"The Three Shades of Tax Avoidance of Corporate Groups: Company Law, Ethics and the Multiplicity of Jurisdictions involved".

Introduction

In 2011 Apple's Irish subsidiary had a profit of 16 billion Euros but only 50 million of them were charged as tax in Ireland. Apple ended up paying a tax rate of only 0.005% in 2014 on the profits of its Irish subsidiary down from an anyway low 1% in 2003[1]. This is but one example of so-called "jurisdiction arbitrage" by which large companies avoid or evade liabilities.[2] It is now estimated that total tax losses amount to $400 billion for OECD members alone[3] and to a global revenue loss of around $650 billion[4]. Company law provides the multinationals with the legal tools which enable tax avoidance. MNEs, which are a series of inter-linked companies formed in various national legal systems, incorporate subsidiaries in jurisdictions which provide them with legal yet unethical tax loopholes. Basic company law principles such as the principle of separate legal personality and limited liability have evolved into a veil which protects multinationals from external control on their tax affairs at multiple levels. Each member of the group is deemed as of independent from each other in most instances. Yet, taxing its profits within the jurisdiction where they were actually produced could prove impossible. Despite the recognition of each member of the group as a separate legal entity, company law allows the members of the same group to transfer intellectual property and licensing rights within the group and to therefore shift their tax base to whichever jurisdiction offers a more attractive set of tax rules. When unrelated companies transact with each other the costs and prices of their financial exchange are driven and fixed by the market. The article argues that this is not the case with multinationals and their intra-group exchanges. When members of the same group transact then the price of the transaction may not be fixed by the free market but by the need to minimise the groups' costs and tax liability. That leads to a lawful tax avoidance which renders a reform of company law ethically imperative and necessary from a legal and economic point of view. Therefore, our thesis is that tax avoidance at the level of multi-national groups in the EU is now *institutionalised*. The article argues for a reform of company law to address the instutitionalisation of corporate tax avoidance.

To that end it is argued that the principles of separate legal personality and limited liability in their current form are unfit for corporate groups when issues of taxation are at stake. They

[1] Commission Decision, *Ireland gave illegal tax benefits to Apple worth up to £13 billion*, 12 Company Lawyer, 377-378. (2016)

[2] J. Dine, '*Jurisdictional Arbitrage by Multinational companies'*, 3 Journal of Human Rights and the Environment, 44 (March 2012).

[3] Crivelli, E., de Mooij, R., & Keen, M. *Base Erosion, Profit Shifting and Developing Countries*. 72(3) FinanzArchiv: Public Finance Analysis, 268–301. (2016).

[4] Tax Justice Network, Alex Cobham, Tax *Avoidance and Evasion – The Scale of the Problem*,. See: http://www.taxjustice.net/wp-content/uploads/2017/11/Tax-dodging-the-scale-of-the-problem-TJN-Briefing.pdf (accessed 5 December 2017).

should be significantly reformed, so that each member of the group is viewed as established in the member state where it operates with its revenues shielded and -most importantly- taxed in that jurisdiction. When this proves to be too difficult or complicated, the corporate veil should be lifted altogether and the mother company of the group should be taxed for the entire set of profits made by all the members of the group in the EU.

The article is structured as follows. It will examine the purposes of tax, arguing that the social compact between a government and the population is enhanced by taxes. The article will explain the nature and functions of corporate groups. It will look at the concept of jurisdictional arbitrage; namely at the ways in which the cross-national structure of corporate groups can be used in order to avoid taxation in multiple jurisdictions with a special focus on the European Union and its member states. The article will explain the history, structures and complex multi-layered and multi-jurisdictional mechanics of corporate tax avoidance, which flow from the failings of company law. It will then argue for a review of the application of the principles of limited liability and of separate legal personality at the group level for tax purposes. It will explain how intellectual property emerged as a basic tool for tax avoidance within the context of a group. Company law provides groups with a set of lawful tools to escape taxation in all jurisdictions where the multinationals are physically present and fully operational. This is particularly evident in the three case-studies that the article focuses upon. The Starbucks, Google and Apple groups availed themselves of the full set of tools provided to them by company law. They structured their group and operations in such a way so that their profits were transferred not just to the jurisdiction where the tax rates were the lowest in the EU, but also to the jurisdictions which provided them with tax loopholes. The latter allowed them not only to escape the low rates in question but, to pay only a fraction of them. These tactics are unethical yet lawful on the basis of the current company law framework. The article concludes that the law should change so that groups and their individual members pay the appropriate amount of tax as set by the jurisdictions where they operate.

The Purpose of Tax

"The whole history of tax, government and democracy is entangled precisely because those who have been taxed have demanded that their *consent* to taxation be sought before any such charge was imposed."[5] Murphy's point is that even if the population is disenchanted with their politicians, they have the right to vote, and governments can be unseated. A new administration might change the tax laws as the people do have the right to vote in elections that result in the formation of the governments that set the taxes in the countries which they reside. However, the definitions of 'tax and taxes' are decided by the prevailing economic climate where individuals are 'burdened' by governmental levies. According to the Oxford dictionary 'tax or taxes' are "a *compulsory* contribution to state revenue, levied by the government on workers' income and business profits, or added to the cost of some goods, services and transactions."[6] Contrast this definition to The Encarta definition; "*Money paid* to a government, an amount of money levied by a government on its citizens and used to run the

[5] Richard Murphy, *The Joy of Tax*, 31, (Bantam Press), (2015). The italics are ours.

[6] Oxford Dictionary, https://en.oxforddictionaries.com/definition/us/tax, used by Richard Murphy, *The Joy of Tax*, 30, Bantam Press, (2015), (accessed on 12 October 2016).

government and the country or state"[7] The Oxford dictionary's definition focuses on *compulsion* and there is no reason given for the purpose of levying the money. A legal dictionary defines tax as 'a governmental assessment (charge) upon property value. . . simply counting the possible means of taxing property, an arid technical definition.[8] On the other hand, the Encarta dictionary's definition hints at the reasons and it also suggests that the 'money is paid' by taxpayers without compulsion. Without going deeply into what is 'compulsion'; it is interesting that in the Word Thesaurus 'compulsion' is synonymous as 'pressure' or 'obligation'.' Murphy argues that in a democratic state with a full franchise, the money paid by the taxpayers is *optional* since all people have debated the taxes and the law has been set democratically. Compulsion is hard to suggest in this case."[9] 'Pressure' and 'obligation' could be better words because the tax is levied by consent. The crucial point is: "How can sovereign citizens democratically decide how much of their resources they wish to devote to common goals"[10]

Here we can only highlight crucial aspects of the struggle between States, governments and the people. It is well known that the prevailing economic model in the Anglo-American sphere[11] is the neo-liberal paradigm. The recent history of neo-liberalism is to be found in the scholarship propounded by the Austrian economist and social philosopher, Ludwig Von hurdles and Friedrich Von Hayek.[12] Von Mises's axiom that 'egoism is the basic law of society'[13] led him to conclude that unrestricted laissez-faire, free markets and governments that are confined to the defence of unhampered private property rights comprised the only viable policy for the human race.[14] The neo-classicist doctrine is that rational actors will, if left undirected, make maximally efficient economic decisions which will maximise their welfare, leading to an efficient economy where all will eventually benefit: "For more than 20 years economists were enthralled by so-called "rational expectations""[15]. One of the tenets of neo-liberalism is that economic growth will deliver benefits to all[16]. Faithful adherents in this

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[7] Encarta World English Dictionary, 1931, Bloomsbury, (1999).

[8] The Free Dictionary, https://legal-dictionary.thefreedictionary.com, (accessed on 15 November 2017).

[9] Richard Murphy, *The Joy of Tax*, ibid at 5.

[10] Thomas Picketty, *Capital,* 404, Harvard University Press, (2014).

[11] Particularly in the US where the Washington Consensus is still very strong; see Janet Dine and Marios Koutsias, *The Nature of Corporate Governance; The Significant of Natural Cultural Identity,* Edward Elgar, especially Chapter 1, (2013).

[12] Birch &Mykhnenko,*The Rise and fall of Neo-Liberalism: The collapse of an Economic Order*, Zed Books, 3, (2010).

[13] ibid

[14] Murray N. Rothbard, '*Biography of Ludwig Von Mises (1881-1973)*' Ludwig Von Mises Institute <http://mises.org/about/3248> (accessed 16 August 2012).

[15] J. Stiglitz, The Guardian, (Friday December 20th 2002). See: J. Stiglitz, *The Price of Inequality*, Allen Lane, Penguin, (2012).

[16] Jonathan D. Ostry, PrakashLougani and DavideFurceri, "*Neoliberalism: Oversold?*" , 53 Finance & Development No2, (June 2016). See: http://www.imf.org/external/pubs/ft/fandd/2016/06/ostry.htm, (accessed on 15 July/2017).

model are acting on the theory and many believe it is the dominant economic paradigm for the world. The debates between the neo-liberal vision and a welfare economy are very intense. This is particularly true in a democratic State where there is an understanding that there is a social compact between the government and the people. Issues of tax involve power, democracy and inequality because all of them are involved in struggle to evolve a society as Piketty has shown[17]. Richard Murphy's book is apposite; the book is entitled 'The Joy of Tax'[18] because if we need to design a *just* society you need a legal framework which includes a redistribution mechanism between the advantaged and the less prosperous citizens. Some believe that this can found in 'the Rule of Law' a vague concept where laws are promulgated, predicated on a loose understanding of niceness, human rights and liberal values.[19] These values are important but the power struggle to design a society is based on a constant fluctuation between actors involving moral values, selfishness and pragmatism.[20] In this struggle taxes are right in the frame. Legal discourse on ownership rights and property rights are vital. They are crucial because there is a constant tension between the extent of protection for property rights and what sort of property rights should be valued. In the tax arena, the discourse is shrill. Many neo-liberal commentators, especially the Libertarian Alliance, argue that all tax is theft because in a free market all services can be purchased and government should have no say on pre-tax income. They argue that it is a fiction that the government provides services because they are in the public interest.[21] To challenge this point of view Murphy and Nagel have a written a scholarly thesis arguing that taxes are the most significant instrument by which the political system can put into practice a conception of economic justice and showing that the fairness of the distribution of pre-tax income is a red herring and a misconception of property rights. The property right of pre-tax income lies in the government and taxes should be understood as a democratic levy for society.[22] In this, Richard Murphy concurs where he argues that taxes are optional.[23] Pope Francis also argues against the neo-liberal ideology and he propagated 'Evangelii Gaudium'' (The Joy of the Gospel) in 2013. Here he argues that free market will certainly not benefit everyone. He argued that a simplistic neo-liberal economic model shows "a crude and naïve trust in the goodness of those wielding economic power in the sacralised working of the prevailing

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[17] See: footnote 6.

[18] Richard Murphy, *The Joy of Tax*, Bantam Press, (2015).

[19] Philip Wood, *The fall of the Priests and the rise of the Lawyers,* Bloomsbury, (2016). See WorldJustice, https://worldjusticeproject.org/about-us/overview/what-rule-law. This NGO promotes 4 principles which are extremely vague. One principle is that law should be 'fair'. (Accessed on 19 May 2017).

[20] Foucault, *Power/Knowledge,* Pantheon, (2018), Rowan Williams, *Faith in the Public Square,* Bloomsbury, (2012), J. Dine and Andrew Fagan (eds), *Human Rights and Capitalism,* Edward Elgar, (2007) especially in Michael Blecher, "Law in Movement: Paradoxontology, law and social movements", Chapter 4, 80-114, Tomas Sedlacek, *Economic and Good and Evil,* Oxford University Press, (2011), Harvey Cox, *The Market as God,* Harvard University Press, (2016).

[21] Chris R Tame, *"Taxation is theft",* Political Notes No 44, http://www.libertarian.co.uk/lapubs/polin/polin044.pdf, (accessed on 15 July 2017).

