FRIENDS WITHOUT BENEFITS?: THE U.S. TREASURY WHITE PAPER ON THE EU STATE AID CASES

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I. INTRODUCTION

On August 24, 2016, the U.S. Treasury Department issued a White Paper[1] condemning recent "state aid" investigations by the European Commission ("EC"), pertaining to advance transfer pricing rulings that particular EU countries had issued with respect to U.S. and other corporate taxpayers.[2] The White Paper represents a good-faith effort to advance the interests of the American people, which after all is the Treasury's job in the international arena. However its arguments, when evaluated from a neutral perspective rather than a self-interested one, are generally unpersuasive. Moreover, the underlying tactical judgment about where America's interests lie in responding to the state aid cases, while not clearly wrong, is at least questionable.

When I was a law student, my tax professor, the great Marvin Chirelstein, used to ask students in his classes questions in the form of, "Would you argue X?" If the student hesitated, Chirelstein might add: "For a fee, I mean. Would you argue X for a fee?"

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[1] U.S. Department of the Treasury White Paper, The European Commission's Recent State Aid Investigations of Transfer Pricing Rulings (August 24, 2016).

[2] The particular EC investigations that the White Paper, supra at 2-3, mentions pertain to (a) Apple and Ireland, (b) Starbucks and the Netherlands, (c) Fiat and Luxembourg, and (d) Amazon and Luxembourg. The White Paper suggests, however, that other such investigations may be forthcoming. See id. at 3 (noting the possibility that the EC's state aid cases may "continue[] on their present trajectory").

In addition to keeping us amused by saying this, and perhaps expressing a degree of cynicism about legal practice, Chirelstein was giving voice to a fundamental point about legal advocacy. In general, there are (a) arguments one truly agrees with, (b) arguments one finds preposterous, and (c) arguments in a middle range, where one disagrees but believes that they can be advanced in good faith by reasonable people. Those who engage in legal advocacy as a profession generally cannot restrict themselves to Category A. While they may face ethical issues with regard to Category B, they really cannot avoid Category C. Imagine, for example, that you were a Supreme Court advocate in a pending case, and believed that only three members of the Court could be persuaded that your side was right by Category A arguments. Two more votes, however, might be procurable if you dipped into Category C. Assuming that you couldn't simply hand the task of making those arguments to a colleague, you would be failing in your ethical duty of effective representation if you allowed your personal skepticism to keep them out of the brief and oral argument.[3]

I myself am not in the business of being someone's legal advocate. Therefore, with respect to the EU state aid cases, I can combine rejecting Treasury arguments that I would place in Category C with accepting that it is doing its job in good faith by making them. This places me in a position that may sound like arguing against American interests, but that in fact reflects the ethical duties that I face as an academic commentator. Academic ideals, as I see them, call for analyzing issues without being swayed by personal, institutional, or group self-interest – that is, honestly and neutrally

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[3] You also probably would not be obligated to drop the case – and, if you did, it would be a sure sign that you were unusual among paid legal advocates and probably should find a different line of work.

from one's own perspective, although one should always keep in mind that others may, equally honestly and neutrally, disagree.

In section II of this paper, I briefly describe the EU state aid cases, and the White Paper's three main lines of criticism. Sections III through V of the paper then address, in turn, each of those criticisms in greater detail, explaining why I generally find them either unpersuasive or immaterial. Section VI argues that the effect of the state aid cases on U.S. national self-interest – as well as on the interests of EU countries – is more complicated than the Treasury (or other U.S. critics of the cases) may recognize. Section VII offers a brief conclusion.

