

The curious case of "SA 38945" and its political button ...





The Story Begins on 19 June 2013...
(maybe somewhere over 11 o'clock)

... when “the European Commission sent a letter to Luxembourg requesting information about its tax ruling practice”.

In the following months, the Commission sent additional requests for information regarding the ruling in favour of the **Amazon Group**, **Fiat group**, **GDF Suez group**, and the **McDonald’s group**.

These all will become “ad hoc state aid (S.A.) cases regarding tax base reduction”

In 2014-2016, Brussels sent new letters, regarding all four cases, having in the end the same new (old?) story: “In light of the foregoing considerations, the Commission’s preliminary view is that the tax ruling by Luxembourg in favour of (...) constitutes State aid within the meaning of Article 107(1) TFEU and the Commission has doubts at this stage as to that ruling’s compatibility with the internal market. The Commission has therefore decided to initiate the procedure laid down in Article 108(2) TFEU with respect to that measure ...”

After “in-depth” investigations, in the name of the TFEU ...

30 mil. euro
at stake

SA.38375, decision Oct. 2015 The tax ruling (on transfer pricing) issued by Luxembourg on September 2012 in favour of **Fiat Finance and Trade Ltd.**, which enables the latter to determine its tax liability in Luxembourg on a yearly basis for a period of five years, ...

250 mil.
euro

SA.38944, decision Oct. 2017: “The tax ruling of November 2003 by virtue of which Luxembourg endorsed a transfer pricing arrangement proposed by **Amazon.com, Inc.** that allowed Amazon EU S.á.r.l. to assess its corporate income tax liability in Luxembourg from 2006 to 2014 and the subsequent acceptance of the yearly corporate income tax declaration based thereon...

120 mil
euro

SA.44888, decision June 2018: The State aid granted in favour of **Engie S.A. (ex GDF)**, and all companies directly or indirectly controlled by Engie S.A. on the basis of the tax ruling (concerning intragroup transactions) from 2008-2012 issued by the Luxembourg tax administration ...

... “constitutes aid within the meaning of Article 107(1) of the Treaty on the Functioning of the European Union that is incompatible with the internal market and that was unlawfully put into effect by Luxembourg in breach of Article 108(3) of the Treaty on the Functioning of the European Union. ... Luxembourg shall recover the incompatible and unlawful aid from companies) ...”

But another "in-depth" investigation, another tax base reduction, even a double non-taxation case ...

SA. 38945, **opening case decision December 2015** : "For all the foregoing reasons, the Commission considers, at this stage, that the tax ruling issued by the Luxembourg tax administration on 17 September 2009 in favour of McDonald's Europe constitutes State aid within the meaning of Article 107(1) TFEU. (...) The Commission considers that the revised tax ruling appears to result in a reduction of charges that should normally be borne by the entity concerned in the course of its business, and should therefore be considered as operating aid. According to Commission practice, such aid cannot be considered compatible with the internal market in that it does not facilitate the development of certain activities or of certain economic areas, nor are the incentives in question limited in time, digressive or proportionate to what is necessary to remedy to a specific economic handicap of the areas concerned".



.. "Following an in-depth investigation launched in December 2015, based on doubts that Luxembourg might have misapplied its Double Taxation Treaty with the United States, the Commission has concluded that Luxembourg's tax treatment of McDonald's Europe Franchising does not violate the Double Taxation Treaty with the United States. On that basis the tax rulings granted to McDonald's do not infringe EU State aid rules...."

(Press Release, September 2018- The public version of the final decision is not yet available).

AND A VERY VERDICT ... ANTICLOCKWISE

So, good news ...

BUSINESS NEWS SEPTEMBER 19, 2018 / 12:56 PM / 5 DAYS AGO

EU says McDonald's, Luxembourg tax deal not illegal

Fan Yun Chee

(This September 19 story corrects to read Gracia, paragraph 13)

4 MIN READ



Bloomberg

Business EU Ends Tax Probe Into McDonald's With a Rare Reprieve

“Ending the McDonald’s probe comes a week before Vestager plans to meet U.S. officials and politicians in Washington amid criticism that EU investigations have often targeted successful American companies. Google has been fined about 6.7 billion euros to date and is still facing a further antitrust probe”.



