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Texas Hold'em Poker: France Bet Google & McDonalds. Will U.S. Treasury Double Down?

William Byrnes (Texas A&M University Law) · Monday, May 30th, 2016

In highly dramatic fashion the French tax authorities and IT specialists raided Google's headquarters and McDonalds. I don't own Google stock. I'm not in favor of Google's near monopoly on search (though it has accomplished this by offering a really great product and (free) work tools that make my life much easier). I don't eat Big Macs.

But my U.S. nationalistic eyebrows rise high on my forehead when I read the headlines. And I thought of Texas Hold'em. Let me explain….

"Google, now part of Alphabet Inc, pays little tax in most European countries because it reports almost all sales in Ireland. … If staff in countries like France finalize contracts with local clients, then the company would be obliged to report the revenues nationally and pay taxes in each country."

The McDonalds story is merely a continuation from January 2014 of a transfer pricing dispute over the value of the franchising rights and "brand" intangible of McDonalds.

Prof. David Herzig (Visiting at Loyola Law, Los Angeles this summer) and I discussed for an hour yesterday whether Google may, or may not, have a PE. Whether the activities of the Irish company in France, or the French company on behalf of the Irish company, rise to the level of a permanent establishment under the Ireland-French tax treaty will inevitably require a Court to decide. At least, we couldn't decide and we consider ourselves reasonable minds.

Perhaps the France authority will beat Google down to just accept a UK deal, albeit a bit higher. But I take a contrarian perspective that will be as unpopular with my academics colleagues as my current Starbucks stance. (see Starbucks' Transfer Pricing & The EU Commission Decision) (also see EU Commission State Aid Starbucks Decision – My U.S. Perspective)

The UK Revenue, at least according to its testimony in Parliament, with a fine tooth comb, swept all of Google's operational practices and procedures, examined emails and memos, interviewed dozens of staff and executives, and after this three-year intensive investigation concluded that Google did not have breach the threshold of a PE (at least according to the Ireland – UK tax treaty).

I think it unlikely, albeit recognize it is plausible, that Google France may have different operational procedures, or that Google may have hoodwinked the UK revenue authorities. France, on the same set of facts, may find under its law that the treaty PE threshold has been breached whereas the UK may not (which would be a damaging finding to the EU system of Rule of Laws and to the general tax treaty system PIL, but that's another issue).

But does it require a "raid" upon another US multinational to collect the facts? Would a disclosed subpoena have been sufficient legal protocol for both sides to then establish a time for the meeting, document collection, and interviews, in an orderly fashion. Would a MAP request under the Ireland – France treaty with EoI not been effective? France could have requested an EoI from the UK Revenue for the evidence gathered from the UK exhaustive investigation.

The McDonalds' transfer pricing dispute is a certain loser for the France revenue authority. I have not undertaken a brand value or franchise intangibles study, so I have no data immediately at hand to support my position. But I do have common sense. Place a McDonalds Big Mac, without the name built on decades of non-stop advertising, next to any other hamburger, even a tiny (Krystal) burger, and you'll choose the "anything else". Place the generic Big Mac next to just about any other fast food choice. But put the "McDonalds" and "Big Mac" label on it and somehow it becomes a competitive fast food choice. I could do a half-million dollar intangibles study to get me to the same place that common sense already brings me.

France could have made many innovative "brand discount" arguments to reduce the value of the brand, none of which require extensive or hard to collect documentation from McDonalds.

But instead, the French government chose to organize a "raid" US companies – equivalent of a perp arrest walk. Obviously, the French are seeking headlines, the French President seeking votes (kicking the Americans is always a popular French vote getter) and nationalistic social – political pressure on Google (perhaps the French will boycott the Internet).

Perhaps the PE system must be changed or its definition in treaties? Perhaps McDonalds is fattening the French youth and requires a Bloomberg soft drink tax. But that's not where the law stands today. If France wants to capture more tax revenue from Google and McDonalds, let France change its laws to do so and then apply those prospectively, not retroactively.