II. BACKGROUND TO THE EU STATE AID CASES AND THE WHITE PAPER

Article 107(1) of the Treaty on the Functioning of the European Union (TFEU) bars "any aid granted by a Member State … in any form whatsoever which distorts or threatens to distort competition" by favoring particular undertakings or items to the detriment of the proper functioning of the EU's internal market.[4] The EC has recently initiated a set of investigations regarding favorable tax rulings that U.S. and other companies obtained from particular Member States. The four investigations so far, each of which remains short of definitive resolution (at least in the EU courts), involve (a) Apple and Ireland, (b) Starbucks and the Netherlands, (c) Fiat and Luxembourg, and (d) Amazon and Luxembourg.

There may well be more EC state aid investigations of advance transfer pricing rulings, given the views expressed by EC officials in these four cases, along with the broader prevalence of practices by Member States like those which the EC condemned in

[4] Consolidated Version of the Treaty on the Functioning of the European Union, article 107(1).

the above four instances.[5] Out of the four cases that the EC has brought so far, and that the White Paper discusses, three involve U.S.-headquartered companies (Apple, Starbucks, and Amazon). The fourth company, Fiat, includes what is left of a formerly independent U.S. company (Chrysler)[6] that still has significant U.S. operations, albeit probably not comparably high levels of share ownership by U.S. individuals.

In each of the four EU state aid cases to date, the EC asserted that what it is fair to view as highly favorable advance pricing arrangements, entered into between the specified taxpayer and country, involved illegal state aid that effectively was akin to, say, illegally giving money to the companies as a way of attracting them to the issuing jurisdictions.[7] The rationale for viewing what the EC considered unduly favorable tax rulings as forms of state aid resembles that which underlies tax expenditure analysis.[8] Thus, suppose one were to specify that, under the totality of circumstances in a given case, no reasonable advance pricing arrangement could have resulted in the multinational's (via its local affiliate) paying tax of less than €100X. If the advance pricing arrangement caused the local affiliate to pay tax of only €10X, this would be

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[5] On the likelihood that there will be more EU state aid cases, see, e.g., Mindy Herzfeld, *How BEPS Brought on the State Aid Investigations*, Tax Notes International, June 6, 2016.

[6] Chrysler was a U.S. company until it merged into a German company, Daimler, in 1998. Chrysler entered bankruptcy (and received U.S. government bailout aid) in 2009, and was acquired by Fiat during the period from 2011 to 2014.

[7] This view arguably is supported by the way that the EU countries under investigation are said to have made the challenged advance transfer pricing rulings. Edward Kleinbard has noted: "As I read the EC's 2014 preliminary report on its state aid investigation of Ireland and Apple, for example, the EC's argument is that these agreements were not tax administration agreements at all – they were shams designed to resemble tax agreements so as to deliver state aid in a manner that would on their face pass muster as confidential tax cases solely within the purview of a member state. As reported by the EC, in its APA process Apple did not produce comparables or propose a transfer pricing methodology so much as it simply negotiated to a number. Apple described how many employees it maintained in Ireland, observed that it was reviewing its worldwide operations, and then negotiated an APA that in part was "reverse engineered so as to arrive at a taxable income of around USD [28-38] million, although [this figure] . . . . does not have any economic basis." Edward D. Kleinbard, International Tax Reform Begins at Home, Testimony Prepared for Hearing on "The Global Tax Environment in 2016," U.S. House of Representatives Committee on Ways and Means, February 24, 2016.

[8] See, e.g., Daniel Shaviro, *Rethinking Tax Expenditures and Fiscal Language*, 57 Tax L. Rev. 187 (2004).

economically equivalent to the country's having combined (a) collection of the full €100X, with (b) payment to the affiliate of a direct subsidy in the amount of €90X.

Given the prominence of U.S. companies both among the EC's investigative targets to date and its suspected future targets – which in turn reflects the great success of many leading U.S. companies (such as Apple, Starbucks, and Amazon) in recent years, both in generating high profits and sales and in their international tax planning – neither the predominant direction nor the tenor of American responses comes as a great surprise. Not just U.S. policymakers, both in the Obama Administration and on Capital Hill, but also a wide swathe of American academic and other commentators on international tax policy, have been taking a strong and mainly hostile interest in the state aid cases.[9] In this regard, the White Paper is merely the latest, albeit most extended and authoritative, chapter.