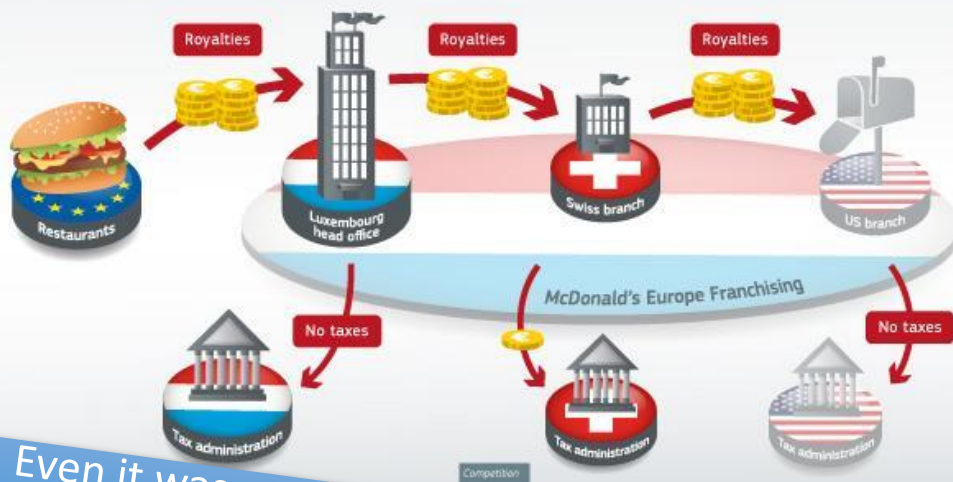
“The decision is the first formal investigation in EU competition commissioner Margrethe Vestager’s five-year crackdown on tax rulings where she concluded that an arrangement was not illegal under the EU’s state-aid rules”.

BUT ... WHY?

Three years ago, Brussels was more confident in its feelings!