[22] Liam Murphy and Thomas Nagel, *The Myth of Ownership*, Oxford Scholarship Online, (2002).

[23] Richard Murphy, *The Joy of Tax*, Bantam Press, (2015).

economic system . . ." in the meantime the disadvantaged are left destitute.[24] Harvey Cox argues that "At the time of writing, markets have assumed mythological proportions.[25] The consequences of the neo-liberal system is are dire for the populations of these countries'[26] such as the denigration of the environment[27] and increasing inequality which may lead to the hollowing out of national states and of democracy. Thomas Picketty's seminal book *Capital,* shows that in Anglo-Saxon countries the share of the top 0,1% cent highest incomes in total income rose sharply since the 1970 countries[28]. He also argues that taxation is not a technical matter rather it is a political issue.[29]. Where countries had huge inequality, frequently it fuelled revolutions because the society lost a purpose; "without taxes, society has no common destiny"[30]. Picketty argues that French revolution and the revolt of the British colonies were a *fiscal* upheaval. "No taxation without representation"[31]. The neo-liberal regime provides a "universally valid and application 'policy mix' and is propagated accordingly. This means that political reforms should be oriented towards economic objectives – low inflation, a balanced budget, the removal of trade barriers and foreign currency controls, maximum mobility for capital minimum regulation of the labour market ... these are *the* reform objectives of the neo-liberal regime...it is supposed to be apolitical but of course it is highly political"[32]

Less tax is one of the neo-liberal tenets because of the thrust of individualism and this itself leads a wish to slim governments and welfare. The opposite philosophy argues that less advantaged people need governmental services and the government needs to raise revenue to allow a welfare state to thrive. Furthermore, industry needs good infrastructure to promote business. The U.S. Department of Transportation estimates that "the nation's highways and bridges face an $808.2 billion backlog of investment spending"[33] "[34]. Why is all of this

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[24] Pope Francis, *Evagelii Gaudium:The Joy of the Gospel*, New York, (2013).

[25] Harvey Cox, *The Market as God,* Harvard University Press, (2016).

[26] OECD, "*Income Inequality*",.https://data.oecd.org/inequality/income-inequality.htm, (2014), (accessed on 15 December 2017). The OECD uses the Gini coefficient.

[27]Naomi Klein, *This Changes Everything,* Penguin, (2014).

[28] Thomas Picketty, *Capital,* 319, Harvard University Press, (2014).

[29] ibid, page 493.

[30] Ibid.

[31] Ibid

[32] U Beck, *Power in the Global Age*, 79, Polity Press, (2005).

[33] Christiina Pazzanese http://news.harvard.edu/gazette/story/2017/01/our-crumbling-infrastructure/, Harvard Gazette, Jan 6, 2017, (accessed on 22 May 2017).These projects include $479.1 billion in critically needed repairs. More than two-thirds of the nation's roads and nearly 143,000 bridges are classified in "dire need" of repair or upgrades..

[34]Thomas Picketty, *Capital,* 404, Harvard University Press, (2014).

important? In a neo-liberal[35] economy the discourse is to suggest that an individual has absolute property rights including money and all assets. This is particularly important in the corporate arena. Legally a corporation is a person, but the prevailing discourse is that its objective is profit maximisation. In this context, the company's directors have a duty to avoid tax as their property rights are sacred and absolute. This means that common goals like health and education are denigrated and profit maximisation is promoted.

Although it is impossible to delve into all of the economic philosophies around property rights in this article we will focus on the role of tax avoidance by MNEs and damage done by the lost tax revenue to the governments.[36] Margaret Hodge, chair of the public accounts committee, told Google's northern Europe boss, Matt Brittin, that "his company's behaviour on tax was "devious, calculated and, in my view, unethical"[37]. Although the tax avoidance schemes were legal it is clear that government services are hit if the biggest companies do not pay tax. There is abundant research to show that the poor need public services more than the rich.[38]

Groups of Companies and Jurisdictional Arbitrage

The "company" as a legal and social phenomenon has not only been one of the successful human inventions but it has been one of the pillars of the modern economy and at the end society. This is due to its attributes of legal personality and limited liability. These are legal principles which were granted by the state to the company rendering the latter the vehicle through which investment is channelled. Legal personality entails the recognition of the company as nearly equivalent to a natural person[39]. The principle has been a "foundation stone"[40] in the development of company law. The company therefore, exists independent of its founders as well as its members and it can sign contracts, sue and be sued and own assets on its own. Incorporating a business aims at ensuring that is members will not incur personal liability[41]. The creation of a legal fiction which amounted to a legal entity, which was

[35]It is impossible to deal with the intricacies neo-liberal economic paradigm in this article, the crucial point is this ideology is promotes strong property rights for individuals as against community rights, leading to inequality, see U. Beck, *Power in the Global Age,* Polity Press, (2005).

[36]Alex Cobham, *"Estimating Tax Avoidance; New Finding, New Questions,* https://www.taxjustice.net/2017/03/22/estimating-tax-avoidance-questions/, March 22nd, 2017, (accessed on 15 July 2017).

[37]Simon Bowers and Rajeev Syal, *"MP on Google Tax Avoidance Scheme 'I Think that you do Evil'",* https://www.theguardian.com/technology/2013/may/16/google-told-by-mp-you-do-do-evil, (accessed on 15 July 2017).

[38] Poverty and Social Exclusion (PSE) http://www.poverty.ac.uk/tags/public-services, (accessed on 24 May 2016); World Bank *"Breaking the Cycle of Poor Service Delivery in the Middle East and North Africa",* http://www.worldbank.org/en/news/feature/2015/04/10/breaking-the-cycle-of-poor-service-delivery-in-the-middle-east-and-no, April 14 2015, (accessed on 24 May 2016).

[39]*Salomon v Salomon & Co* [1897] AC22.

[40] Paul Hughes, *Competition Law Enforecement and Corporate Group Liability – Adjusting the Veil,* 35(2) European Competition Law Review, 75, (2014).

[41]*Salomon v Salomon & Co* [1897] AC22, page 35.

separate from the humans behind it, was substantial for recognising responsibility for harmful actions or, in legal terms, "liability"[42]. From the introduction of a separate legal personality and onwards the management of the company and its shareholders were no longer going to be held accountable for wrongs perpetrated by them; the liability was to be shouldered by the legal person that is the company. At the level of an individual company this may be quite helpful to the claimant taking into account that it is easier to sue a company for wrongs perpetrated by it, rather than attempting to identify the humans behind it, which may demand sufficient time, and resources that the claimant may not possess. Therefore, the granting of a separate legal personality to the company has enhanced legal clarity as liability can be attributed to the individual legal person rather than a variety or a network of natural persons who are behind it and are difficult to identify.

At the level of a corporate group however, as it is going to be explained later in this article, the principle in question creates an additional layer of protection to the parent company shielding it further against unlawful or harmful acts perpetrated by its subsidiary. All of the companies in the group are separate, therefore it is difficult to sue a company because the damage may we caused by one or more of the companies in the group. All of the companies are separate legal entities responsible for their own actions; and therefore importantly shielded against liability for the actions of other members of the group. Where one or more company are incorporated in different jurisdictions the protection afforded increases because there may be procedural hurdles for claimants (including *forum non conveniens*[43]), differences between company laws in the jurisdictions and sometimes lax regulations in diverse jurisdictions. These differences are seized by the MNEs to protect them and allow them to minimise their tax liability. In the *Adams*[44] case the court stated that it is within the rights of the company to structure its group in such a way so that all liabilities fall on one of the members of the group. That effectively shields the rest of the members and primarily the parent from any liability against claims even though they were quite likely masterminded by it. This seems to constitute a distortive application of one of the most fundamental principles of company law, which is undoubtedly of critical importance for our entire legal system. Company law recognises subsidiaries as a useful tool to establish domestic corporate residence or citizenship for doing business and to limit the extent of the liability of the parent but the law has overreached this principle[45].

The granting of limited liability to the company was a critical moment in history. Limited liability establishes that the individuals behind the company are only liable to the extent of their investment to the company. Limited liability effectively removed the risk inherent in corporate activities and paved the way for millions of people to engage themselves in corporate investments. In case of insolvency[46] their liability will be limited to their

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[42] Eric Orts W., *Business Persons, A Legal Theory of the Firm*, 34, (Oxford : Oxford University Press, 2015).

[43] This entails the power for a judge to dismiss a claim if a better jurisdiction is more suitable.

[44] *Adams v Cape Industriesplc* [1990] BCLC 479.

[45] See: Eric Orts W., *The Legitimacy of Multinational Corporations, in Progressive Corporate Law*, edited by Mitchell Lawrence E., Westview Press, (1995).

[46] See: Omar P.J., *Themes and Movements in International Insolvency Law*, 12 Insolvency Law Journal, 7-8 (2004).

contribution to the company's assets. In no way can it be extended to their personal assets. Therefore, limited liability effectively allows the shareholder eager to invest into a company to pre-determine the maximum level of his liability and losses in case of insolvency. It created a safety net which allows investors to provide their capital to the company without the threat of losing more than their pre-calculated acceptable loss in case of insolvency. Limited liability was viewed as the "greatest single discovery of our times...even steam and electricity are far less important than the limited liability corporation and they would be reduced to comparative impotence without it"[47]. The rationale behind this quite strong statement is the importance ascribed to the principle of limited liability for spurring the investment which was necessary to fuel the industrial revolution. As the industrial revolution was taking pace, it brought along rapid and radical changes to all aspects of economic life. It became evident that if England was to fully profit from the technological advances taking place in its territory it had to put in place corporate structures that would facilitate large scale investment. Admittedly, the existence of unlimited liability that rendered private investment in companies and ongoing industrial projects a decision of high risk was perceived as the main obstacle to the realisation of the enormous potential of the new economy. The doctrine came into existence roughly at the same time as the industrial revolution was gathering pace.

Groups of Companies: history, structures, invisibility, purpose and challenges.

The two principles which form the core of company law are clear in their application when it comes to a single corporate entity, but they can acquire a certain degree of controversy when they apply in a group of companies. The growth of MNEs has been possible precisely because most legal systems regard one company holding shares in another in exactly the same way as if the company were a human individual shareholder. Most legal systems take no account of the reality of the accumulation of power represented by a large number of companies related by interlocking shareholdings, despite the fact that many companies are organised in a 'group' structure wherein control is exercised over a number of subsidiaries through shares held by a 'parent' company. While the simplest case is a hierarchy with 100 per cent shareholding by a parent company, there are numerous other ways of creating effective control of one company over others through a range of share structures and other contractual devices such as franchises and joint ventures.[48]

From a legal point of view "each individual is a juridical entity with his own rights and duties"[49]. The principle of limited liability covered initially only the shareholders who were natural persons as a company could not become a shareholder in another company[50]. It facilitated investment as it ensured private individuals that their private property could not be seized by creditors in case of corporate insolvency. In fact, in the nineteenth century in the UK if the memorandum of association was silent, it was *ultra vires* for a company to purchase

[47]. William Hackley P, Tracey Benson G., *Shareholder Liability for Inadequate Capital*, 43 University of Pittsburgh Law Review, 841, (1982).

[48] EM Weitzenboeck, '*Between Contract and Partnership: Dynamic Networks as CollaborativeContracts and More*' (PhD Thesis, Oslo University, April 2010).

[49] Philip Blumberg, *Accountability of Multinational Corporations: The Barriers Presented by Concepts of Corporate Judicial Entity*, 24 Hastings International and Comparative Law Review, 207, (2001). Also see: J. Dine *The Governance of Corporate Groups,* (Cambridge: Cambridge University Press (2000) .