In particular, the White Paper offers three extended sets of arguments against the EC's position to date in the state aid cases. First, it asserts that the cases depart from prior EU case law.[10] Second, it describes the EC as impermissibly seeking "retroactive recoveries under its new approach."[11] Third, it argues that the EC's approach in the cases is "inconsistent with international norms and undermines the international tax system."[12]

In brief, I view these arguments as follows. As to the first one, while I am not an expert on EU case law – a limitation that might also conceivably extend to U.S. Treasury personnel who worked on the White Paper – I regard the proper interpretation of such

[9] See Daniel Shaviro, *The U.S. Response to OECD-BEPS and the EU State Aid Cases*, NYU Center for Law, Economics, and Organization, Law & Economics Research Paper Series, Working Paper No. 16-27 (July 2016); White Paper at 4-5.
[10] *See* White Paper at 5-14.
[11] *See* id. at 14-17.
[12] *See* id. at 17-25.

law as generally best left to EU authorities. That said, even if one agrees that the EC's position in the state aid cases is highly novel and a departure from prior practice, this would hardly be the first time that tax law (including that in the United States) has changed significantly in response to rising policy concerns, even without legislation. What is more, the concerns that appear to underlie the state aid cases – at least, if one interprets them more charitably than as simply a revenue hunt aimed at profitable U.S. companies – make considerable sense (whether or not one ultimately agrees with them) from an EU policy standpoint. Thus, even if we choose to pursue our own strategic priorities in response to the EU's actions, we should not be surprised dismayed, or angered by its policymakers' doing things that we might have done as well under similar circumstances.

The White Paper's argument about retroactivity pretty much collapses, other than as an appeal to EU policymakers' discretion, if one accepts that the EU state aid cases might be defensible as a matter of EU law. And finally, the White Paper's critique of the relationship between the state aid cases and international tax norms rests on an overly optimistic view of how well those norms can work on the shaky base of existing transfer pricing doctrine – even in the aftermath of recent efforts to improve such doctrine[13] – combined with an overly pessimistic view of the state aid cases' long-term ramifications.

III. THE STATE AID CASES AND PRIOR EUROPEAN UNION LAW

The White Paper spends more than one-third of its overall text analyzing prior EU state aid decisions – not an area in which the U.S. Treasury Department was previously

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[13] I am referring here to the OECD/G20 Base Erosion and Profit Shifting ("BEPS") project, which attempted to shore up the feasibility of arm's length transfer pricing as an approach to income allocation between jurisdictions.

known to have developed expertise. It concludes from this analysis that the four EU state aid cases represent a significant departure from established legal doctrine in the EU.

The gist of the analysis is as follows. Previous cases and rulings establish two distinct requirements for a finding of improper state aid. The first is advantage – that is, favorable treatment of the aid's asserted recipient relative to some neutral baseline. The second is selectivity – that is, singling out particular recipients for benefits that are or would be arbitrarily denied to others. Thus, suppose it were clear that Ireland would have denied to Amazon the favorable treatment that it so eagerly granted to Apple. Then, the White Paper appears to concede, the EC would be on strong ground, tracking prior state aid doctrine, in treating the markedly favorable advance transfer pricing ruling that Ireland granted to Apple as illegal state aid. But, needless to say, there is no reason to doubt that Ireland would have been happy to accommodate Amazon as well as Apple.

The EC's doctrinal error in interpreting prior EU law, according to the White Paper, lies in its asserting that, where a highly favorable transfer pricing agreement departs from the arm's length principle, thereby substantially reducing a given multinational's taxes, "that reduction constitutes both the advantage granted by the tax measure and the [improperly selective] derogation from the system of reference."[14] To avoid legal innovation, the White Paper asserts, the EC would have had to show that *other multinational companies* would have been denied comparably favorable treatment by Ireland.