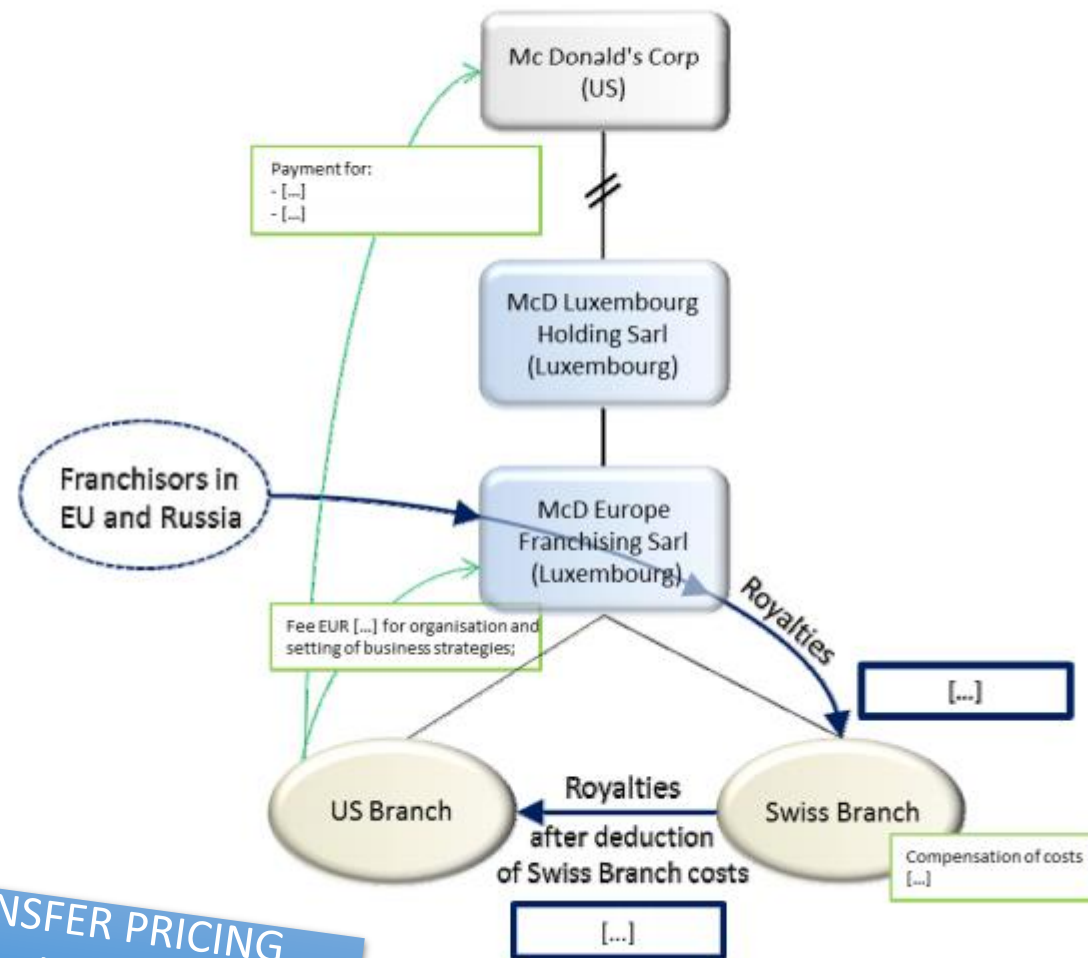
A not quite simple fiscal structure

Concern: McDonald's Europe paid tax neither in EU nor US



Even it was not much about the ...usual suspect, aka TRANSFER PRICING (it was used only one time in the entire opening case decision from December 2015)

McD Europe Franchising Sarl (2013)



Even the market has expected consistent penalties ...

"If the standard Luxembourg tax rate of 29.2 per cent applied to those earnings – following the broad principles the commission applied in the Apple case – McDonald's would owe the Grand Duchy nearly half a billion dollars".
(FT, 2016)



It's about a complex structure...

The real issue is around the role of the US branch of the McDonald's Europe.

Europe is the largest market of the US corporation McDonald's (generating USD 11 billion in 2014, against USD 8.6 billion – generated by US market). McD Europe profit in 2010-2013 is over USD 600 million, at over 3.5 billion net turnover.

In order to centralise the oversight and management of the European franchise rights, McD Europe buys-in to certain pre-existing and future developed franchise rights owned by McDonald's Corporation and its US affiliate, McDonald's International Property Company (MIPCO). As a result, McD Europe acquired beneficial ownership of a number of franchise rights intangibles. Subsequently, McD Europe allocated the franchise rights as well as the obligations to its US Franchise Branch. All royalties that were once received by McDonald's Corporation are now to be received by McD Europe through its US Franchise Branch.

This US Franchise Branch assumes various economic risks associated with the development of the franchise rights and bears associated costs. In bearing those costs, the US Franchise Branch is effectively participating in the QCS Agreement with McDonald's Corporation and MIPCO. The related activities at McDonald's Corporation (or its affiliates) that are reimbursed by the US Franchise Branch are directed and performed by employees within McDonald's Corporation. The US Franchise Branch does not employ any direct staff.

(From the decision to initiate the formal investigation procedure December 2015)

You can make easily interpretations in a way or another

In their discussions with the Luxembourg authorities, McDonald's argued that the US branch of McDonald's Europe Franchising **constituted a "permanent establishment" under Luxembourg law**, because it had sufficient activities to constitute a real US presence.

Simultaneously, McDonald's argued that its US-based branch **was not a "permanent establishment" under US law** because, from the perspective of the US tax authorities, its US branch did not undertake sufficient business or trade in the US. (According to the information submitted by Luxembourg to the Commission, the US Franchise Branch does not employ any direct staff).