[50] Maria Jose Navarro Lezcano, *Piercing the Corporate Veil in Latin America Jurisprudence, A Comparison with the Anglo-American Method,* 16, (London/New York, Routledge, 2016).

shares of another company[51]. This meant that unless the –then- constitution of the company specifically allowed a company to buy shares of another company, the former could not do that. And if it did, the action would have been found invalid as an *ultra vires* act, which means an act which falls outside of the objects of the company. The UK Company's Act 1862 did not contain any explicit prohibition of inter-company shareholding[52] but, apparently the approach towards this issue was cautious. In the USA until the end of the nineteenth century a company could not acquire shares in another company save the cases where this was explicitly authorised by statute[53]. In the US this changed in 1890s when the state of New Jersey introduced new legislation[54] which allowed a company to form a subsidiary and to own its shares[55].

So, it is fair to argue that limited liability for corporate groups "emerged from a historical accident"[56]. After companies were allowed to become shareholders of other companies, the doctrine of limited liability began applying to parent corporations, as shareholders, for acts of their subsidiaries[57]. Within a group the doctrine of limited liability limits the liability of both the parent company –for the actions of its subsidiaries- as well as of individual shareholders. That creates a multi-layer protection for the parent company which dissociates itself from any harmful actions perpetrated by subsidiaries linked to it unless they are functionally the same entity[58].

At the early stages of corporate formation, the groups of companies consisted mostly of companies within the same jurisdiction. However, nowadays this is certainly not the case. Nowadays, the members of the group are present in multiple countries. Therefore, the main problem now is the extraterritoriality of national jurisdiction. Let us examine this a little more closely. Each nation-state has equal sovereign power to regulate its territory and to enact its own laws. Companies are a legal fiction invented by national law. Each state possesses the power (and usually the exclusive power) to regulate the company and to enforce its liabilities. It is important to note that a group of companies as a whole does not have legal personality[59]. It is not a single legal entity. MNEs are, rather, complex structures made up of individual

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[51] In *re European Society Arbitration Accounts*, 8 Ch. D. 679, 692 (1878)

[52] *Barned's Banking Company* 3 L.R.-Ch. 105, 112-13 (1867).

[53] See: *Louis K. Liggett Co.v Lee, 288 US 517, 556. 1933*

[54] New Jersey Act, 4 April 1888, ch 269 s1 (1888 N.J. Laws 385).

[55] H. Butler, *Nineteenth Century Jurisdictional Competition in the Granting of Corporate Privileges*, Volume 24 Journal of Legal Studies, 161, (1985).

[57] Gwynne Skinner, *Rethinking Limited Liability of Parent Corporations for Foreign Subsidiaries' Violations of International Human Rights Law*, 72 Wash. & Lee L. Rev. 1769, 1773, (2015)..

[57] Gwynne Skinner, *Rethinking Limited Liability of Parent Corporations for Foreign Subsidiaries' Violations of International Human Rights Law*, 72 Wash. & Lee L. Rev. 1769, 1773, (2015)..

[58] Meredith Dearborn, *Enterprise Liability: Reviewing and Revitalizing Liability for Corporate Groups*, 97 Cal. L. Rev. 195, 197, (2009),.

[59] Melvin Aron Eisenberg, *Corporate Groups in Gillooly Michael, The Law Relating to Corporate Groups*, The Federation Press, 2, (1993).

companies in a variety of interrelationships. While globalization means that the world appears to be a smaller place and while goods and people can move freely across borders, companies remain legally tied to the country where they are formed. The operation of equal sovereign power, moreover, normally means that regulations made in one jurisdiction, in the normal course of events, cannot have any impact on corporate liability in another. This is the problem of extraterritoriality. The fact that MNEs are series of companies formed in different national legal systems and tied together in various legal ways, either by holding shares in each other or by various legally binding agreements between them presents genuine complexity. The latter renders taxing MNEs quite difficult.
Therefore, the main motives for opening a subsidiary in another jurisdiction are the desire to escape "the difficulty – if not the impossibility- of qualifying the parent company as a foreign corporation in a particular state...the avoidance of taxation...the desire for limited liability"[60]. A primary purpose for this parent-subsidiary organisational structure is to minimise the potential liability of the parent company[61] for the operation and potential claims against its subsidiaries[62]. A corporate group can be defined as two or more companies that operate "under a similar directive to achieve a common objective"[63]. Groups are complex structures made up of individual companies in a variety of interrelationships[64]. Given the complexity of the links between the members of the group it is difficult to provide a uniform definition of the term "group"[65]. A crucial element is the element of control that one member exerts over the other that determines whether the companies are "affiliated", "associated" or we are talking about a "collective conduct of the integrated business"[66]. Vertical groups comprise a parent and its subsidiaries, while horizontal groups comprise of companies with cross-holdings or pyramidal structures[67]. Within the group each company enjoys the privileges of

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[60] Douglas O. William, Shanks M. Carrol, Insulation from Liability Through Subsidiary Corporations, 39 Yale Law Journal 193, 193, 1929.

[61] John Matheson H., *The Modern Law of Corporate Groups: An Empirical Study of Piercing the Corporate Veil in the Parent Subsidiary Context*, 87 North Carolina Law Review, 1094, (2008-2009).

[62]See John Matheson H, Brent Olson A., *A Call for a Unified Business Organization Law*, 65 George Washington Law Review, 1, (1996).

[63] Maria Jose Navarro Lezcano, *Piercing the Corporate Veil in Latin Americal Jurisprudence, A Comparison with the Anglo-American Method,*15, (London/New York: Routledge, 2016)

[64]See the US Third Restatement, ALI '*Restatement of the Law, Third, Foreign Relations'* at para 213: 'For purposes of international law, a corporation has the nationality of the state under the law of which the corporation is organised'. And on 'Multinational Corporations': 'The Multinational enterprise or corporation … is an established feature of international economic life, but it has not yet achieved special status in international law or in national legal system. A multinational corporation generally consisted of group of corporations, each established under the law of some state, linked by common managerial and financial control and pursuing integrated policies.'
[65] D. Prentice, *Some Aspects of the Law Relating to Corporate Groups in the United Kingdom*, 13(1) Connecticut Journal of International Law, 313, (1999).

[66] See N. Mendelson, *A Control Based Approach to Shareholder Liability for Corporate Torts,* 102(1) Columbia Law Review, 1203, (2002).

[67] See: Janet Dine, *The Governance of Corporate Groups*, Cambridge Studies in Corporate Law, Cambridge University Press, (2000). And: D. Prentice, *Some Aspects of the Law Relating to Corporate Groups in the United Kingdom*, 13(1) Connecticut Journal of International Law, 313, (1999).

limited liability and of the independence guaranteed by the separate legal personality. Despite the fact that the group companies share a "unity of purpose"[68] and "commonality of design"[69], the members of the group are independent entities. Each of the members of the group is subject to the jurisdiction of the country where it is established. Therefore, although the members of the group may follow the same strategy and pursue the same agenda, they are independent of each other and subject to a different set of laws depending on the jurisdiction and the country of establishment. The companies are "creatures of national legal systems since they are incorporated in certain jurisdictions"[70]. The term "multi-national enterprises" stems from the recognition of the fact that the group consists of members operating in an array of different countries[71]. Hence, they are subject to different jurisdictions which entail a set of legal obligations and standards that need to be adhered to, which may vary significantly from country to country. The operation of equal sovereign power, moreover, normally means that regulations made in one jurisdiction, in the normal course of events, cannot have any impact on corporate liability in another. The combination of separate legal personality and limited liability rendered the creation of a subsidiary an attractive choice. It enables its parent company to enter another jurisdiction, unfold its business activities while shielded from liability. It insulates an area of investment and a set of assets from pressures from either creditors or the judiciary as the liability will fall on the subsidiary rather than the controlling parent. Limited liability was created to protect private investment into companies. However, at group level there is a shifting of risk from the parent company and its shareholders to the creditors of a subsidiary[72]. This is because the parent is protected by two levels of limited liability; one that shelters the parent company against liability of the subsidiary and a second one which shelters the parent's shareholders from any claim against them.

Limited Liability and Separate Legal Personality should not apply to groups for tax purposes.

Problems started to emerge when the traditional company law concepts of limited liability and separate legal personality applied at the group level. Legal personality and limited liability as well as company law in general took shape at a time when "business enterprises were organised and conducted through a single independent corporation"[73]. The role of a natural person as a shareholder differs from that of a company as a shareholder. The former is usually apathetic and unaware of corporate developments which can lead to insolvency and therefore

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[68] Shwetank Ginodia, Rishi Shroff, *A Corporate Governance Perspective on Lifting the Veil in Group Companies in India and the United Kingdom*, International Company and Commercial Law Review, 423, (2014).

[69] Philip Blumberg , *The Transformation of Modern Corporation Law: The Law of Corporate Groups*, 37(1) Connecticut Law Review, 606, (2005).

[70] Muzzafer Eroglu, *Multinational Enterprises and Tort Liabilities, An Interdisciplinary and Comparative Examination*, 70, (London: Edward Elgar, 2008).

[71] Karen Vandekerckhove, *Piercing the Corporate Veil*, Kluwer Law International, 5, (The Netherlands, 2007).

[72] Muzzafer Eroglu, *Multinational Enterprises and Tort Liabilities, An Interdisciplinary and Comparative Examination*, 72, (London: Edward Elgar, 2008).

[73] Karen Vandekerckhove, *Piercing the Corporate Veil*, Kluwer Law International, 5, (The Netherlands, 2007).

in need of protection covering his personal assets. In such a context limited liability reduces transaction and monitoring costs[74]. It reduces the need for shareholders to monitor managers[75]. That has been viewed as enhancing efficiency[76]. However, when those concepts apply to the "complex corporate structure of the large multinational enterprise, they break down"[77].

Nowadays, within the group context limited liability that insulates parent corporations from "liability for the claims of involuntary creditors of the controlled corporation causes even economists to...concede that limited liability raises serious problems because it enables the enterprise to externalize its costs"[78]. Limited liability now enables a corporate group which is structured in tiers of companies to insulate each corporate tier of the group, and thus, achieve "layers of insulation for the parent corporation from liability for the obligations of its numerous subsidiaries"[79]. Shareholder protection is not even an issue at this stage. Even if a parent company is not shielded against the liabilities of its subsidiaries, the shareholders of the parent will still be protected as they are covered at individual level by limited liability[80]. Hence, the liability for the subsidiaries' harmful action will not be shouldered by them but by the legal person that is the parent company.

Thus, while at the level of an individual company the necessity of limited liability is almost self-evident, the case for disregarding the corporate entity is more compelling when the shareholder itself is another corporate entity[81]. Granting limited liability to individual investors may encourage "investment in productive albeit risky activities"[82]. However, its extension to parent companies is inappropriate because they "manifestly constituted an important part of the enterprise"[83]. The majority of private individuals acquiring shares of

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[74] Judith Freedman, *Limited Liability: Large Company theory and Small firms*, 63(3) The Modern Law Review, 37, (2000).

[75] Frank H Easterbrook., Daniel R. Fischel, *The Economic Structure of Corporate Law*, Harvard University Press, 41-44, (1996).

[76] Frank H Easterbrook., Daniel R. Fischel, *The Economic Structure of Corporate Law*, Harvard University Press, 41-44, (1996)..

[77] Philip Blumberg, *Accountability of Multinational Corporations: The Barriers Presented by Concepts of Corporate Judicial Entity*, 24 Hastings International and Comparative Law Review, 207, (2001).

[78] Philip Blumberg, "*Limited Liability and Corporate Groups*" Faculty Articles and Papers. 28, (1986). Also at: http://digitalcommons.uconn.edu/cgi/viewcontent.cgi?article=1027&context=law_papers, Janet Dine, *Jurisdictional Arbitrage by multinational companies: a national law solution*?, 3 (1) Journal of Human Rights and the Environment, (March 2012).

[79] Philip Blumberg, "*Limited Liability and Corporate Groups*", (Faculty Articles and Papers. 28, (1986).

[80] John Swain A., Edwin Aguilar E., *Piercing the Veil to Assert Personal Jurisdiction Over Corporate Affiliates: An Empirical Study of the Cannon Doctrine*, 84 Boston University Law Review, 446, (2004).