What about extending the frame of analysis from multinational firms to *all* firms conducting business in Ireland, including those that are purely domestic? The White Paper asserts that – again, as a matter of prior EU legal doctrine – favoring multinationals

[14] See id. at 8 (quoting the EC's final decisions in the Starbucks and Fiat cases).

relative to domestic companies cannot and does not constitute undue "selectivity." "Of … 65 cases cited by the Commission, none resulted in a finding [of impermissible selectivity] … solely because it resulted in disparate treatment between multinational groups and standalone companies. Instead, in each case where multinational companies were implicated, there were additional conditions that distinguished the multinational companies that benefited from those that did not."[15]

While conceding my own lack of legal expertise regarding the pre-2014 history of EU state aid doctrine,[16] I must admit to finding this line of argument singularly unimpressive. It seems to treat legal doctrine as rigid and static in a way that certainly is contrary to two-plus centuries of United States law. Can't an existing doctrine regarding selectivity be applied in a new way, in response to new developments on the ground? And isn't that inherently a part of what case law does? If a new case is wholly on all fours with prior ones, then only factual disputes could trigger a need for litigation to resolve the uncertainties. Moreover, while I recognize (albeit, departing even further from topics on which I am personally expert) that the role of courts and case law, under the continental European civil law tradition, may differ strikingly from that in the United States, the Treasury makes no arguments based on the distinction between civil law and common law systems.

Let us suppose, however, that the White Paper is correct in asserting that the four EU state aid cases depart significantly from prior precedent and practice. I am then irresistibly reminded of the following analogy. In 1935, the U.S. Supreme Court decided

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[15] White Paper at 10-11.

[16] The EC initiated its state aid investigations of the Apple, Starbucks, and Fiat cases on June 11, 2014, and added the Amazon investigation on October 7 of that year. See White Paper at 2-3.

the landmark case of *Gregory v. Helvering*,[17] establishing the business purpose doctrine and that of substance over form. These have been core principles in U.S. tax law ever since. In 1960, the Court decided *Knetsch v. United States*,[18] which arguably pushed beyond *Gregory* by holding that "sham transactions" are wholly to be disregarded by the tax system.[19] No doubt there were widespread complaints each time that these were unprecedented departures from well-established principles of U.S. tax law. They also prompted complaints – echoed by the White Paper with regard to the EU state aid cases – that the new doctrine would create significant "uncertainty" for taxpayers.[20] Yet the Internal Revenue Service had the effrontery (so to speak) to argue for these novel doctrines, and I suspect that the White Paper's authors agree with me that the Supreme Court was right to accept them.

The EU state aid doctrine reflects the concern that unequal treatment – such as allowing a given company to pay a far lower effective tax rate than other companies that operate in the same markets – will "improve the competitive position of the recipient compared to other undertakings with which it competes. For all practical purposes, a distortion of competition within the meaning of Article 107(1) of the Treaty is generally found to exist when the State grants a financial advantage to an undertaking in a … sector where there is, or could be, competition."[21]

Whatever the exact character of prior EU state aid precedents, must we assume that this broad principle can only properly be applied to protect against the apparently

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[17] 293 U.S. 465 (1935), *aff'g* 69 F.2d. 809 (2nd Cir. 1934).
[18] 364 U.S. 361 (1960).
[19] On the by now largely moot question of whether *Knetsch* merely reaffirmed, or expanded on, *Gregory*-based jurisprudence, see Walter J. Blum, *Knetsch v. United States: A Pronouncement on Tax Avoidance*, 1961 S. Ct. Rev. 135 (1961).
[20] See White Paper at 17, 20.
[21] European Commission, Communication from the Commission: Commission Notice on the notion of Stae aid as referred to in Article 107(1) TFEU (Brussels, 2016).

