Euro Tax Flash from KPMG's EU Tax Centre

European Commission state aid announcements

State aid – Tax rulings –Transfer pricing – Profit allocation – Luxembourg – Ireland

During a press conference organized on October 4, 2017, the European Commission announced its final decision (see the Commission's Press Release) on its state aid investigations into transfer pricing rulings granted by Luxembourg to the Amazon group. In its decision the Commission rules that the rulings in question may underestimate the taxable profits of the group by deviating from the arm's length principle, and therefore constituted illegal state aid (see Euro Tax Flash 244). The Commission estimates the value of the competitive advantage granted at up to EUR 250 million, plus interest. It is up to the Luxembourg tax authorities to determine the exact amount and to recover what the Commission considers to be illegal aid.

The Commission also announced its decision to refer Ireland to the Court of Justice of the European Union (CJEU) for failure to recover up to EUR 13 billion in tax benefits deemed by the Commission as illegal state aid in August 2016 (see Euro Tax Flash 307).

Below we will summarize the main elements of the press releases issued by the Commission. It should be noted that these press releases reflect the opinion of the Commission only.

Background

The decision concerning Luxembourg follows an in-depth investigation launched in October 2014 and is part of what the Commission refers to as a wider strategy towards tax transparency and fair taxation, which has led to inquiries into the compatibility of the tax ruling practices of Member States with EU law, starting in June 2013. In December 2014, the Commission extended the information inquiry into tax rulings issued by all Member States since January 1, 2010, and in June 2015 requested 15 Member States to provide detailed information on some of their rulings. These investigations have led the Commission to conclude that Belgium (the "excess profit" tax scheme – see Euro Tax Flash 271), Luxembourg (the Fiat case) and the Netherlands (the Starbucks case) – see Euro Tax Flash 262, have granted selective tax advantages that are illegal under EU state aid rules. The Commission has also opened in-depth investigations into tax rulings issued by Luxembourg to McDonald's (see Euro Tax Flash 264) and GDF Suez (see Euro Tax Flash 302). Following the Commission's final decision in the tax ruling granted by Ireland to Apple (see Euro Tax Flashes 300 and 307), both Ireland and Apple have filed appeals with the General Court of the EU. In this case the United States have filed a request with the General Court to be permitted to submit a position paper in the procedure.

The Commission is required by EU law to review state aid granted by Member States and, if it finds that the aid is incompatible with the internal market, to order the Member State concerned not to put it into effect, or to abolish or alter it. The Member State is also required to recover the aid from the beneficiary within a prescribed timeframe in order to remove the distorting effect on competition. Broadly speaking, aid is incompatible with EU law if it distorts competition by, for example, selectively favoring certain undertakings thus affecting trade between Member States, provided that it does not meet the conditions for Commission approval under the EU Treaty.

The Decision

The decision concerns a tax ruling granted by Luxembourg in respect of the method to calculate the taxable base of an operating company of the Amazon group. In the Commission's view, the tax ruling indirectly endorsed the method used to calculate payments made – in exchange for the rights to use Amazon intellectual property – to a Luxembourg-incorporated holding company, which is also part of the group. According to the Commission, its investigation did not challenge the holding company's ownership of such intellectual property, but only the level of the payments, particularly in proportion to what the holding company paid to the US parent company under the group cost-sharing agreement. Furthermore, this investigation did not concern the wider group structure, but only focused on the tax treatment of the aforementioned companies established in Luxembourg. The Commission found that the payments reduced the profits of the operating company to "a quarter of what they were in reality", which, the Commission considered, is what enabled the company to pay less tax than other companies. The Commission therefore concluded that the tax treatment given by Luxembourg to Amazon under the investigated tax ruling is illegal under EU State aid rules.

The decision requires Luxembourg to determine the exact amount of unpaid tax in Luxembourg on the basis of the methodology established by the Commission and recover the amount thus determined from Amazon. The Commission has estimated the difference between what the operating company paid in taxes and what it would have been liable to in the absence of the disputed tax ruling at around EUR 250 million, plus late payment interest which would have to be determined on the basis of domestic legislation (no penalties apply under EU State aid rules).

The case against Ireland

The Commission also announced its decision to refer Ireland to the CJEU for failure to recover an estimated EUR 13 billion in following the Commission's decision in the Apple case. The deadline for Ireland to implement the Commission's decision was January 3, 2017 (four months from the official notification on the decision). Although Ireland has made progress in determining the exact amount to be recovered and in setting up an escrow account in which the recovered amount is to be placed pending the outcome of the CJEU procedure, according to the Commission the Member State is only planning to finalize the process by March 2018.

EU Tax Centre comment

The Luxembourg Ministry of Finance o has acknowledged the Commission's decision in a statement issued on the same day, noting that "Luxembourg will use appropriate due diligence to analyse the decision and reserves all its rights." The statement also notes that Amazon was taxed in accordance with the tax rules in force at the time, which have evolved since in line with Luxembourg's commitment to tax transparency, the fight against harmful tax avoidance and the OECD BEPS project – Luxembourg is a member of the OECD Inclusive Framework on BEPS.

It is perhaps noteworthy that the Commission sees its tax-related state aid investigations as being part of the wider strategy towards fair taxation and greater transparency, which include the automatic exchange of information on tax rulings and country-by-country reports, the Anti-Tax Avoidance Directive, on-going work on the C(C)CTB proposals and the proposed mandatory disclosure requirements for intermediaries.

Should you have any queries, please do not hesitate to contact KPMG's EU Tax Centre, or, as appropriate, your local KPMG tax advisor.

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