[81] See: Kurt Strasser A., *Piercing the Veil in Corporate Groups*, 37 Connecticut Law Review, 664-665, (2005).

[82] David Leebron W., *Limited Liability, Tort Victims and Creditors*, 91 Columbia Law Review, 1566, (1991).

[83] Philip Blumberg., *The American Law of Corporate Groups*, in McCahery, Picciotto and Scott, *Corporate Control and Accountability*, Clarendon, 308, (1995).

either a private or a public company do not possess the assets and capital that a company has when it sets up a network of subsidiaries. In the case of the latter, the company possesses sufficient capital and financial and legal expertise to set up a network of inter-connected companies in a variety of jurisdictions. The parent company will not act as a passive investor or as a “normal shareholder”[84]who is in need of protection. It will actively engage in the management of the subsidiary. For this reason there are no information and monitoring costs either. In this case the principle of limited liability is actually twisted in making sure that the parent is to be safeguarded against any legal claims against the subsidiary when the latter is involved in illegal or sometimes criminal activities. Therefore, what was designed as an incredibly important legal tool which protected the rights of individuals, evolved into a mechanism which shields a parent company against liability for illegal activities perpetrated by its subsidiary in an anyway quite complex web of inter-related companies. In such a case the parent company’s liability will be limited to the extent of its shareholding in the subsidiary. However, parents will arrange their legal and financial affairs in such a way so as to minimise involvement of that type in subsidiaries.
This enables an era of “organisational decoupling” primarily achieved through the so-called subsidiarisation[85]. Subsidiarisation is a term which is employed when it is to define the channelling of corporate activities through different legal entities[86]to avoid risk. Subsidiarisation on the basis of the *Adams* case[87]has become a part of a business strategy to “insulate one card in the house of corporatisation from the collapse of another card”[88]. The organisational structure of the group can be shaped so as to shift liability exclusively in one member of a group, which is established in the jurisdiction with the less restrictive legislative framework. As the final part of the article will argue, it can also be shaped in a manner which can attain significant tax avoidance for the group using a web of intra-company loans, transfer agreements, intellectual property and other undoubtedly legal tools which can relieve the parent from many regulatory or tax burdens. This “organisational decoupling”[89]or “liability outsourcing”[90]aims at breaking down the central business into a variety of legal entities operating in different jurisdictions so that the parent escapes liability. This means that a parent can outsource liability-prone activities to the subsidiary. The parent can simply lead its subsidiary to legal demise by ordering its liquidation and the potential transfer of its assets to the parent or to another member of the group. This means that the subsidiary will cease to

[84] See: Peter Muchlinski, *Holding Multinationals to Account: Recent Development in English Litigation and the Company Law Review*, 23 Company Lawyer, pages 173-175, (2002).

[85] Linn Anker-Sørensen, .‘*Financial Engineering as an Alternative Veil for the Corporate Group’*. 5 European Company Law 13, 158, (2016).

[86] Such as subsidiaries, franchises, joint ventures, holding companies etc

[87] *Adams v Cape Industriesplc* [1990] BCLC 479.

[88] See: Griggs L. &Lugten G., *Veil over the Nets (Unravelling the Corporate Liability For IUU Fishing Offences),* 31(2) Marine Policy, 159-168, (2007).

[89] Linn Anker-Sørensen, .‘*Financial Engineering as an Alternative Veil for the Corporate Group’*. 5 European Company Law 13, 161, (2016)..

[90] Alexander Daehnert , *Lifting the Corporate Veil: English and German Perspectives on Group Liability*, 18(11) International Company and Commercial Law Review, 393, (2007).

exist from a legal point of view which entails the loss of any liability in the first place. In the best case scenario the litigators are left with the herculean task to detect any sufficient business or administrative link between the subsidiary and the parent which will result in the liability attached to the latter. But, the group will have positioned and structured itself in such a way that such links would be almost impossible to prove. The most distinctive feature of multinational corporate groups is their incredible complexity[91]. Therefore, tracing liability within the context of a corporate group[92]is viewed as one "of the great unsolved problems of modern company law and probably the most controversial problem of group law"[93]. And this is why piercing the veil or otherwise establishing a legal link between the parent and the subsidiary so that the former will be found liable for the harmful acts of the latter is the "most litigated issues in corporate law"[94].

Countering MNE's arbitrage

The simple way to counter the protection afforded to MNEs via the doctrine of separation between companies is to lift the corporate veil. The lifting or piercing of the corporate entails that the two companies are not to be viewed as independent legal entities but as a single one bearing the same level of liability. In this case the parent is liable for the actions of its subsidiary which loses its independence before the court. The problem is that the piercing of the veil is one of law's most "unpredictable doctrines...predicting when the veil of limited liability will be disregarded is like predicting lightening strikes"[95]. This is because the lifting of the veil will be very much dependent on the nature of the case, the preferences of the individual judges[96] who will be called up to issue a decision based on criteria which are anything but solid[97]. It is astonishing that even today the UK does not possess a "specific body of law applicable to corporate groups"[98]. The problem with the doctrine is its "raison

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[91] T Hadden, *Inside Corporate Groups*, 12 International Journal of the Sociology of Law, 271, (1984).

[92] C. Schmitthoff , *BancoAmbrosiano and Modern Company Law*, Journal. Business. Law, 363 (1982).

[93] Karen Vandekerckhove , *Piercing the Corporate Vei*l, Kluwer Law International, The Netherlands, 56, (2007).

[94] Robert B. Thompson , *Piercing the Veil Within Corporate Groups: Corporate Shareholders as Mere Investors*, 13 Connecticut Journal of International Law, 383, (1999).

[95] Stephen Bainbridge M., Todd M. Henderson, *Limited Liability, A Legal and Economic Analysis*, 4, (Edward Elgar, 2016).

[96] See S. Ottolenghi , *From Peeping Behind the Corporate Veil to Ignoring it completely*, 53 Modern Law Review, 338, (1990).

[97] See *Adams v Cape Industriesplc* [1990] Ch.433 (A.C.). The criteria on the basis of which the veil may be lifted are whether the subsidiary operates as a facade to conceal fraud, whether the parent and the subsidiary form a "single economic unit" and whether the subsidiary operates as an agent of the parent. All criteria are fluid and open to interpretation on the part of the judges.

[98] Simeon Obidairo , *Transnational Corruption and Corporations. Regulating Bribery through Corporate Liability*, 182, (Ashgate, 2013).

d'être"[99]. It exists as an exception to the rule of limited liability so as to prevent injustice and unfairness[100]. Therefore, the application of the doctrine has always been "fact specific and open-ended"[101] or "incoherent and unpredictable"[102], "uncertain and doctrinally unsustainable"[103] or an "incomprehensible mess"[104].

The UK jurisprudence in this area is "far from principled"[105]. The courts are reluctant to admit the reality of interrelated companies acting in any other way than as a number of separate entities tied together by their relationship as significant shareholders in each other. It is not difficult to accept that perhaps the most "extreme example of separate units is the UK".[106]The UK will employ a contractual approach towards the corporate group. It will view its constituent companies merely as shareholders who are pursuing their individual interests while protected by limited liability. Consistent to its laissez-faire economic principles the country refrained from putting in place any statute regulating liability at group level. The UK courts will consider the subsidiary as a single entity with the mother company only in cases of fraud or where it is shown beyond any possible doubt that the two companies constitute a single economic unit; that means that the subsidiary acts simply as the agent of the parent. These requirements have historically proved very hard to meet, as is shown by case law and legal practice. The approach of the UK courts is epitomised in the *Adams*[107] case, where the Court of Appeal spelled out its position on the subject matter in the clearest terms: "if a company chooses to arrange the affairs of its group in such a way that the business carried on in a particular foreign country is the business of the subsidiary and not its own it is entitled to do so". In the UK a 98% controlling interest of the parent in the subsidiary does not of itself give rise to an agency relationship so as to treat the parent and the subsidiary as one enterprise[108]. Therefore, so far as the English courts are concerned, there is no single group

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[99] Edwin Mujih C., *Piercing the Corporate Veil as a Remedy of Last Resort after Prest v Petrodel Resources Ltd: inching towards abolition?*, 40, Company Lawyer, (2016).

[100] Jeff Chan H.Y. , *Should "reverse piercing" of the corporate veil be introduced into English Law?,* Company Lawyer, 163, (2014).

[101] T.K. Cheng , *The Corporate Veil Doctrine Revisited: A Comparative Study of the English and the US Corporate Veil Doctrines,* 34 Boston College International and Comparative Law Review, 330, (2011).

[102] D. Millon , *Piercing the Corporate Veil, Financial Responsibility and the Limits of Limited Liability*, 56(5) Emory Law Journal, 1307, (2007).

[103] Marc Moore , *A Temple Built on Faulty Foundations: Piercing the Corporate Veil and the Legacy of Salomon v Salomon*, Journal of Business Law, 180, (March 2006).

[104] John Matheson H., *The Modern Law of Corporate Groups: An Empirical Study of Piercing the Corporate Veil in the Parent Subsidiary Context,* 87 North Carolina Law Review, 1095, (2008-2009).

[105] Simeon Obidairo , *Transnational Corruption and Corporations. Regulating Bribery through Corporate Liability*, 186, (Ashgate, 2013)..

[106] Janet Dine, *The Governance of Corporate Groups*, 43-44, Cambridge Studies in Corporate Law, (Cambridge University Press, 2000).

[107]*Adams v Cape Industriesplc* [1990] BCLC 479.

[108] *Kodak Ltd v Clark* [1903] 1 KB 505.

`entity' as such.[109] In many ways globalisation poses such a challenge for the traditional legal system which is based on sovereign domestic legal systems. The activities of multi-national groups of companies point to the difficulty of holding them liable under "this traditional understanding of international law"[110]. International law is still focused on nation states as the main players[111] therefore applying its jurisdiction to a group of companies will collide with national sovereignty. As explained before individual members of the group are subject to the jurisdiction of their establishment as the group does not possess a single legal personality and it does not amount to a single legal entity but to a collection of companies subject to divergent laws and legal norms.

The main jurisdiction providing for avenues to link parents and subsidiaries using control mechanisms is Germany with the *Konzenrecht*[112]. A number of jurisdictions[113] are using the German system and adding an 'enterprise' concept using a 'control' concept which links companies who are part of a company group together, often using connections which show that they are controlled by the same financial systems, overlapping managements or shareholders. The legal doctrine of the separation of the companies is breached in particular situations including the overlapping connections. In this way, the German law uses the relevant connections to say that some companies in the group will have legal obligations. However strong the connections between companies in the group they will not have obligations between companies *unless* they are linked by with an equity relationship i.e. a proportion of the same shareholders. This is not the same as the Albanian Law on Entrepreneurs and Companies[114] because, although it which was modelled on the basis of the German law, it defines a parent-subsidiary 'relationship' which *does not involve shareholder holding*. Rather, the relationship 'shall be deemed to exist where one company regularly behaves and acts subject to the directions or instructions of another company.' The idea is that a claimant can sue the parent company or and subsidiaries wherever the company is incorporated. The 'enterprise' idea is not new[115] but there is an invigorated push because of

[109] Janet Dine, *Jurisdictional Arbitrage by multinational companies: a national law solution*?,3 (1) Journal of Human Rights and the Environment, 44, March 2012..

[110] Katarina Weilert , *Taming the Untamable? Transnational Corporations in the United Nations Law and Practice, Max Planck* Yearbook of United Nations Law, Volume 14, 447, (2010).

[111] Stefan. Kirchner , *The Subjects of Public International Law in a Globalised World*, 2 Baltic Journal of Law and Politics, 83 (2009).