As a result, the Luxembourg authorities **recognised** the McDonald's Europe Franchising's US branch as the place where most of their profits should be taxed, whilst US tax authorities **did not recognise** it. The Luxembourg authorities therefore exempted the profits from taxation in Luxembourg, despite knowing that they in fact were not subject to tax in the US. (Press release December 2015)

Usually, a double tax treaty (as that DTT between Luxembourg and United States, from 1996) states that "The business profits of an enterprise of a Contracting State shall be taxable only in that State unless the enterprise carries on business in the other Contracting State through a permanent establishment situated therein.."

And you can use a RARE accusation: "Deliberately"!

(54) [...] Whether or not the US Franchise branch constitutes a taxable presence in the US as being effectively connected to a US trade or business, i.e. whether the US actually exercises its taxing right under the DTT, is therefore irrelevant; there is no need to assess whether the nexus for taxation in the US is fulfilled (the "effectively connected to a US trade or business") under Luxembourgish law. Luxembourg knew or should have known of this assessment.

(55) Furthermore, in its tax returns for US income tax purposes, McDonalds stated that they did not have a permanent establishment for the purposes of any applicable tax treaty between the United States and a foreign country.

In the Commission's views, Luxembourg therefore deliberately granted the ruling with a tax exemption under the Luxembourg-US DTT, although having all information necessary to be aware that no taxation would take place in the US, and although it seems that the US branch would not normally fulfil the criteria under Luxembourgish law to qualify as a permanent establishment. (Decision 2015).

"You may wonder how Luxembourg can rely on a Treaty meant to avoid double taxation to endorse double non-taxation. We asked ourselves the same question, which is why we opened a State aid investigation in December 2015" (Commissioner Vestager, 2018).

No other opening case decision (Amazon, Fiat, Engie) doesn't contain "deliberately"

And despite these "Signs", Brussels is making a ...step back.

"The result was double non-taxation of the income by Luxembourg and the US. However, this was not due to any special treatment awarded by Luxembourg to McDonald's, which was the issue that our investigation under EU State aid rules focused on". (September 2018)

We can see here another message that analysing the compliancy with the TFUE has become a political tool.

If the McD ruling is not a "selective measure", then why the Fiat or Amazon, or Apple (Ireland), or Starbucks (Netherlands) should be considered as selective? In their ongoing appealing of the Commission's decisions before the EU courts, the states involved are asking the same – "where is the selective advantage?" Because, they said, the Commission failed to demonstrate this.

"It is thus well established that, for a measure to be categorised as State aid within the meaning of that provision, there must, first, be an intervention by the State or through State resources; second, the intervention must be liable to affect trade between Member States; third, it must confer a selective advantage on an undertaking and, fourth, it must distort or threaten to distort competition.

Notwithstanding the competence of the Member State over their systems of taxation, tax measures are not excluded from the scope of Article 107(1) TFEU.³²" (from the Decision 2015)

DELIBERATELY?

IT IS NOW A QUESTION OF TIME (CLOCKWISE OR NOT)!

Another strange message – it's ok to have a double non-taxation situation, but it's not welcomed to have transfer pricing arrangement (as in Fiat, Amazon, Apple etc. cases) which gave certainty to the taxpayer?

Meanwhile, Luxembourg is changing the tax rules – the Tax Authorities may request from the taxpayer (if it wants to benefit from a tax exemption in Luxembourg) a confirmation that the other Contracting State (in a DTT) recognises the existence of a permanent establishment in its territory of that taxpayer. This measure is not part of any an ad-hoc directive, but ... is “very much welcomed” by the Brussels.

One could wonder what would be the outcome of the McD Europe in the absence of the new Luxembourg tax changes? Or in the absence of this new transatlantic context (commercial and fiscal war)?

“Member States have been using the momentum to reform their corporate taxation framework, to make it both fairer and more efficient”.
(Commissioner Vestager statement, September 2018)



Variations on the same ... trend. “SA. 38945” is just another sign of how the next EU integration stage will look like, with a European Minister of Finance giving certificates for what is good or bad for the common (and less national) interest!

SO, BE WISE...

ABSOLUTELY AND DELIBERATELY,

BEPS YOUR TAX APPROACH : BE PREPARED TO SWITCH!



www.transferpricing.ro/en/i-need-to-understand-transfer-pricing