What I see is are U.S. companies, bushwacked then drug through the mud, because the French government has decided that the company under a doctrine of equity and fiscal necessity does not pay enough tax to support the French *joie de vivre*. My question: What is the U.S. Treasury going to do about it? File another "I protest" speech? (See Will the US Impose IRC Section 891 – Double US Tax Rates – on EU Companies for State Aid Retribution?).

A French colleague has reminded me that the "American chicken has come home to roost". Not Colonel Sanders. The chicken is the U.S. government's imposition of a $10 billion OFAC fine on BNP. To be clear – I did not support the $10 billion fine. Because it did not hold the correct people accountable – the Board and managers. A long prison sentence for everyone involved would have been a better deterrence of future behaviour than the mere reduction of BNP's proposed dividend that year. Yes – that the inevitable outcome of the fine was a reduction in dividend borne not by France at all but 10.3 % by the Belgian government shareholder and 76% by institutional, mainly pension funds, shareholders.

OFAC was, at the time, clear law, that BNP clearly violated (the , and its chief executive team lied about the violations until a whistleblower came forward with minutes that had group executive officers telling the meeting documentor not to minute the meeting lest the Americans find out.

It wasn't a civil tax dispute based on heavy facts. It was a fundamental human rights matter of a bank funding governments known for genocide and terrorism, accepted as such by the French government. Recall that BNP officials described Darfur as a "humanitarian catastrophe" and, then while discussing the $8 billion on BNP transactions for certain Sudanese banks, stated that these banks "play a pivotal part in the support of the Sudanese government which…has hosted Osama Bin Laden and refuses the United Nations intervention in Darfur." BNPP's senior compliance personnel *agreed to continue the Sudanese business* and rationalized the decision by stating that "the relationship with this body of counterparties is a historical one and the commercial stakes are significant. For these reasons, Compliance does not want to stand in the way." See BNP Paribas pleads guilty, pays $8.9 billion for Iran and Sudan sanctions busting).

Anyway, I said then that the large U.S. fine of BNP was merely passing on the blame to the Belgian government and pension fund shareholders – where the blame clearly did not attach. But the French wanted to protect the executives from criminal responsibility and the American let them get away with it for $10 billion. You'd think that the clear lesson is not to fund genocidal, terrorist regimes.

I think BNP has something to do with the Google and the McDonalds raid though. The French have a long memory, and experts at diplomacy. The French government did not fold on BNP, rather it traded on a bad hand. It knew that the hand was a loser, and thus accomplished a trade-off to keep the executives from being hunted down like Swiss bankers. Perhaps the Google and McDonalds raid are a feint – not about whether Google it has a PE in France, or whether McDonalds' brand has a value of Y instead of a value X. Instead this is France's payback, and a warning to the U.S. federal authorities in general about geo-politics.

If it is the sore feelings left from BNP, then France is playing like a game of poker with a wry smile. Will the U.S. fold, call, or up the ante?

But in Texas we play Texas Hold 'em poker with the cards face up, not face down. Because more information is available, we bet aggressive on a good hand but fold quickly on a bad hand.

If America lets France win this hand, not only does it shift the burden of France's welfare state unto the American taxpayer and the American retiree (through reduced retirement savings/pension growth), but it also tells America that it is not OK for the U.S. authorities to go after European companies that fund genocide and terrorism.

I hope the U.S. Treasury follows Texas Hold 'em style and realizes it has a good hand. Double down on the bet by languaging a bill for Section 891 and submitting it to the President and Congressional for comments! Conduct a couple IRS "raids" of French companies to gather evidence for Section 482 intangibles audit. (see Will the US Impose Double US Tax Rates on EU Companies from Countries that Retroactively Impose State Aid Claw Backs?)

After the poker game is over, the countries may get back to international tax PIL protocols and procedures without political interference. Internationally, France and the U.S. should work within the agreed framework of the OECD to prospectively evolve the international tax system to address PE threshold and IP valuation challenges. "Raids" do not support the cooperative framework necessary for such discussions.

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