[112] The Konzernrecht provisions are found in the *Aktiengesetz of 6 Sept. 1965* (Federal Law Gazette I, 1089), See: Alexander Scheuch, *Konzernrecht: An Overview of the German Regulation of Corporate Groups and Resulting Liability Issues*. 13 (5) European Company Law, *(*December 6, 2016); University of Oslo Faculty of Law Research Paper No. 2016-29. Available at SSRN: https://ssrn.com/abstract=2881180 Company Law, Vol. 13,

[113] The *Konzenrecht* has been copied in Brazil, Portugal, Slovenia, Croatia, and Taiwan See:, Mads. Andenas, and Frank. Wooldridge, *European Comparative Company Law,* CUP, 448-449, (2009). Albanian Law has an extended extraterritoriality concept , See: Law No. 9901 'On Entrepreneurs and Companies' 2008.

[114] No. 9901 2008, specifically Article 207.

[115] J. Dine, *The Governance of Corporate Groups, (*Cambridge University Press 2000).

moral outrage against tax avoidance by MNEs[116]. Recent scandals involving extraterritoriality arbitrage by MNEs have focused on tax avoidance and evasion.[117] It is difficult to estimate the extent of the problem presented by tax havens because they operate as a 'hidden economy'. However, Tax Justice and Oxfam have estimated that US$18.5 trillions are processed in the havens, and that developing countries have lost US$12 trillions to illicit outflows.[118] The company mechanisms of lifting the veil or a concept of enterprise groups are blunt tool and later we will consider other European initiatives. However, the company law mechanism of an 'enterprise group' is interesting, other initiatives found in this paper may be stronger.[119]

Intellectual Property as a tool for tax avoidance

In this context one needs to examine intellectual property as it "has become the leading tax-avoidance vehicle"[120] for multinationals. Multinationals are "stripping money out of market countries and into tax haven intangibles holding companies"[121]. Certain of the characteristics of intellectual property make it ideal for avoiding tax[122]. Firstly, in contrast to tangible property such as hardware or factories, intellectual property such as patents or copyright can easily be transferred to low tax countries or to tax havens with the click of a button or through the submission of paperwork[123]. Secondly, the nature of the intellectual right renders its precise market valuation very difficult to establish. That grants to multinationals the ability to justify the artificially low market valuations that entail low tax assessments. Virtually "all IP-based tax-avoidance schemes involve assigning an artificially low price to a piece of IP"[124] at some point in time. The most prevalent way to shift profits is therefore through transfer pricing and licensing. Transfer pricing is a business structural tool that helps multinationals to

[116] Linn Anker-Sørensen,, *Parental Liability for Externalities of Subsidiaries: Domestic and Extraterritorial Approaches* University of Oslo Faculty of Law Research Paper No. 2014-36 (October 7, 2014).; Nordic & European Company Law Working Paper No. 14-06. Available at SSRN:http://ssrn.com/abstract=2506508 or http://dx.doi.org/10.2139/ssrn.2506508

[117] Nicholas Shaxson, *Treasure Islands, (*Vintage Books, 2012), OECD: *The OECD Project on Harmful Tax Practices, (*2002), IMF: *IMF Working Paper; Base Erosion, Profit Shifting and Developing Countries,* WP/151/118, (2015), W. Crivelli, R. De Mooij, M Keen, *IMF Policy Paper; Spillovers in International Corporate Taxation, (*2014), the IMF said that the effect is 'significant and sizable'.

[118] The Tax Justice Network, '*The Size of the Problem'*, 2016 and see footnote 32 in this article

[119] Ibid, see the section entitled 'It is time to change'.

[120] Andrew Stanek-Blair, *Intellectual Property Solutions to Tax Avoidance*, 62 UCLA Law Review, 2, 4, (2015).

[121] Lee Sheppard A, *Is Transfer Pricing Worth Salvaging?*, 136 Tax Notes 467, 470, (2012).

[122] Michael Graetz J., Rachael Doud, *Technological Innovation, International Competition and the Challenges of International Income Taxation*, 113 Columbia Law Review, 347, 402, (2013).

[123] See: Yariv Brauner , *Value in the Eye of the Beholder: The Valuation of Intangibles for Transfer Pricing Purposes,* 28 Virginia Tax Review, 79, 88, (2008).

[124] Andrew Stanek-Blair, *Intellectual Property Solutions to Tax Avoidance*, 62 UCLA Law Review, 2, 5, (2015).

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manipulate the prices on intra-firm trade and the flow of services within the group to their own advantage[125]. When unrelated companies transact with each other the costs and prices of their financial exchange are driven and fixed by the market. This is not the case with multinationals and their intra-group exchanges. When members of the same group transact then the price of the transaction may not be fixed by the free market but by other considerations linked to minimising the groups' costs and tax liability. The valuation of assets by mispricing assets including intellectual property assets exacerbates the first avoidance scheme where arbitrage is to transfer assets to a low-tax country[126]. Many MNEs establish a company in a low tax country -like Ireland for example- to which it licenses all patent rights. That allows all the future profits from the patents at international level to accrue to the Irish subsidiary, which is subject to a low taxation rate. Also, all the members of the group trading products and services under the brand name and the trademark transferred to the subsidiary will pay licensing fees to the member of the group established in the low tax country; those fees will be subject to low taxation. On top of that the licensing fees in question amount to costs that the other members of the group have to bear. Costs that could be deductible from their profits and significantly lower their taxability in their respective host countries too. At the same time the licensing fees are also subject to a low tax rate. A result of transfer pricing, the prices charged for intra-firm flows of goods, services, intangible property may differ significantly from those charged to independent companies for comparable goods or services[127]. This is why national law and international codes usually requires the parent company to receive what's now called "arm's length" royalties from its low-tax subsidiary for the use of the patents. The "arm's length" standard which states that inter-unit transactions should be priced the same as the prices chosen by unrelated parties engaged in similar trades under similar circumstances[128].However, the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations is quite hard to enforce due to the "lack of market parallels, multinationals' use of tax heavens, and lack of disclosure of either earnings worldwide or of pricing methods"[129].Of course the OECD Guidelines are just that it is a piece of soft law without any significant sanctions and the arm's length price is not of a fixed value. It could be estimated on the basis of the price of similar products or services if traded between unrelated companies, but there is a high degree of uncertainty when

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125 See: Alfredo Urquindi J., *An Introduction to Transfer Pricing*, New School Economic Review, Volume 3(1), 27, (2008). See: Roger W.Y Tang,. 1997. *Intrafirm Trade and Global Transfer Pricing Regulations*. Connecticut: Quorum

126 K Hassett, K Newmark, *Taxation and Business Behaviour: A Review of the Recent Literature, in Fundamental Tax Reform: Issues, Choices and Implications*, edited by J Diamond, G Zordow, MIT Press, Cambridge, 208, (2008).

127 See: Sylvaine Plasschaert, *Transfer Pricing and Multinational Corporations: An Overview of Concepts, Mechanisms and Regulations*, (New York: Praeger, 1979).

128 See: Lorraine Eden, *Taxing Multinationals: Transfer Pricing and Corporate Income Taxation in North America*, (University of Toronto Press, Toronto, 1998). See: OECD: *The OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations,* Article 9, (Paris, 2010).

129 Dirk Schindler, Guttorm Schjelderup, Transfer *Pricing and Debt Shifting in Multinationals*, Centre of Economic Studies &Ifo Institute, Working Paper No.4381, 2, (August 2013).

engaging in such price calculations. The fluidity in the outcome of such estimations renders the investigation of transfer pricing strategies difficult.

The Case of Starbucks

The case studies which are examined in this article demonstrate the significance of the problem. The three companies in question are all prominent and reputable corporations in their distinctive fields. Despite their high-profile corporate brand and international profile, the multinationals in question took advantage of their structures and shifted their profits among the members of the group in order to avoid tax. Company law provided them with the tools which enable tax avoidance. We argue that this should change. Between 2009-2013 Amazon, Google and Starbucks paid a combined total of £57,7 million despite revenues of nearly £32 billion over the same period, meaning only 0.18% of revenues were paid in corporation tax[130]. The loss of significant tax revenue on the part of large corporate entities, which are producing great profits in the UK results in heftier tax bills for individuals and smaller companies fuelling resentment against the current economic model and subsequently the political arrangements which underpin it. The group is shifting profits from one jurisdiction to the other benefiting from the loopholes in national and international law to avoid paying appropriate tax to the various jurisdictions it is involved in. Taking into account that 60% of world trade takes place within multinational firms[131], the extensive use of transfer pricing may be indicative of the potential tax losses for both developed and developing countries around the world. The House of Lords Select Committee on Economic Affairs Report on "Tackling corporate tax avoidance"[132] admits that the "UK faces a serious problem of avoidance of corporation tax especially by multinational companies even when they do large scale business in this country". It identifies "transfer pricing" and the payment of "royalties"[133] among the members of the group for the use of intellectual property rights and brands as two of the most effective means of lowering corporate tax bills. The Report stated the companies' "assessments are based on accounts that defy economic and business realities" as they show profit being earned in low-tax jurisdictions in which "little or no real business takes place"[134]. The Report underlines the importance of tackling tax avoidance so

[130] Peter Conell, *Ending the Free Ride, Making Multinationals Pay Their Way*, 6, (London: Civitas, November 2014).

[131] OECD Observer: John Neighbour, OECD Centre for Tax Policy and Administration, *Transfer pricing: Keeping it at arm's length*, Read it at :http://oecdobserver.org/news/archivestory.php/aid/670/Transfer_pricing:_Keeping_it_at_arms_length.html (Accessed on 15 January 2017)

[132] House of Lords, Select Committee on Economic Affairs, 1st Report of Session 2013-4, *Tackling Corporate Tax Avoidance in a Global Economy: is a new approach needed?,* Report, (31st July 2013), HL Paper 48, page 7.

[133] Royalty fees charged to UK subsidiaries can be raised so as to cut profits in the UK and raise them in subsidiaries in lower tax jurisdictions.

[134] House of Lords, Select Committee on Economic Affairs, 1st Report of Session 2013-4, *Tackling Corporate Tax Avoidance in a Global Economy: is a new approach needed?*, Report, 31st July 2013, HL Paper 48, page 9.

that the corporations pay their "fare share of tax"[135].Zucman has calculated the total amount of wealth that is legally hidden as $7,6 trillion.[136]The problem is that it is law and to a great extent company law which provides the structures and the tools that enable tax avoidance. The 2013 OECD Action Plan on Base Erosion and Profit Shifting[137]accepts that these practices undermine the perceived integrity of "the tax system and may have a deleterious effect on tax compliance generally"[138]. This is an example of the philosophies examined at the beginning of this article. It undermines the fairness of national tax systems because taxpayers must bear a greater share of tax burden. American President F.D. Roosevelt noted that "taxes, after all, are the dues that we pay for the privileges of membership in an organised society"[139]. When some of the most powerful members of the society are not paying their feed then the entire society could face be destabilised.

Starbucks which is a prominent multinational present in many wealthy high-tax countries in Europe as well as in North America did not have to pay any considerable tax in the UK[140]. While it maintains its physical presence through a chain of cafes in crowded high streets across the UK, it put its IP assets like "trademarks, proprietary roasting methods, and trademark-protected stored dress"[141] into law tax jurisdictions. While Starbucks UK is the largest coffee chain in the UK, it has been reporting losses. This is because of transfer pricing within the group. It pays the parent company a royalty of 6% of sales for its use of intellectual property such as brand and business processes[142]. Therefore, while Starbucks UK made a loss, overall the group made substantial profits partly due to the UK operations[143].

[135] House of Lords, Select Committee on Economic Affairs, 1st Report of Session 2013-4, *Tackling Corporate Tax Avoidance in a Global Economy: is a new approach needed?,* Report, (31st July 2013), HL Paper 48, page 10.

[136] See: Gabriel Zucman, *The Hidden Wealth of Nations: The Scourge of Tax Heaven*s, (Chicago University of Chicago Press, 2015).

[137]OECD *Action Plan on Base Erosion and Profit Shifting*, OECD Publishing(2013). See: https://www.oecd.org/ctp/BEPSActionPlan.pdf See: Wolfgang Schoen, *Transfer Pricing Issues of BEPS in the Light of EU Law*, British Tax Review, 3, 417, (2015).

