

How to fight state aid cases through a full VCA: Starbucks and Apple cases

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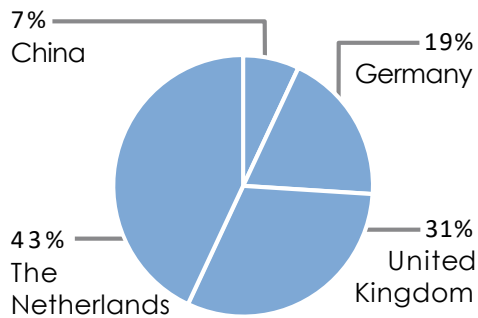
Amsterdam, the Netherlands

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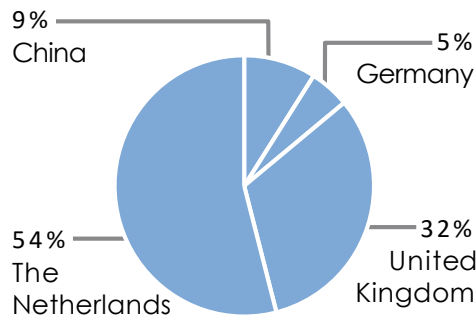
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VCA Agenda: Alignment Between Operating Margin, Sales and FTEs

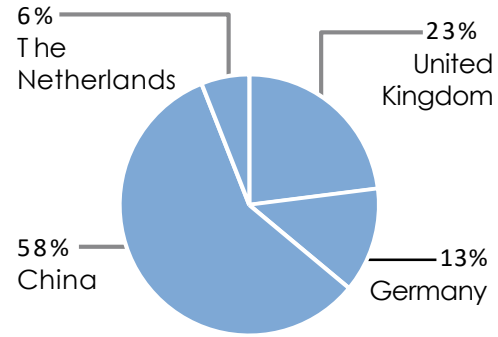
Operating Margin (OM) Ratio
Country OM to Total Group OM



Sales Ratio
Country Sales to Total Group Sales



Full Time Employee (FTE) Ratio
Country FTEs to Total Group FTEs



Misalignment is visible when expressed as the ratio of country and total group for operating margin, sales and FTEs. The higher the delta, the greater the need to provide explanations to the Tax authorities.

VCA - Example

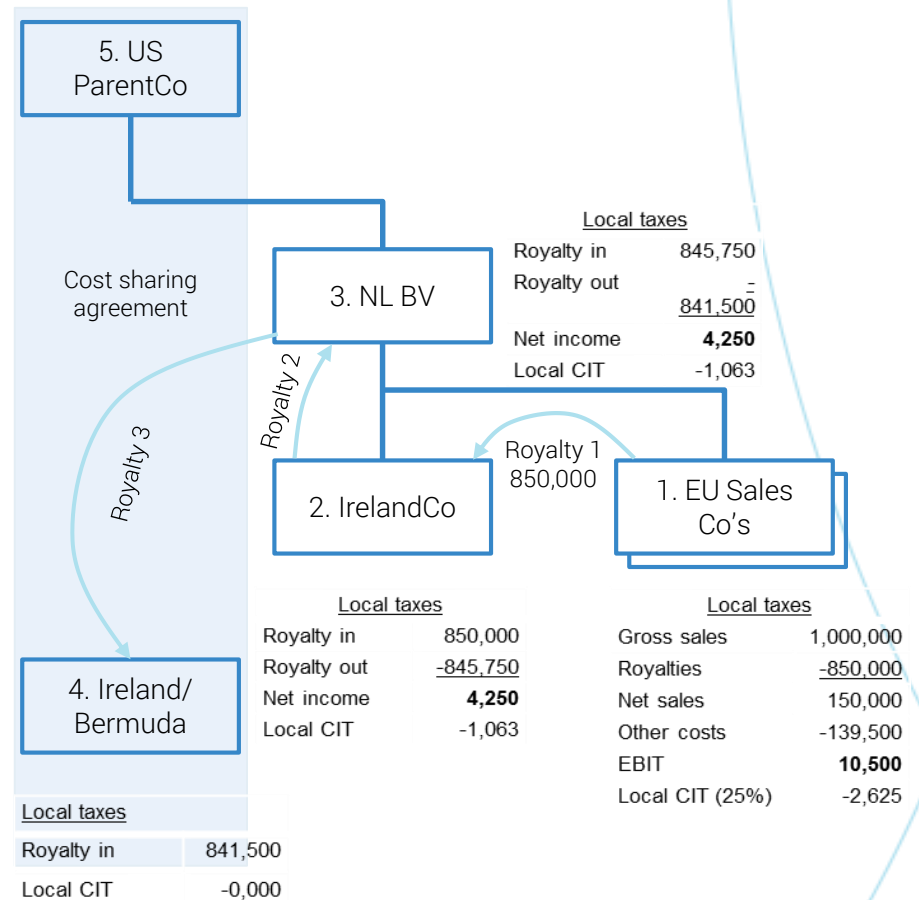
An example of conducting a value chain analysis based on technique 1 is presented below:

