

New State aid investigation into Dutch Ruling practice: Nike

Introduction

On 10 January 2019, the European Commission (“EC”) opened a formal State aid investigation into tax rulings granted by the Dutch tax authorities (“DTA”) to two Nike group companies, European Operations Netherlands BV and Converse Netherlands BV (“DutchCo’s”).

The EC wishes to examine whether DutchCo’s were given, as a result of the tax rulings granted by DTA, a selective advantage that distorted competition within the EU’s internal market, in breach of EU state aid rules.

Nike structure



The DutchCo’s develop, market and record the sales of Nike and Converse products in Europe, the Middle East and Africa (the EMEA region).

To perform such activities the DutchCo’s obtained through a license agreement the right to use intellectual property (“IP”) relating to Nike and Converse products in the EMEA region. Pursuant to the license agreement the DutchCo’s paid a (tax deductible) royalty to the IP owners. The IP owner’s, however, were two Dutch tax-transparent partnerships.

The rulings under investigation were granted from 2006 to 2015 by the DTA (two of which are still in force) and refer to the transfer pricing method used to calculate the royalty payments made by Nike European Operations Netherlands and Converse Netherlands for the use of the IP.

As a result of the transfer pricing method endorsed by the rulings, the OpCo's were taxed in the Netherlands on their operating margin based on sales, which the Dutch tax authorities considered at arm's length.

The investigation

Once again the EC question's tax ruling concerning royalties payments made by European companies of US multinationals group.

The EC is concerned that *"the royalty payments endorsed by the rulings may not reflect economic reality. They appear to be higher than what independent companies negotiating on market terms would have agreed between themselves in accordance with the arm's length principle"*.

The EC indicates that the IP owners *"have no employees and do not carry out any economic activity"* whereas the DutchCo's have more than 1,000 employees and performs the development, management and exploitation of the IP. The EC's also highlights that the OpCo's carry out and bear the costs of marketing and sales activities.

The main point of focus seems to be that the remuneration paid by the DutchCo's is not aligned neither with the substance of the IP owners nor with the functions (or perhaps the lack thereof) performed by the IP owners to what regards the IP.

In essence the EC seems to question whether under transfer pricing method endorsed in the tax ruling (Transactional Net Margin Method) the IP owners should have been left with the residual profit and the DutchCo's with a "limited operating margin".

Under the current TP Guidelines in force in the Netherlands, the DEMPE functions are key to allocate profits related to the IP, where legal ownership of the IP itself, does not confer any rights ultimately to retain returns derived by exploiting the IP.

Conclusion

The opening of an in-depth investigation does not mean that an illegal aid was granted, as can be seen from the MC Donalds case.

However, from the wording of the press release, the present case seems to be similar to Starbucks where the EC proceeds to judge the existence of an aid based on its own interpretation of the arm's length principle and also on the application of post-Beps standards for the remuneration of IP (reference to DEMPE functions is subtle but undeniably there) to pre-Beps arrangements.

Nonetheless, the opening of an in-depth investigation gives the Netherlands and interested third parties an opportunity to submit comments.