[138] Brian Arnold J, James Wilson R, *Aggressive International Tax Planning by Multinational Corporations: The Canadian Context and Possible Responses*, The School of Public Policy Research Papers, University of Calgary, Vol 7, Issue 29, page 6, (September 2014).

[139] Read his speech at: http://www.presidency.ucsb.edu/ws/?pid=15201 (accessed on 20 January 2017)

[140] Edward Kleinbard D., *Through a Latte Darkly: Starbucks's Stateless Income Planning*, 139 Tax Notes 1515, 1522, (2013).

[141] Andrew Stanek-Blair, *Intellectual Property Solutions to Tax Avoidance*, 62 UCLA Law Review, 2, 15, (2015)

[142] Special Report: How Starbucks Avoids UK Taxes, Monday October 15, 2002, http://uk.reuters.com/article/uk-britain-starbucks-tax-idUKBRE89E0EW20121015 (Accessed on 25 January 2017)

[143] Peter Conell, *Ending the Free Ride, Making Multinationals Pay Their Way*, 17, (London:Civitas, November 2014).

Starbucks established a subsidiary in the Netherlands which was the only company responsible for its trade activities in Europe, Africa and the Middle East. Starbucks Manufacturing BV which is a resident in the Netherlands is responsible for roasting the coffee beans which are used in the brand's outlets in the aforementioned regions. The beans are bought by the Switzerland subsidiary of the group and then re-sold to the other members of the group. The costs for the cross-selling of beans are added to the royalty payments for the use of intellectual property. The tax ruling issued by the Dutch authorities in 2008 gave a selective advantage to Starbucks Manufacturing, which has unduly reduced its tax burden since 2008 by €20 - €30 million. In particular, the ruling artificially lowered taxes paid by Starbucks Manufacturing in two ways. Firstly, Starbucks Manufacturing paid a very substantial royalty to Alki which is a UK-based company in the Starbucks group for coffee-roasting know-how. Since, the intellectual property rights of Starbucks are not located in the Netherlands, the royalties for them cannot be taxed in the Netherlands. That reduced the tax which was to be paid in the Netherlands. The Commission's investigation established that the royalty paid by Starbucks Manufacturing to Alki cannot be justified as it does not adequately reflect market value. In fact, only Starbucks Manufacturing is required to pay for using this know-how – no other Starbucks group company nor independent roasters to which roasting is outsourced are required to pay a royalty for using the same know-how in essentially the same situation. In the case of Starbucks Manufacturing, however, the existence and level of the royalty means that a large part of its taxable profits are unduly shifted to Alki, which is neither liable to pay corporate tax in the UK, nor in the Netherlands.

Secondly, it paid an inflated price for green coffee beans to the Switzerland-based Starbucks Coffee Trading SARL[144]. In fact, the margin on the beans has more than tripled since 2011. Due to this high key cost factor in coffee roasting, Starbucks Manufacturing's coffee roasting activities alone would not actually generate sufficient profits to pay the royalty for coffee-roasting know-how to Alki. The royalty therefore mainly shifts to Alki profits generated from sales of other products sold to the Starbucks outlets, such as tea, pastries and cups, which represent most of the turnover of Starbucks Manufacturing[145].

In 2008 it got a tax ruling from the Dutch tax authorities fixing "its remuneration as a mark up of 9-12% on a defined cost base"146. The Commission challenged the outcome of the Advanced Pricing Agreement between the Dutch Tax Authorities and Starbucks. It found that this "tax ruling issued by the respective national tax authority artificially lowered the tax paid by the company"[147]. The Commission concluded that, "the tax ruling endorsed artificial and complex methods to establish taxable profits for the companies. They do not reflect economic reality. This is done, in particular, by setting prices for goods and services sold between companies of the Starbucks group -so-called "transfer prices"- that do not correspond to

[144] See: EU Focus, *Commission Decision, Selective Tax Advantages for Fiat in Luxembourg and Starbucks in Netherlands declared illegal*, 338, 22-24 (EU Focus 2015).

[145] See: SA.38374 *State aid implemented by the Netherlands to Starbucks*, http://ec.europa.eu/competition/elojade/isef/case_details.cfm?proc_code=3_SA_38374

[146] Richard Lyal, *Transfer Pricing Rules and State Aid*, 38(4) Fordham International Law Journal, 1026, (2015).

[147] *Commission decides selective tax advantages for Fiat in Luxembourg and Starbucks in the Netherlands are illegal under EU state aid rules*, Brussels 21 October 2015, See: http://europa.eu/rapid/press-release_IP-15-5880_en.htm (accessed on 25 January 2017)

market conditions. As a result, most of the profits of Starbucks' coffee roasting company are shifted abroad, where they are also not taxed"[148]. Therefore, the Commission has ordered the Netherlands to recover the unpaid tax from Starbucks in order to remove the unfair competitive advantage they have enjoyed and to restore equal treatment with other companies in similar situations. The amounts to recover are €20 - €30 million. It also means that the companies can no longer continue to benefit from the advantageous tax treatment granted by these tax rulings.

The Case of Google

Google has been the centre of controversy too when using similar tax avoidance schemes. The House of Commons report on Google stated that "to avoid UK corporation tax, Google relies on the deeply unconvincing argument that its sales to UK clients take place in Ireland, despite clear evidence that the vast majority of sales activity takes place in the UK"[149]. The committee accepted that Google generated US $18 billion revenue from the UK between 2006 and 2011. The company paid the equivalent of just US $16 million of UK corporation taxes in the same period. Google defends its tax position by claiming that its sales of advertising space to UK clients take place in Ireland. This was found to be deeply unconvincing on the basis of evidence that, despite sales being billed from Ireland, staff in the UK generated most of the sales revenue. It is quite clear that sales to UK clients were the primary purpose, responsibility and result of its UK operation, and that the processing of sales through Google Ireland has no purpose other than to avoid UK corporation tax. This elaborate corporate construct has damaged Google's reputation in the UK and undermined confidence in the effectiveness of HMRC. Google also conceded that its engineers in the UK are contributing to product development and creating economic value in the UK[150]. Google's tax avoidance scheme used the famous "double Irish Dutch sandwich"[151]. This is because the scheme[152] involved two Irish affiliates and a Dutch shell company[153]. Google US moved part of it intellectual property namely its search and advertisement technologies to a subsidiary named Google Holdings. Google Holdings was incorporated in Ireland, but it is controlled and managed by another Google company in Bermuda. Therefore, as explained before it is

[148] *Commission decides selective tax advantages for Fiat in Luxembourg and Starbucks in the Netherlands are illegal under EU state aid rules*, Brussels 21 October 2015, See:http://europa.eu/rapid/press-release_IP-15-5880_en.htm (Accessed on 25 January 2017)

[149] House of Commons, *Tax Avoidance – Google, Ninth Report*, See: https://www.publications.parliament.uk/pa/cm201314/cmselect/cmpubacc/112/112.pdf (Accessed on 25 January 2017)

[150] House of Commons, *Tax Avoidance – Google, Ninth Report*, page 5. See: https://www.publications.parliament.uk/pa/cm201314/cmselect/cmpubacc/112/112.pdf(Accessed on 25 January 2017)

[151] See Gabriel Zucman, *Taxing Across Borders: tracking personal wealth and corporate profits*, 28 (4) Journal of Economic Perspectives, (2014).

[152] See: http://www.investopedia.com/terms/d/double-irish-with-a-dutch-sandwich.asp (Accessed on 25 January 2017)

[153] See: Edward Kleinbard, *Stateless Income*, 11(9), Florida Tax Review, pages 699–774, (2011).

not a tax resident of Ireland. It is a tax resident of Bermuda. The transfer of intellectual property took place in 2003 before Google's initial public offering. We do not know if the arm's length rules were enforced as the purchase price is not public information[154]. Google's market value increased greatly since its initial public offering therefore, the company was able to move its intangibles to its offshore subsidiary for what was a low price. The Irish/Bermuda hybrid then created yet another Irish subsidiary named "Ireland Limited," to which it granted a license Google's technologies. The new subsidiary licenses Google's intellectual property to all Google affiliates in Europe, the Middle East, and Africa. Each one of the Google companies in these regions pays royalties to Ireland Limited to have the right to use the company's intangibles including its technologies. Therefore, the bulk of Google's non-US profits end up being taxable in Ireland only, where the corporate tax rate is 12.5%[155]. After that, Ireland Limited makes a royalty payment to the Bermuda subsidiary; namely to Google Holdings. The profits are therefore transferred from Ireland to Bermuda where the corporate tax is conveniently enough set at 0%. But, according to Irish tax law there is a tax which is to be imposed on royalty payments from the Irish to the Bermuda subsidiary. In order avoid this tax, "a detour by the Netherlands is necessary"[156]. Ireland Limited then pays royalties to the Dutch Google subsidiary –Google BV- a Dutch shell company. That payment is tax free since both countries are members of the EU. The Dutch shell then pays back everything to the Irish/Bermuda holding, but not it is tax-free because on the basis of Dutch tax law the holding is Irish, not Bermudian.

Tricks on the Menu: A Double Irish, Dutch Sandwiches and the Case of Apple Inc

One of the EU countries, which found itself in the centre of the controversy related to multinational, is Ireland. Ireland attracted massive investment due to its low 12.5% corporation tax rate but also due a variety of tax incentives such as the "double Irish"[157]. The "double Irish"[158] tax formula that allows companies to escape tax by allocating intellectual property rights to the Irish subsidiary. Under Irish law companies are considered tax resident

[154] Gabriel Zucman, *Taxing Across Borders: tracking personal wealth and corporate profits*, 28(4) Journal of Economic Perspectives, 125, (2014).

[155] Gabriel Zucman, *Taxing Across Borders: tracking personal wealth and corporate profits*, 28(4) Journal of Economic Perspectives, 125, (2014).

[156] Gabriel Zucman, *Taxing Across Borders: tracking personal wealth and corporate profits*, 28(4) Journal of Economic Perspectives, 126, (2014)..

[157] See: Stephen C. Loomis, *The Double Irish Sandwich: Reforming Overseas Tax Havens*, 43 Saint Mary's Law Journal, 825, (2012).

[158] The double Irish exploits the different definitions of corporate residency in Ireland and the US. Dublin taxes companies if they are controlled and managed in Ireland, while the US' definition of tax residency is based on where a corporation is registered. Companies exploiting the double Irish put their intellectual property into an Irish-registered company that is controlled from a tax haven such as Bermuda. Ireland considers the company to be tax-resident in Bermuda, while the US considers it to be tax-resident in Ireland. The result is that when royalty payments are sent to the company, they go untaxed - unless or until the money is eventually sent home to the US parent company. See: https://www.ft.com/content/f7a2b958-4fc8-11e4-908e-00144feab7de (accessed on 5 February 2017).

if they are controlled or managed in Ireland[159]. Therefore, foreign companies incorporated in Ireland can escape Irish tax residency as long as they were managed and controlled by a company established in another country. Therefore, some companies are "tax resident in Ireland for some tax purposes, but are not tax resident for corporate tax payments"[160].

Apple established two subsidiaries in Ireland; namely Apple Operations Europe (AOE) and Apple Sales International (ASI). AOE provides services for Apple companies in Europe, the Middle East and Africa. ASI buys Apple brand products from manufacturers and sells them on to companies within the Apple group. They hold the right to use and sell Apple's intellectual property outside America under a so-called cost-sharing agreement with Apple Inc. According to that, ASI has "economic rights to Apple's intellectual property"[161] outside the Americas; the legal ownership of intellectual property rests with Apple Inc. Under this agreement the two Irish subsidiaries made annual payments to Apple in the USA to fund research and development conducted on behalf of the Irish companies in the USA. These payments amounted to $2 billion in 2011 and then significantly increased in 2014[162]. These payments contributed to fund more than half of all research by the Apple group in the USA to develop its intellectual property worldwide[163]. According to the Irish law these expenses are deducted from the profits recorded by the Irish subsidiaries. ASI "enjoys the perfect complementary definition of corporate tax residence in Ireland and in the USA and it is not a tax resident of any country"[164]. This is because the definition of tax residence in Ireland appears to be the "perfect partner"[165] for the USA. ASI is not a resident of Ireland, because its central management and control is in the USA. But, it is not a resident of the USA either because it is not incorporated in the USA[166]. Therefore, the two subsidiaries were "stateless

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[159] See Philip Brennan, *Tax Acts 2016: Income Tax, Corporation Tax, Capital Gains Tax,* (London : Bloomsbury Professional, 2016).

