic. With respect to the purchases of Pure Magic, the requirement for applying the transaction value method continues to be that the relationship between ForeignCo and LocalCo does not influence the price. From a transfer pricing perspective, the cost-plus method does not appear appropriate to establish an arm's length price for distributors (based on both Dutch and OECD guidance).

## 7.2. Case Study 2

### Facts

Assume the following scenario. LocalCo is resident in the Netherlands and purchased a mixture of natural ingredients used in the production of Pure Heaven. Pure Heaven is an organic ice cream produced by ForeignCo, a company located in Country X. LocalCo claims it produces ice cream using only natural ingredients.

At the time the goods were cleared, LocalCo declared to the customs authorities in the Netherlands that it (LocalCo) was related to ForeignCo. After importation, the customs authorities in the Netherlands decided to conduct a review of the circumstances with respect to the sale of goods between LocalCo and ForeignCo. The customs authorities have some reservations about the price. They made enquiries about the sale of products by ForeignCo to other buyers in the Netherlands and, if relevant, any reasons for a difference in price. The customs authorities forwarded the questions to ForeignCo.

The mixture of natural ingredients was acquired by ForeignCo from other manufacturers. It is neither manufactured nor processed by ForeignCo. In the Netherlands, LocalCo is the only person to whom the mixture of natural ingredients is sold. ForeignCo does not sell any other goods.

There are four sellers of synthetic ingredients in Country X. These ingredients are added to ice cream for the same reason as the mixture of natural ingredients used by LocalCo. The synthetic ingredients are acquired from other manufacturers.

LocalCo provided the customs authorities with a transfer pricing study. The cost-plus method was used. According to the information provided by LocalCo, the profit margin on the sale of synthetic and natural ingredients is more or less the same.

The functions performed by ForeignCo and the four sellers of the synthetic ingredients are more or less the same. None of these entities have inventories or significant assets. In addition, the risks assumed were broadly the same.

<sup>75.</sup> See also art. 136 UCC IA.

<sup>76.</sup> Under art. 159 CCIP, a royalty or licence fee in respect of the right to use a trademark was only to be added to the price actually paid or payable for the imported goods where: (i) the royalty or licence fee referred to goods which were resold in the same state or which were subject only to minor processing after importation; (ii) the goods were marketed under the trademark, affixed before or after importation, for which the royalty or licence fee was paid; and (iii) the buyer was not free to obtain such goods from other suppliers unrelated to the seller.

The contractual terms in transactions between the sellers and unrelated buyers are broadly the same as those between ForeignCo and LocalCo.

In the relevant tax year, the cost-plus markup of ForeignCo in its transactions was 20%. The four sellers used the following markups in transactions with unrelated buyers in the Netherlands:

- Seller 1: 23%.
- Seller 2: 20%.
- Seller 3: 17%.
- Seller 4: 15%.

### Questions and answers

1. *Based on the above facts, would the cost-plus method be acceptable for transfer pricing purposes, and why? What factors are critical in making this judgement?*

The cost-plus method may be applicable in the Netherlands – especially since ForeignCo operates as a supplier and LocalCo acts as the entrepreneur in the Dutch market. The CUP method may not be applicable due to product differences – especially in view of the importance of natural ingredients for LocalCo.

2. *If there were to be a tax audit, would the tax authorities in the Netherlands make an adjustment?*

The facts and circumstances do not offer a lot of ground for any tax adjustment. The applicable markup is fairly consistent with the identified comparables. Thus, a tax adjustment as such seems unlikely.

3. *Based on the above facts, which customs valuation method would be used, and what factors are critical in making this judgment?*

In this situation, the transaction value method is in principle the appropriate starting point for establishing the customs value of the mixture of ingredients.<sup>77</sup> The fact that LocalCo and ForeignCo are related parties for customs purposes is not a reason to consider the transaction value method unacceptable. However, Customs has the right to examine the circumstances surrounding the sale and Customs needs to accept the transaction value method if the relationship has not influenced the price. If it can be shown that LocalCo and ForeignCo buy from and sell to each other as if they were not related, this would demonstrate that the price had not been influenced by the relationship. As an example of how this can be established by the customs authorities, article 134(2) of the UCC indicates that it needs to be demonstrated that the price of the imported mixture of ingredients should be settled in a manner consistent with the normal pricing practices of the industry in question. The transfer pricing study provided by LocalCo to the customs authorities can further support this position. Based on the available data on cost-plus markup, profit margin, functions and contractual terms in transactions between comparable sellers and unrelated buyers in this industry, it seems that the transactions between ForeignCo and LocalCo take place in such a way that would also apply if these parties were unrelated and therefore the price would not be influenced by the relationship.

4. *Would it make a difference if ForeignCo were to manufacture a mixture of the natural ingredients? If so, in what way?*

From a customs perspective the answers given above would not be very different if ForeignCo produced the mixture itself, albeit that the transfer pricing documentation and applicable transfer pricing method may be different. The procedure – steps in the process and arguments presented to the customs authorities – for justifying the transaction value method can be the same. The customs authorities can examine the situation to see that the relationship has not influenced the price in order to allow LocalCo to use the transaction value method. LocalCo can present the transfer pricing documentation to the customs authorities in order to support its argument that the “circumstances of sale test” is met. Purely from a transfer pricing perspective, if ForeignCo were to be a producer, the comparison with the independent sellers is arguably less appropriate.

77. Different interpretations are possible with regard to the *Hamamatsu* judgment of the ECJ (DE: ECJ, 20 Dec. 2017, Case C-529/16, *Hamamatsu Photonics Deutschland GmbH v. Hauptzollamt München*, Case Law IBFD). One interpretation is that where a transfer price is used which can be adjusted retroactively, the transfer pricing method cannot be used to determine the customs value of the imported goods. The EC is currently still discussing the *Hamamatsu* judgment and is expected to issue a guidance. It is not yet known when such guidance will be issued.