

UPDATES & OTHER TIDBITS

Authors

Kenneth Lobo
Sheryl Shah
Beate Erwin

Tags

Cuba
Google
European Commission
Inversions
Seized Property
State Aid
T.A.X.E. Committee
Transfer Pricing
U.K.

A.B.A. RECOMMENDS HIGHER CUBAN COMPENSATION FOR AMERICAN BUSINESSES

President Obama recently announced the re-opening of relations between Cuba and the U.S. However, before the U.S. embargo of Cuba can be removed, several issues must be resolved. One of these issues is the value of compensation that must be paid to American businesses and individuals for property seized by the Castro government.

The A.B.A. (American Bar Association) Tax Section recently recommended that any compensation paid by Cuba should not include tax benefits beyond those previously received by U.S. companies and individuals. Excluding tax benefits from the calculation would undoubtedly raise the amount of compensation that Cuba would pay.

According to the A.B.A., this approach would further American interests in several ways. Firstly, the compensation might amount to \$1 billion dollars. Secondly, if the compensation erroneously included tax benefits, the I.R.S. would garner less tax on the reclaimed amount, and claimants might recover funds worth less than the basis in the property before confiscation.

Settling these claims is just one of the issues that must be resolved before the U.S. embargo on Cuba is removed. It is expected that the majority of outstanding Cuban-American disputes will be resolved while President Obama is still in office. If outstanding disputes cannot be resolved during President Obama's administration, a Republican successor may take a "hardline" approach against the re-opening of relations between the U.S. and Cuba.

U.S. HOUSE PANEL DISCUSSES INVERSIONS, EUROPEAN INVESTIGATIONS

During a hearing of the U.S. House of Representative's Ways and Means Committee, Democratic and Republican lawmakers commented on inversions and current European Commission investigations into the tax practices of U.S. multinational enterprises ("M.N.E.'s").

Repatriation of Funds & Inversions

Much of the commentary focused on the unwillingness of U.S. enterprises to repatriate funds back to the U.S. to avoid the 35% U.S. corporate income tax. Republican lawmakers believe this practice will continue so long as the corporate tax rate remains at 35%. Lowering the U.S. corporate tax rate is thus one of the Republican's

goals. Democrat lawmakers instead focused on reducing the practice of inversions by limiting the ability of entities to use tax deductible interest payments between related parties to erode a country's tax base. The issue will likely be unresolved until the U.S. presidential elections this year.

European Investigations

Republican lawmakers also inquired about the merit of European Commission's investigations into American multinational enterprises alleging infringements of E.U. "State Aid" rules.¹ Witnesses offered differing opinions as to whether the investigations were "political" in nature or if questions of merit were mostly "hyperbolic exaggerations" by American companies. This hearing corresponds with hearings before the T.A.X.E. Committee of the European Parliament in which officials from U.S. M.N.E.'s, such as Apple and Google, testified on March 15 and 16. These proceedings are intended to be followed by a joint session of Congress and the T.A.X.E. Committee in May.²

Tension between the U.S. and the European Commission has definitely increased since State Aid investigations were initiated by the European Commission. Whether the upcoming hearings and joint session will calm the situation remains to be seen.



I.R.S. MAY SEEK PENALTIES IN COCA-COLA TRANSFER PRICING CASE

In the company's ongoing \$9.4 billion dispute, Coca-Cola could face a surcharge of up to 40% and as much as \$3.3 billion worth of taxes for the years 2007 through 2009, based on alleged undercharging of foreign affiliates for the use of intellectual property.

Coca-Cola claims that it is entitled to prospective penalty protection as a result of a 1996 closing agreement, provided the company follows an agreed-upon transfer pricing method. The company further claims that its compliance was confirmed by the I.R.S. during the past five audits, which covered 11 years through 2006.

The I.R.S., on the other hand, alleges that the closing agreement only applied to parts of the income allocated to Coca-Cola and did not apply to the years in dispute. Although the agency admits that it accepted the use of the closing agreement's transfer pricing method through 2006, it also claims that it had adjusted Coca-Cola's application of the method upon its audit.

The underlying reason for this change in treatment is assumed to be the significant restructuring of Coca-Cola operations, which occurred in previous years and involved the recombination of certain operating divisions and the reorganization of the company's North American activities. Updates on this case will follow.

¹ Beate Erwin and Christine Long, "[Apple in Europe – The Uphill Battle Continues.](#)" *Insights* 1 (2016): pp. 9-15.

² *Id.*

U.K. FINDS GOOGLE SETTLEMENT TO BE “DISPROPORTIONATELY SMALL”

The U.K. House of Commons Public Accounts Committee (“the Committee”) found the \$181 million tax settlement between Alphabet Inc., Google Inc.’s parent company, and the U.K. tax authority, Her Majesty’s Revenue and Customs (“H.M.R.C.”), to be disproportionately small when compared to the size of Google’s business in the U.K. The U.K. is the second largest market for Google after the U.S., but the company claimed that its sales to U.K. clients took place in Ireland in order to avoid corporate tax.

The settlement has been highly criticized because the deal was secret, and without full transparency, its fairness is difficult to judge. Much of the tax in dispute related to transfer pricing rules, and a significant portion of the settlement payment was interest, with no penalty charged. The Committee has requested that H.M.R.C. re-open the settlement if new evidence becomes available.

Additionally, the Committee is calling upon H.M.R.C. to lead the overhaul of international tax rules. They have made recommendations that include consulting with other tax authorities, devoting significant resources to tax investigations, strengthening the penalty regime, and monitoring the outcome of investigations, in order to ensure that multinational corporations are not being favored. These initiatives are in line with O.E.C.D.’s B.E.P.S. Project as well as similar tax transparency and anti-State Aid developments on the level of the E.U. The tax environment for multinational companies is definitely becoming tighter in view of these initiatives, combined with an increased exposure to scrutiny from European tax authorities. Structures that may have been acceptable in the past should be reviewed in light of these developments.

“The U.K. is the second largest market for Google after the U.S., but the company claimed that its sales to U.K. clients took place in Ireland in order to avoid corporate tax.”