[160] Jim Stewart, *Is Ireland a Tax Heaven*?, IIIS Discussion Paper No.430, 6, (July 2013), See: https://www.tcd.ie/iiis/documents/discussion/pdfs/iiisdp430.pdf (Accessed on 15 February 2017)

[161] Antony Ting, *iTax – Apple's International Tax Structure and the Double Non-Taxation Issue*, 1 British Tax Review, 44, (2014).

[162] See: *Commission rules that Ireland gave illegal tax benefits to Apple worth up to EUR 13 billion*, (EU Focus 2016), Commission Decision, 348, pages 26-28.

[163] See: *Commission rules that Ireland gave illegal tax benefits to Apple worth up to EUR 13 billion*, (EU Focus 2016), Commission Decision, 348, pages 26-28. .

[164] Antony Ting, *iTax – Apple's International Tax Structure and the Double Non-Taxation Issue*, 1 British Tax Review, 44, (2014).

[165] Antony Ting, *iTax – Apple's International Tax Structure and the Double Non-Taxation Issue*, 1 British Tax Review, 44, (2014).

[166]In May 2017 the EU took a major step in tackling tax avoidance via non-EU countries by addressing the "hybrid-mismatches" between tax systems of an EU with a non-EU country like in this case. As explained at this part of the article one of the most common tools for tax avoidance on the part of the multinationals is to exploit the disparities between EU and non-EU jurisdictions so as to reduce their tax payments. The example of Apple and the mismatch between the Irish and the USA tax system emphasises the need to address this issue. The directive on hybrid mismatches complements and amends the Anti-Tax Avoidance Directive of 12 July

companies"[167]. As a result they were treated as a branch in Ireland and they were subject to tax only on the trading income attributable to that branch[168]. The Irish authorities agreed that the majority of ASI's profits should be allocated to its head office. Only, this is a problem, because the head office, according to the Commission's assessment, existed only on paper and could not have generated such sums. The head office was not based in any country and it did not have any employees or premises. The only recorded activities were occasional board meetings. At the time of the EU investigation in 2014, the head offices' profits were not subject to any tax in any country under provisions of the Irish law that was no longer in force[169]. As a result of that although in 2011 ASI recorded a profit of 16 billion Euros only 50 million of them were charged as tax in Ireland[170]. The greatest part of its profits was simply untaxed. The Commission opened investigations in 2014 regarding the allocation of profits between the two subsidiaries. The Commission found that the artificial allocation of profits was not reflective of the arm's length principle and therefore they constituted unlawful state aid.[171] A 1991 ruling by the Irish tax authorities "set its net profit at 12.5% of branch operating costs...and since 2007 its profits are deemed to be 8-18% of branch operating costs"[172]. The Commission found that the Irish tax authorities paid insufficient regard to the changing economic environment since 1991; the Irish authorities had substantially and artificially lowered the tax paid by Apple since 1991[173]. The tax ruling was renewed on very similar terms in 2007 and it was terminated in 2015. As a result of these rulings, Apple paid a tax rate of only 0,005% in 2014 on the profits of ASI down from an anyway low 1% in

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2016 (EU) 2016/1164 which is applicable within the Single Market. See the *Council Directive on Hybrid Mismatches* at: http://data.consilium.europa.eu/doc/document/ST-6661-2017-INIT/en/pdf

[167] See: *Apple to repay Ireland 13billion of unlawful state aid*, 5(6), Compliance & Risk, 17, (2015).

[168] See: *Apple to repay Ireland 13billion of unlawful state aid*, 5(6), Compliance & Risk, 17, (2015)..

[169] See: *Ireland gave illegal tax benefits to Apple worth up to £13 billion*, 37(12), Commission Decision, Company Lawyer, 377-378, (2016).

[170] See: *Apple to repay Ireland 13billion of unlawful state aid*, 5(6), Compliance & Risk, 18, (2015)..

[171] *Article 107(1) of the TFEU* prohibits "any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods shall, in so far as it affects trade between Member States, be incompatible with the internal market". The CJEU clarified from an early stage that "the concept of aid is...wider than that of a subsidy because it embraces...interventions which...mitigate the charges which are normally included in the budget of an undertaking and which...are similar in character and effect to subsidies" Any alleviation of a financial burden that would normally been borne by the undertaking could be considered to be entering the ambit of a state aid. Therefore, schemes which enable tax avoidance are increasingly linked to state aid. In any case, it was clear from a very early point that the Court will not focus on the name or aim of the measure but on its effect[171]. This is one of the main principles of the internal market in any case. See: *Commission v Italy*, Case 173/73, [1974] ECR 709.

[172] Richard Lyal, *Transfer Pricing Rules and State Aid,* 38(4) Fordham International Law Journal, , 1023, (2015).

[173] See: *Ireland gave illegal tax benefits to Apple worth up to £13 billion*, 37(12), Commission Decision, Company Lawyer, 377-378, (2016).

2003[174]. Apple recorded in Ireland the entire set of profits made by sales of Apple products in the entire EU single market[175]. Apple used the low tax rates and IP transfer mispricing arbitrage scheme but they also used a contractual arrangement to avoid even more tax. Apple set up their sales operations in Europe in such a way so that customers were contractually buying products from ASI in Ireland rather than from the shops which sold those products to customers across the EU[176]. The Commission concluded that the Irish authorities had benefited Apple by ignoring the arm's length principle and therefore ordered Ireland to recover 13 billion Euros of unlawful state aid plus interest between 2003 to 2014. Apple was illegally given a significant advantage over other businesses which were operating under the same national tax rules.

The extension of the EU state aid rules to such cases is an important tool which aims at catching tax avoidance of such a scale. The state aid criteria in this case were all met. The 1991 and 2007 rulings were issued by a state; Ireland. Ireland used state resources to provide an advantage to a private firm; namely the foregone potential tax revenues due to the corporate schemes in question. This policy obviously distorts competition and affects trade between member states as investment, which would otherwise, been diverted to other members of the union rested in Ireland due to the tax avoidance schemes. Apple and other multinationals were granted a selective advantage, which was not available to taxpayers in a similar or comparable situation. The arm's length principle was clearly violated within the context of the intra-group transactions contributing to levels of tax that were simply unacceptable. That granted Apple a significant advantage in its competition to local firms which had to bear the regular tax burden provided for by law. Advance pricing agreements where transfer pricing is confirmed by tax authorities can constitute state aid on the basis of article 107TFEU since any "relief from tax is inevitably financed by the State or granted through State resources if they confer an economic advantage on a selective group of undertakings that distorts competition and affects trade"[177]. The use of the arm's length principle by the Commission is an important element of its strategy against tax avoidance as it allows it to catch practices, which albeit in compliance with the local law, are in violation of the principle in question. Therefore, if the intra-group transactions are set at a price, which

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[174] See: *Ireland gave illegal tax benefits to Apple worth up to £13 billion*, 37(12), Commission Decision, Company Lawyer, 377-378, (2016).

[175] The issues of tax avoidance and its effect on the internal market were dealt with a new EU directive based on the OECD BEPS principle. The *Directive (EU) 2016/1164 of July 2016* laying down rules against tax avoidance practices that directly affect the functioning of the internal market. The directive is a step towards adopting an EU-wide policy against tax avoidance. It covers many areas of concern including the so-called hybrid mismatches. See: *Recital number 13 of the Directive*. See: http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32016L1164&from=EN See: CedelleAnzhella, The EU Anti-Tax Avoidance Directive: a UK Perspective, British Tax Review, 2016, page 490.

In February 2017 there was a new proposal for a Council Directive to amend Directive (EU) 2016/1164 as regards hybrid mismatches with third countries

[176] See: See: *Commission rules that Ireland gave illegal tax benefits to Apple worth up to EUR 13 billion*, (EU Focus 2016), Commission Decision, 348, pages 26-28.

[177] Liza Gormsen Lovdahl, *EU State Aid Law and Transfer Pricing: A Critical Introduction to a New Saga*, 7 (6) Journal of European Competition Law & Practice, 369 (2016).

is not reflective of their market value, the Commission can look at this case. This is because these transactions conceal a corporate strategy aiming at tax avoidance,. Although the arm's length principle is not well defined or pellucid, if it was not in place, then the case would have been dismissed as it did not violate the national law. The arm's length principle is yet to be defined in its total precision however, the fluidity in setting all its parameters in detail allows the Commission to catch more cases on such a basis. As a concept it was formulated in *Belgian Coordination*[178] cases, where the court held that a tax scheme which deviates from the general tax system confers an economic advantage if the tax base under that scheme is composed in such a way that it cannot resemble the tax base under the general scheme. Therefore, embarking from a vague basis the EU constructed the arm's length principle in a flexible enough manner to catch corporate schemes, which lead to significant tax avoidance. This importance since on the basis of these seemingly lawful yet controversial to say at least tax schemes large multinational groups appear to have rendered the "payment of full or even reasonable taxes a relic of the past"[179].

The amount of unpaid taxes to be recovered by the Irish authorities would be reduced if other countries were to require Apple to pay more taxes on the profits recorded by Apple Sales International and Apple Operations Europe for this period in their jurisdictions. This is because the taxable profits of Apple Sales International in Ireland would be reduced if profits were recorded and taxed in other countries instead of being recorded in Ireland. The amount of unpaid taxes to be recovered by the Irish authorities would also be reduced if the US authorities were to require Apple to pay larger amounts of money to their US parent company for this period to finance research and development efforts[180].

Similarly in the USA, the Senate confirmed that, "sending valuable intellectual property rights offshore together with the profits that follow those rights is at the heart of Apple's tax avoidance strategy"[181]. Apple Inc. has created three offshore corporations, entities that receive tens of billions of dollars in income, but which have no tax residence—not in Ireland, where they are incorporated, and not in the United States, where the Apple executives who run them are located. Apple has arranged matters so that it can claim that these ghost companies, for tax purposes, exist nowhere. One has paid no corporate income tax to any nation for the last 5 years; another pays tax to Ireland equivalent to a tiny fraction of 1

[178] Joined *Cases C-182/03 and C-217/03, Kingdom of Belgium and Forum 187 ASBL v Commission of the European Communities,* 2006 I-05479.

[179] Sara Dillon, *Tax Avoidance, Revenue Starvation and the Age of the Multinational Corporation*, Legal Studies Research Paper Series, Research Paper 16-18, Suffolk University Law School, 2, (December 13th 2016).

[180] See the *Commission Decision of 30/8/2016* at: http://ec.europa.eu/competition/state_aid/cases/253200/253200_1851004_666_2.pdf (Accessed on 25 February 2017)

[181] *Offshore Profit Shifting And The U.S Tax Code*—Part 2 (Apple INC.), Hearing before the Permanent Subcommittee On Investigations, May 21st 2013, page 2 See: https://www.gpo.gov/fdsys/pkg/CHRG-113shrg81657/pdf/CHRG-113shrg81657.pdf (Accessed on 25 February 2017)

percent of its total income[182]. As we have seen, the European Commission stated that tax arrangements made by Ireland for Apple amounted to an unlawful state aid under the EU laand .in hearings before the United States Senate it was revealed that these "practices have allowed U.S.-based multinational corporations to amass an estimated $1.9 trillion in profits in offshore tax havens, shielded from U.S. taxes...there is a direct relationship between this rapidly accelerating shift of corporate profits offshore, on the one hand; and on the other, a worrisome Federal deficit fed in part by a decline in the contributions corporate taxes make to Federal revenue"[183].