fictional problem that Ireland or Luxembourg might want to favor Apple relative to Amazon, or vice versa?[22] What about the very real issue, with which both EU countries and the United States have been grappling in recent years, that multinational firms have substantial tax minimization opportunities that are not generally available to standalone domestic firms? Whatever one's ultimate view on the merits regarding how multinationals should be taxed, mightn't it be reasonable – and up to the EU to decide for itself – whether a preexisting legal doctrine concerning distortion of competition can properly be applied in a novel way to the biggest current area of concern regarding tax and resulting competitive disparities? And is it really so novel for there to be legal innovation, through administrative and court action rather than just legislation, that uses familiar doctrines in new ways? Perhaps the late Justice Scalia has communicated from the grave with the U.S. Treasury Department, advancing his view that foundational legal documents are dead and static rather than living organisms.[23] But even in the United States, there is no consensus in this view's favor.

A final argument that the White Paper makes, with regard to finding undue selectivity based upon a distinction between multinationals and domestic firms, is that "the Commission has not demonstrated that a standalone company could not obtain similar rulings … simply by forming or acquiring a foreign affiliate."[24] Even aside from whether this is reasonable – or whether one would expect EU countries to welcome efforts by previously standalone firms to gut the countries' domestic tax bases through what presumably, in many cases, would either be sham or economically undesirable

[22] While Apple and Amazon have very different business models and core product and service offerings, they do, for example, compete with regard to digital music and audiobooks.
[23] See, e.g., Antonin Scalia and Bryan A. Garner, *Reading Law: The Interpretation of Legal Texts* (2012).
[24] White Paper, supra, at 14.

(apart from the tax savings) changes in their operating form – this seems willfully blind to what might well, on the face of things, be an additional policy aim that Article 107(1) advances.

The EU in relation to its Member States – like the United States in relation to our fifty lower-case states – is, among other things, an instrument for creating a large, economically integrated market. Among the advantages of creating the larger scale, with at least some degree of top-down federal-level ability to issue commands, is that it may be used to constrain tax competition between the distinct sub-units, in instances where this is considered harmful, rather than beneficial. From this perspective – and reasoning by analogy from the Commerce Clause to the United States Constitution[25] – one could understand the policy aim of using Article 107(1)'s focus on competition between businesses to advance objectives that relate to what is considered harmful tax competition between Member States.[26]

It is not really for the U.S. Treasury – or for me – to say whether this would be an appropriate use of Article 107(1) as a matter of EU law.[27] The point is simply that

[25] See United States Constitution, Article I, section 8, providing that "Congress shall have power to … regulate commerce … among the several states."

[26] As it happens, the Commerce Clause does not on its face explain why Congress should have power to regulate commerce among the several states, although it is clear that restraining intrastate tax competition is within this power. The so-called dormant commerce clause, which gives the U.S. federal courts a role in striking down state and local legislation that improperly discriminates against interstate commerce, focuses on a problem opposite to that in the EU state aid cases – favoring locals against outsiders, rather than the reverse. See, e.g., Daniel Shaviro, *An Economic and Political Look at Federalism in Taxation*, 90 Mich. L. Rev. 895 (1992). But this certainly offers no ground for Americans, inexpert on EU law, to assert that the EC and EU courts could not reasonably focus on internal tax competition.

[27] Among leading European tax academics whose published views I have consulted, Christiana HJI Panayi argues that Article 107 "is not well suited to dealing with large parts of tax avoidance in the international arena." HJI Panayi, ADVANCED ISSUES IN INTERNATIONAL AND EUROPEAN TAX LAW 280 (2015). She also more broadly questions the EC's analysis in the four state aid rulings. See id. at 278-279. On the other hand, Michael Lang helps to explain the rulings' motivation, noting: "In some countries, ruling practice … has a reputation as a framework for arrangements … which are not consistent with the law…. [R]ulings are often accused of securing benefits for the taxpayer to which the taxpayer is not entitled, under the protection of tax secrecy." Lang, *Tax Rulings and State Aid Law*, 3 British Tax Rev. 391, 392 (2015). Wolfgang Schön notes the tradeoff, central to the ongoing EU debate regarding the state aid cases,