It can be seen from the pie charts that only 6% of FTEs reside in the Netherlands who contribute 54% of Group Sales and 43% of Operating Margin, while 23% of FTEs reside in the UK who contribute 32% of Group Sales and 31% of Operating Margin in an MNE.

This, at the very outset, will at least lead to a question from the tax authorities on such discrepancy. Thus, the MNE should include an explanation (derived from conducting a value chain analysis) of such circumstances in its tax/TP documentation(s) and returns.

Apple case in VCA context

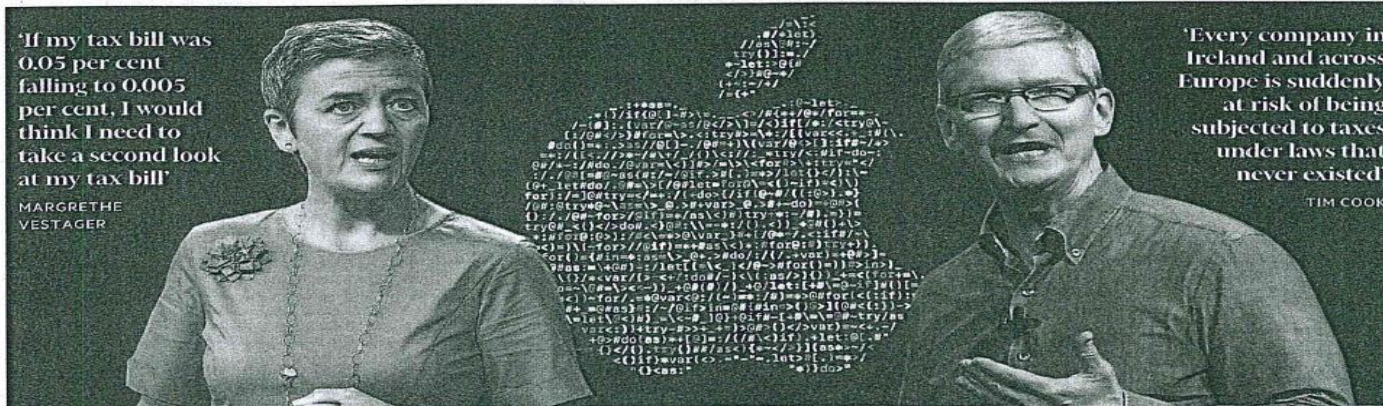
The reduction of the effective tax burden, theoretically	
1. IrelandCo receives royalties assumed	850,000
Assumption: 0.5% remains in Ireland based on an APA	-4,250
2. The Netherlands receives royalties	845,750
Assumption: 0.5% is paid in The Netherlands	-4,250
3. Net to Ireland/Bermuda	841,521
4. Drop taxable basis to $19,000 / 1,000,000 * 100\% =$	1.9%



— = 100% ownership

Brussels' €13bn tax bill clears way for further crackdowns on Apple

◆ Dublin ordered to claw back cash ◆ Vestager urges other authorities to examine figures



ALEX BARKER AND ARTHUR BEESLEY BRUSSELS

Brussels has opened the door for European and US revenue authorities to claim a share of its €13bn recovery order from Apple after declaring the company's Irish tax regime unlawful.

The European Commission ordered Ireland to claw back a record-breaking tax bill after finding the US tech group enjoyed a quarter of a century of illegal state support — prompting a furious response from Apple and Washington.

Margrethe Vestager, competition commissioner, accused the world's biggest company by market value of side-stepping taxes by channelling most of its non-US sales and profits through artificial corporate entities not required to pay tax anywhere.