It is time for change.

The cases studies were indicative of the need to reform the law. Although, it is evident that corporate activities of this type lead to large-scale tax avoidance, it is also clear that the latter despite its clearly unethical nature is at the very end lawful. Tax avoidance at the group level is clearly linked to their ability to manipulate their institutional structures so as to shift profits from one member of the group to the other and perform transactions at artificially low prices. Tax avoidance is therefore clearly institutionalised. Company law allows practices which albeit morally questionable, economically detrimental and socially damaging they are at the end legitimate. Company law provides the MNEs with the legal tools to avoid paying tax, deprive public services from important sources of funding and fuel inequality which generates public discontent; the latter undermines the political system as it is normally channelled towards voting for extreme political forces with a populist agenda.

Therefore, there is a need to change course and reform these aspects of company law that allow corporate groups to transfer profits among their members and escape taxation in potentially all the jurisdictions involved. It is clear that the issue extends further than shifting of profits to low tax jurisdictions such as Ireland. The law provides the groups with the ability to actually by-pass even the obligation to pay the minimum tax-rate which is set by Ireland by using the set of tricks which were explained in the relevant part of the article. The members of the EU are free to set any tax rate they perceive as appropriate for their economy; this is a matter of national sovereignty. So, the need for change of law and policy does not flow from the fact that the EU has members with different rates of taxation but that, corporate groups are allowed to avoid paying tax even in the low-tax EU members. Corporate groups by nature and by definition have a trans-national character since they are present in multiple jurisdictions and they can therefore exploit the legal loopholes inherent in a multiplicity of legal orders. Therefore, a trans-national solution should be sought. And while company law

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[182] *Offshore Profit Shifting And The U.S Tax Code*—Part 2 (Apple INC.), Hearing before the Permanent Subcommittee On Investigations, May 21st 2013, page 3 See: https://www.gpo.gov/fdsys/pkg/CHRG-113shrg81657/pdf/CHRG-113shrg81657.pdf (Accessed on 25 February 2017)

[183] *Offshore Profit Shifting And The U.S Tax Code*—Part 2 (Apple INC.), Hearing before the Permanent Subcommittee On Investigations, May 21st 2013, page 2. See: https://www.gpo.gov/fdsys/pkg/CHRG-113shrg81657/pdf/CHRG-113shrg81657.pdf (Accessed on 25 February 2017)

remains national in the sense that it has not been harmonised at the EU level[184], the principles of separate legal personality and limited liability constitute the fundamental features of company law in all member states of the EU. The article argues that they are indeed fundamental and they should be safeguarded at the level of the single company as they guarantee investment and legal certainty, but they should be revisited at the level of corporate groups in relation to their taxation. The case studies demonstrate that the two principles in question provide the groups with a controversial yet legal avenue through which they can avoid their tax obligations in a variety of jurisdictions. It is true that the EU has recently started to address this issue more seriously but the article argues that more radical reform is needed.

A positive indication towards reform was signalled by the *Cadbury Schweppes*[185]case where thegroup –based in the UK- had established two subsidiaries in Ireland solely in order to benefit from the more favourable tax regime there. The issue here was whether a member state of the EU would be in a position to prevent companies established in its territory from availing themselves of a more favourable tax regime in another member state or whether this would be against the freedom of establishment which is one of the fundamental freedoms of the internal market. The British government argued that it was aiming at countering a specific type of tax avoidance involving the artificial transfer by a resident company of profits from the Member State in which they were made to a low-tax State by means of the establishment of a subsidiary in that State and the effecting of transactions intended primarily to make such a transfer to that subsidiary. The CJEU stated that a national measure restricting the freedom of establishment may be justified where it specifically relates to "wholly artificial arrangements" aimed at circumventing the application of the legislation of the Member State concerned. It follows that, in order for a restriction on the freedom of establishment to be justified on the ground of prevention of abusive practices, the specific objective of such a restriction must be to prevent conduct involving the creation of wholly artificial arrangements which do not reflect economic reality, with a view to escaping the taxnormally due on the profits generated by activities carried out on national territory[186]. This phrase "wholly artificial arrangements" could be an extremely important tool for combating aggressive tax avoidance in any national law. It provides a template to divide moral tax avoidance from immoral tax avoidance. This is a very complicated issue because many national laws include tax avoidance mechanisms as a way to incentivise savers but the difficulties are legion because finding the cut-off between moral tax avoidance and immoral schemes are inherently problematic. [187]In Cadbury Schweppes case, the Court explained that practices such as arranging transfers of losses, within a group of companies, to companies established in the

[184] The EU has introduced the "Societas Europaea" legal form, which is largely governed by EU law, but this is the only legal form for profit-making businesses introduced by the EU; its own regulation is partly left to national company laws

[185]C-196/04 *Cadbury Schweppes plc, Cadbury Schweppes Overseas Ltd v Commissioners of Inland Revenue*

[186] Paragraph 55 of the judgement.

[187] Tax Justice Network: "Tax Avoidance", http://www.taxjustice.net/faq/tax-avoidance/, (accessed on 16 July 2017). The Network argues that some tax avoidance mechanisms are moral, citing the UK Individual Savings Account (ISA), where the British tax system allows people to save up to a certain amount of money each year, and be exempt from tax on the savings income. This zero percent tax rate is analogous to the zero percent tax rate that any progressive tax system levies on the first portion of a citizen's income: it is just the tax rate.

Member States which apply the highest rates of taxation and in which the tax value of those losses is therefore the highest undermine the right of the Member States to exercise their tax jurisdiction in relation to the activities carried out in their territory and thus to jeopardise a balanced allocation between Member States of the power to impose taxes[188]. These practices have no purpose other than to escape the tax normally due on the profits generated by activities carried on in national territory. Therefore, if checking those factors leads to the finding that the subsidiary is a fictitious establishment not carrying out any genuine economic activity in the territory of the host Member State, the creation of that subsidiary must be regarded as having the characteristics of a wholly artificial arrangement.Therefore, article 49TFEU on the freedom of establishment must be interpreted as precluding the inclusion in the tax base of a resident company established in a Member State of profits made by a subsidiary in another Member State, where those profits are subject in that State to a lower level of taxation than that applicable in the first State, *unless* such inclusion relates only to wholly artificial arrangements intended to escape the national tax normally payable.
If this principle is applied to the cases of Starbucks, Google and Apple it will lead to the spectacular increase of their taxable profits as the use of "artificial arrangements" and other legally-safe tricks has significantly decreased the tax they ought to pay. This also shows the difficulty in establishing a link between the parent and its subsidiary company. Should there is proof or indication that the subsidiary is not an establishment which participates in a stable and continuous basis in the economic life of a member state the veil, should be lifted and the profits of the subsidiary should be dealt with as the profits of the parent especially since they were generated in the jurisdiction where the parent is established. The legal privileges, which are absolutely essential for single companies, cannot be misused by groups to legally engage in tax avoidance.
The case studies demonstrated the need to enforce a system where the profits generated by a company in a specific country should be taxed by that jurisdiction. When they are transferred around the members of the corporate group on the basis of artificial exchanges related to intellectual property rights or transactions in abuse of the arm's length principle then at the very end the profits in question are not taxed in any jurisdiction including the low-tax one. In June 2017 the European Commission resurrected its plans for a so-called Common Consolidated Corporate Tax Base (CCCTB) which consists of two proposals one on Common Corporate Tax Base (CCTB) and the other on Common Consolidated Corporate Tax Base (CCCTB)[189]. Both proposals can pass only on the basis of unanimity. The CCTB will introduce new ways of calculating where a company actually makes its money. The formula looks at where the value is created, based on three equally weighted factors: assets, labour and sales. The CCCTBwould put a single member state in charge of collecting all European taxes due from a particular company. Those revenues would then be shared among the other member states according to where the profits were made. The EU would first have to agree upon the CCTB and then move on to the CCCTB.
The package was proposed by the European Commission in 2011 as a single set of rules that cross-border companies could use to calculate their taxable profits in the EU, instead of

[188] Paragraph 56 of the judgement

[189] See: http://www.europarl.europa.eu/RegData/etudes/BRIE/2017/595907/EPRS_BRI(2017)595907_EN.pdf andhttp://europa.eu/rapid/press-release_IP-16-3471_en.htm (Accessed on 25June 2017)

needing to deal with 28 different national systems; this is specific to calculating corporate groups' profits rather than harmonising tax rates which falls within the member states' national sovereignty. At that point, it was opposed by the UK and Ireland and it was shelved. With the departure of the UK from the EU, the EU re-launched the initiative in 2017. There is a focus now on companies paying taxes in the countries where economic activity takes place and profits are generatedvia an apportionment formula which is to be introduced through the new CCCTB proposal. The rules are aimed at ensuring that business profits are taxed in the jurisdiction where value is actually createdmaking it harder for multinationals to avoid tax by transferring intangibles such as brand or intellectual property to low-tax jurisdictions. The proposals include a number of anti-tax avoidance measures that are to be formulated and shaped on the basis of consultation between member states. It would be compulsory for corporations with annual turnover of more than €750m which are tax-resident in an EU country. This is a very good starting point. It should however be complemented with what would be a major reform; that is the explicit removal of the corporate veil in cases where the profits generated by the mother company in its jurisdiction are transferred to its subsidiary which does not constitute an establishment which participates in a stable and continuous basis in the economic life of a member state on the basis of artificial arrangements. In this case the profits should be taxed by the jurisdiction of the mother in their entirety.

Conclusion

The article argued for the fair participation in the tax burden not only of individuals or small and medium sized companies, but also of larger companies and groups. Although the tax avoidance schemes were legal it is clear that government services are hit if the biggest companies do not pay tax. Groups, due to their structures and trans-jurisdictional nature can escape taxation in all jurisdictions involved. Groups can benefit from their jurisdictional arbitrage by using their institutional structures so as to shift profits from one member of the group to the other and perform transactions at artificially low prices. Therefore, it is clear that the so-called "organisational decoupling" of the group in different jurisdictions results in tax avoidance. Groups can attain significant tax avoidance using a web of intra-company loans, transfer agreements, intellectual property and other undoubtedly legal tools which can relieve the parent from many regulatory or tax burdens. The case studies which are examined in this article demonstrate the significance of the problem. The three companies in question are all prominent and 'reputable' corporations in their distinctive fields. Despite their high-profile corporate brand and international profile, the multinationals in question took advantage of their structures and shifted their profits among the members of the group in order to avoid tax. Company law provided them with the tools which enable tax avoidance. Therefore, there is a need to change course and reform these aspects of company law that allow corporate groups to transfer profits among their members and escape taxation in potentially all the jurisdictions involved.

Corporate groups by nature and by definition have a trans-national character since they are present in multiple jurisdictions and they can therefore exploit the legal loopholes inherent in a multiplicity of legal orders. Therefore, a trans-national solution should be sought. And while company law remains national in the sense that it has not been significantly harmonised at the EU level, the principles of separate legal personality and limited liability constitute the fundamental features of company law in all member states of the EU. The article argues that they are indeed fundamental and they should be safeguarded at the level of the single company, but they should be revisited at the level of corporate groups in relation to their taxation. The potential new EU developments and initiatives in this field are consistent with the main argument of this article which is that the law should be reformed so that it puts an end to the institutionalised tax avoidance on the part of corporate groups. The profits of the members of the group should be taxed by the jurisdiction where they are generated. Each member of the group should be viewed as established in the member state where it operates with its revenues shielded and -most importantly- taxed in that jurisdiction. When this proves to be too difficult or complicated, the corporate veil should be lifted altogether and the mother company of the group should be taxed for the entire set of profits made by all the members of the group in the EU. That would be a significant step towards creating a regulatory system that will ensure the fair participation of every individual and company in the tax burden.