Bloomberg BNA

International Tax Monitor Bulletin™

VOL. 0, NO. 0 MAY 27, 2015

Profit Shifting

Amazon's Changing Luxembourg Strategy No Guarantee of Tax Windfall for U.K., EU

Amazon.com has stopped booking European retail sales largely through its affiliate in low-tax Luxembourg, but that won't necessarily translate into a revenue windfall for the U.K. and other countries where it is now reporting the sales, experts in international taxation told Bloomberg BNA.

Richard Murphy, director of the U.K.-based Tax Research LLP, noted that Amazon consistently has reported losses on its global operations—and there is no indication that will change soon. Thus, headlines suggesting the company suddenly will start paying taxes in the U.K. are a "complete exaggeration," he said.

"We have no idea if Amazon is going to pay taxes in the U.K.," Murphy said May 26. "We have no idea if they are going to book a profit or a loss."

Even if the company does in fact incur a higher tax bill in the U.K., Murphy said, there is nothing in the new structure that translates to greater transparency for the retailer's European operations.

"They are going to record transactions in the U.K., but we don't know how much they will record here," he said, noting that Amazon is booking the U.K. sales through a branch of its Luxembourg affiliate. Under current rules, he noted, "there is no obligation to report what activities they may undertake here if it is done through a branch."

Peter Barnes, of counsel with Caplin & Drysdale, agreed that Amazon's tax bills might not change much under the new structure.

"It is well known that Amazon has earned very small profits, because it chooses to reinvest for future growth. So, if expenses are properly allocated to each jurisdiction, it is quite probable that Amazon's profits in a particular country will be small," said Barnes, also a senior fellow at the Duke Center for International Development at Duke University.

Restructuring of European Operations. On May 24, *The Wall Street Journal* reported that Amazon had restructured its European retail operations to stop booking sales through its retail operating company in Luxembourg, Amazon EU Sarl.

Effective May 1, the company is booking sales through the Luxembourg affiliate's local country branches in the U.K., Germany, Spain and Italy.

Amazon confirmed the arrangement in an e-mail statement to Bloomberg BNA May 26.

"We regularly review our business structure to ensure that we are able to best serve our customers and provide additional product and services," the company said. "More than two years ago, we began the process of establishing local country branches of Amazon EU Sarl, our primary retail operating company in Europe."

Amazon also is working on opening a branch for France, the company said.

The arrangement appears to indicate a radical shift in strategy for the Seattle-based e-commerce giant, which has been under investigation by the European Commission for its tax deals with Luxembourg.

But Barnes warned against drawing broad conclusions about international tax planning from Amazon's decision.

"When a company first enters a country, it is often possible to structure the operations in a way that minimizes the tax nexus," Barnes said in an e-mail to Bloomberg BNA. "But, as the company grows, it needs to have a deeper local presence in order to properly serve customers. That greater local presence will often create a greater tax liability."

Amazon's experience in the U.S. is an illustration of this pattern, he said. As the company built warehouses throughout the U.S. to improve its delivery, it increased its tax collection and reporting obligations to various states.

"Amazon is likely facing that same growth and change internationally," Barnes said. "This is an evolution, not a revolution, and many companies have faced these same tax issues as they grow internationally or will face the issues in coming years."

European Commission Investigation. The commission has taken a hard line against tax arrangements that it considers to be "state aid," granting select companies unfair tax advantages over their competitors. Amazon is one of several multinationals that has come under scrutiny.

According to the commission, Luxembourg had approved an arrangement with Amazon under which Amazon EU Sarl paid a tax-deductible royalty to a limited liability partnership, which was also based in Luxembourg but not subject to corporate taxation there. As

 ISSN 0000-0000

a result of this structure, most European profits of Amazon were recorded in Luxembourg but not taxed by Luxembourg.

Despite Amazon's shift in strategy, commission spokesman Ricardo Cardoso said May 26 that the state aid investigation into Amazon ''is ongoing and will continue.''

''We are examining the concerns that the tax ruling provided by Luxembourg is providing the company selected advantages. And in that context we will consider the announcement of Amazon's new tax structure,'' he said.

The EC May 27 will outline its next steps in the field of corporate taxation when it conducts an ''orientation debate'' on proposals due to be published June 17. The proposals will include details on how the European Union's executive body will update its common, consolidated corporate tax base legislation.

Barnes also noted that a number of factors are causing multinational companies to examine their global tax structures, including the state aid issues and country-by-country reporting.

''Successful companies are always looking at their structures to make sure they fully comply with local laws, reasonably minimize tax expense, and, most importantly, support growth and the company's business model,'' he said.

Given Amazon's history of minimizing profits in favor of future growth, Barnes added, ''it is particularly smart of Amazon to adjust its tax structure to support its growing business, rather than constrain the business just to save a minor sum on taxes.''

Murphy described himself as ''cynical'' about Amazon's restructuring because of the likelihood that it wouldn't lead to a significant change in the company's tax posture.

Murphy also was critical of press reports that credited the U.K.'s diverted profits tax for Amazon's shift in strategy. The new tax, which took effect April 1, applies a 25 percent tax rate to profits deemed to be ''diverted'' from the U.K. through the artificial avoidance of a permanent establishment or other ''contrived arrangements''.

''I don't think the diverted profits tax can possibly be the reason because it does not apply in other countries where they are setting up branches,'' Murphy said.

If anything, he said, it was the EU pressure on Amazon, rather than any individual country's pressure, that led to the change—illustrating the importance of coordinated international action in fighting profit-shifting by multinationals.

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   ISSN 0000-0000