"If my tax bill was 0.05 per cent, falling to 0.005 per cent, I would think I need to have a second look," she said, referring to the effective rate of tax paid

Tim Cook has condemned Margrethe Vestager's ruling as threatening the principle of legal certainty in Europe

AFP/Getty Images

by a key Apple unit in Ireland. The ruling sets the stage for a bruising transatlantic political tussle over the taxation of US multinationals, the alleged targeting of Silicon Valley by the EU authorities and the reach of Brussels into national tax policy.

In an open letter to Apple customers, Tim Cook, chief executive, said the ruling threatened to deal a "devastating blow" to the principle of legal certainty in Europe. "We never asked for, nor did we receive, any special deals. We now find ourselves in the unusual position of

being ordered to retroactively pay additional taxes to a government that says we don't owe them any more than we've already paid."

The US Treasury said the "commission's actions could threaten to undermine foreign investment, the business climate in Europe, and the important spirit of economic partnership between the US and the EU".

The huge bill for back taxes is at the extreme end of expectations and came with an open invitation to European tax collectors to review Apple's business in their jurisdictions. Ms Vestager suggested that tax authorities in other European countries and the US examine how Apple booked sales, profits and royalty payments in light of her findings. Such reviews could lead to increased Apple tax payments in other jurisdictions.

Apple and Ireland are preparing separate appeals in the European courts.

These could take years to conclude. Dublin has been directed to calculate Apple's tax liability in line with the ruling, including interest that Peter Vale of Grant Thornton in Dublin estimated at some €6bn.

"I disagree profoundly with the commission's decision," said Michael Noonan, Irish finance minister. "Our tax system is founded on the strict application of the law, as enacted by [parliament], without exception."

In its long-delayed decision, however, the commission argued that Apple's structure in Ireland "did not correspond to economic reality".

Almost all profits from Apple's non-US sales were attributed to a "head office" in its Irish subsidiaries. But Brussels found these existed "only on paper" and could not have generated the profits they received.

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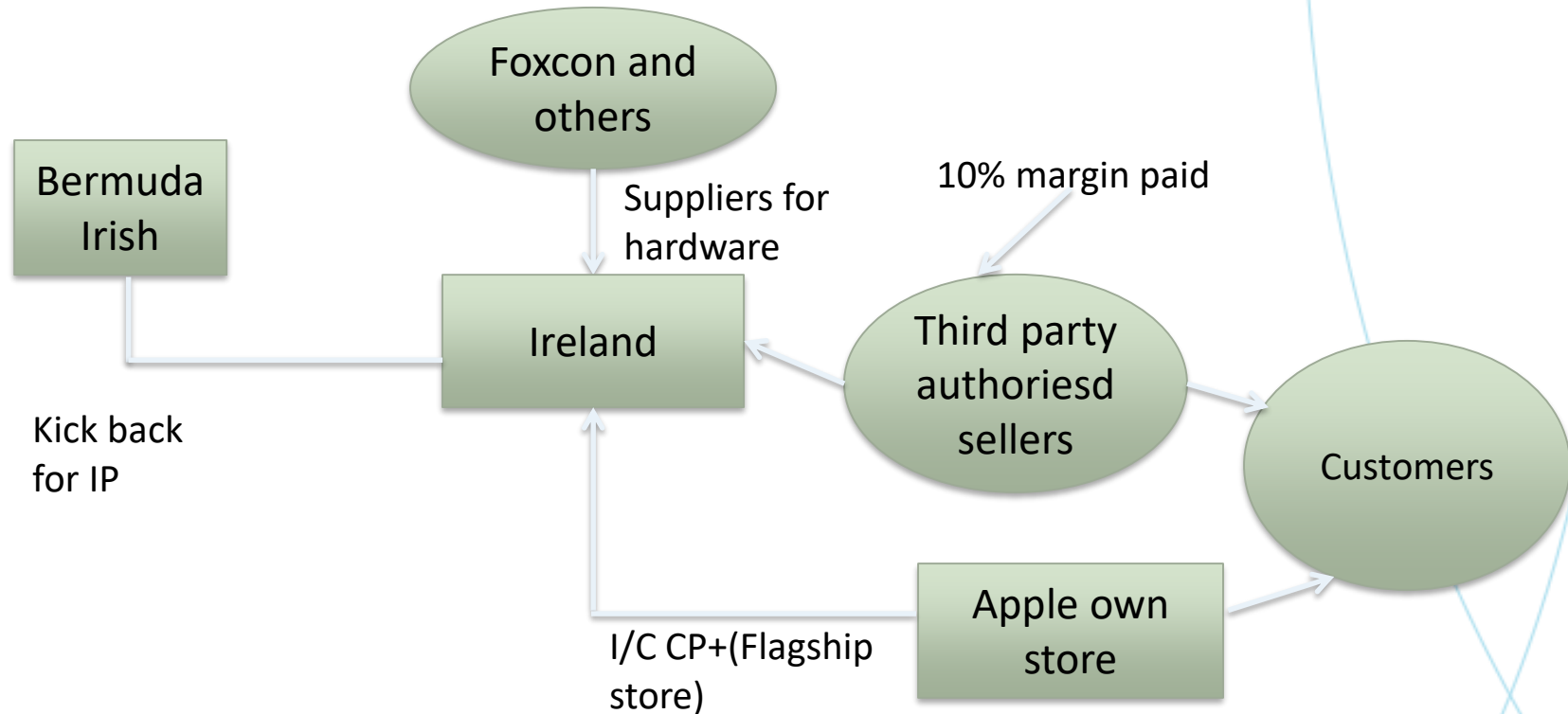
Apple's punishment is unprecedented in its harshness — and at the same time a much better deal than it could have expected to get in the US

Apple case in VCA context

-Views on Apple Case

1. The 841,500 (royalty income) at the level of Ireland/ Bermuda will be taxed upon repatriation to the USA.
2. The 841,500 (royalty income) at the level of Ireland/ Bermuda should have been taxed in various EU countries.
3. The EU “state-aid” assessment protects all taxpayers against individual taxpayers receiving a preferential tax treatment (selective economic benefit), i.e. does not address the statements made under 1 and 2 above.
4. The EU should introduce a special tax on digital economy trade, since companies such as Apple generate taxable profits in Europe without having to build a traditional significant presence, to strengthen the EU taxable base.

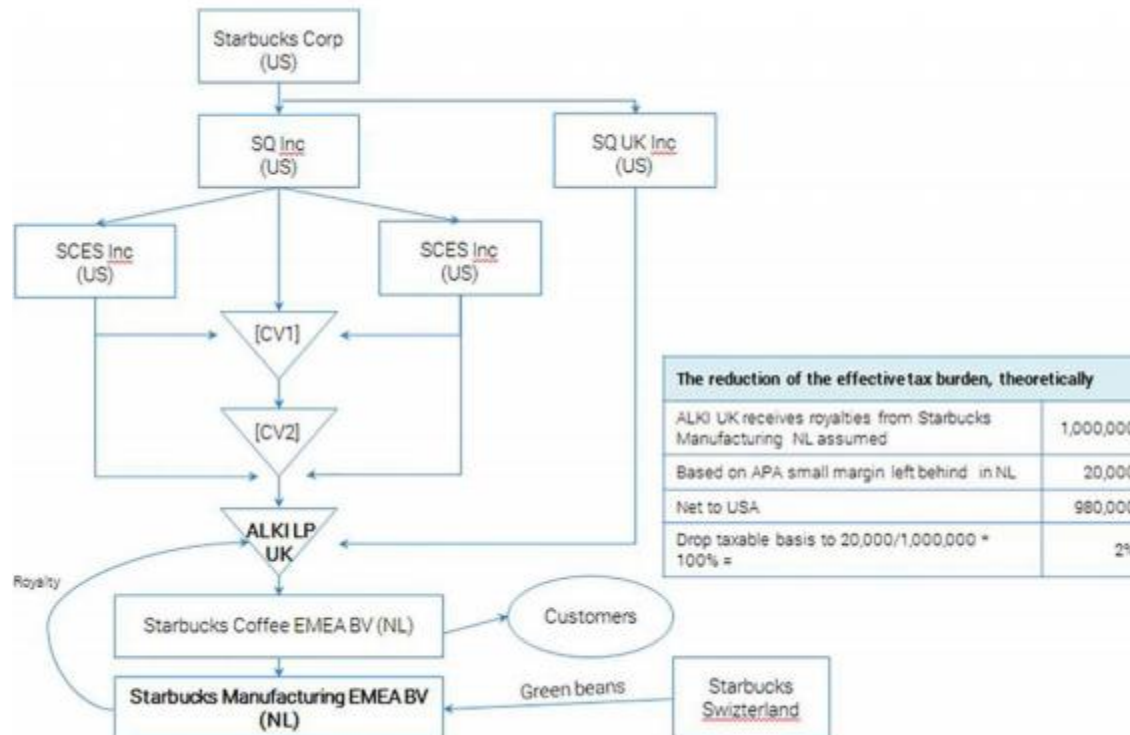
Apple case in VCA context



-Questions

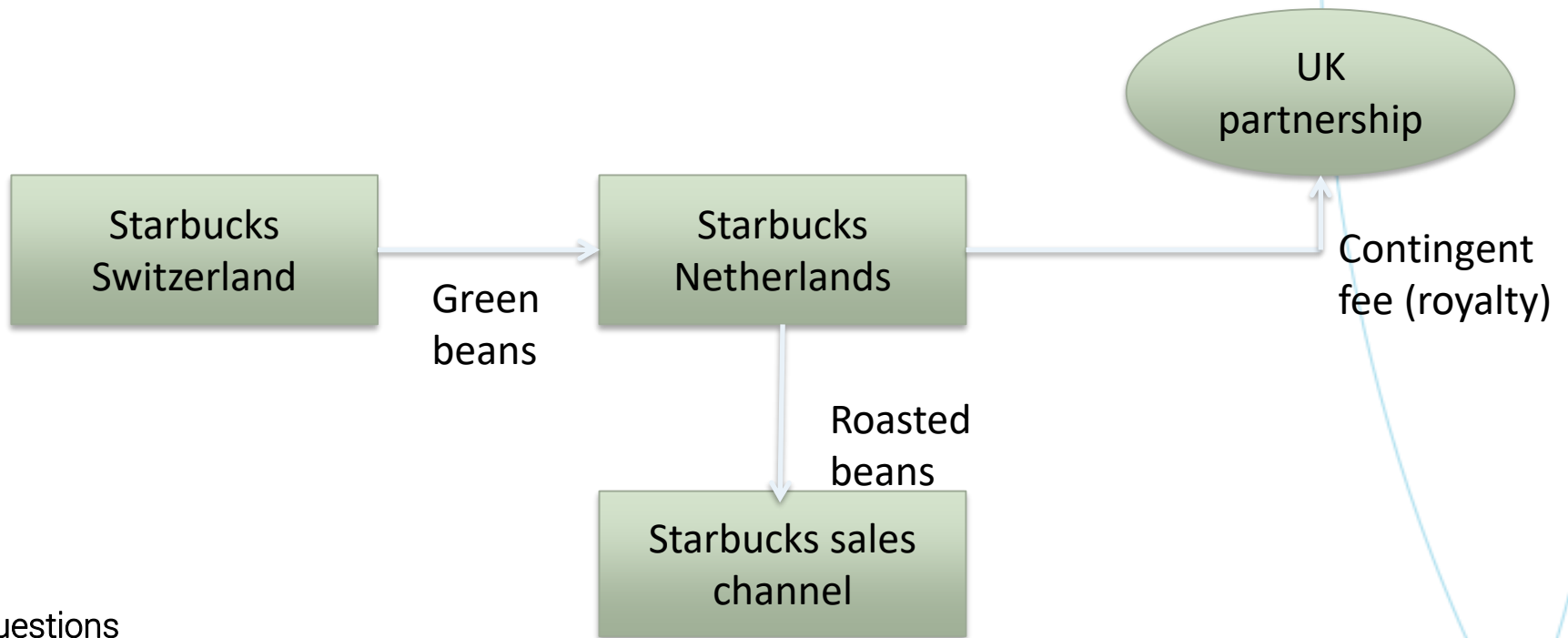
1. Where are the people functions?
2. Who is running the profit centre?
3. Is 841,500 (royalty income) a pure compensation for Apple IP?

Starbucks case in VCA context



The reduction of the effective tax burden, theoretically	
ALKI UK receives royalties from Starbucks Manufacturing NL assumed	1,000,000
Based on APA small margin left behind in NL	20,000
Net to USA	980,000
Drop taxable basis to $20,000 / 1,000,000 * 100\% =$	2%

Starbucks case in VCA context



-Questions

1. Has CUP been applied on green beans?
2. Has Resale Minus been applied on roasted beans?
3. Which of the group participants acts as an investment centre and/or profit centre?
4. Can you apply a contingent royalty model to compensate UK partnership for both acting as investment centre/profit centre?
5. Is there really a DEMPE function for roasting beans?



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