Americans should be familiar with the types of policy concerns that might drive EU policy here, and that one should not assume can only be advanced through the legislative process (which obviously is extremely cumbersome there). We should have this in mind when evaluating legal directives that emanate from the EU. While this point does not reduce the legitimacy of our aggressively promoting our own interests in colloquy with EU policymakers, it does counsel against assuming that they must be proceeding invidiously or unreasonably.[28]

To be fair, the White Paper does not mainly argue that the EC's position in the four state aid cases is wrong as a matter of EU law – just that it is novel. But the White Paper errs in presuming that novelty itself is so novel, especially in the face of what might reasonably be perceived by EU policymakers as important policy aims. The main reason this matters pertains to its second argument, concerning retroactivity.

IV. THE STATE AID CASES AND UNDUE RETROACTIVITY

Concern about retroactivity is unambiguously at the heart of the White Paper's concern about the EU state aid cases. Had the EC authoritatively announced that, as a prospective matter, highly favorable advance transfer pricing rulings would be subject to review, the U.S. response surely would not have been so vehement. (Indeed, as I further discuss in section VI, prospective application of the EC's position has both pluses and

"between providing legal certainty and granting illegal benefits to taxpayers." Schön, *Tax Legislation and the Notion of Fiscal Aid – A Review of Five Years of European Jurisprudence*, Max Planck Institute for Tax Law and Public Finance, Working Paper 2015-14 (2015).

[28] In terms of assessing the reasonableness of the EU's actions, one question that one might ask is whether they are seeking to tax what is actually U.S. source or EU source profits. As with profits reported in tax havens generally, the question is hard to answer. The finding that the EU countries that are targets of the state aid cases failed to make reasonable transfer pricing determinations suggests that the profits were actually EU-source. However, this may have reflected prior profit-shifting by U.S. companies to create foreign-source in lieu of U.S. source income for tax accounting purposes. Of course, if the United States was concerned that these companies were improperly shifting profits out of the domestic tax base, the logical response seemingly would have been to improve our source rules or ramp up our enforcement efforts, rather than to blame someone else for being initially, but not subsequently, accommodating.

minuses from the standpoint of U.S. national self-interest.) However, application of the EC's stance to deals that were consummated before it was announced creates the prospect that the companies involved will face large financial consequences. Apple, for example, has been held by the EC to owe $14.5 billion in back taxes, over a ten-year period,[29] by reason of its arrangement in Ireland.[30] The White Paper offers evidence suggesting that the companies involved did not in fact anticipate this happening.[31] It does not address the possibility that the companies' legal advisors may have egregiously failed to recognize that a particular era's super-aggressive tax planning practices were increasingly, and inevitably, becoming "too good to be true." This, of course, strengthens the already compelling parallel between the EU state aid cases and the evolution of U.S. case law through decisions such as *Gregory v. Helvering* and *Knetsch v. United States*.

Does the EC's apparently having surprised taxpayers suggest that it is being improperly "retroactive"? Administrative and judicial determinations of what the law is generally *do* apply to pre-announcement actions, even if they involve some degree of legal novelty and innovation, and were not entirely predicted or predictable. And while it

[29] Apple, in its press release protesting the final EC decision in the Ireland case, notes that it has contributed 6,000 jobs per year to the Irish economy via its tax-subsidized presence there. If one divides the $14.5 billion in understated taxes over ten years according to the EC by 60,000 jobs (i.e., 6,000 per year for ten years), one derives a fiscal cost of more than $240 million per job per year. That is rather a lot. It is true, however, that Ireland may not actually have sacrificed so much revenue per job, given that Apple could have located its Irish activities elsewhere.

[30] $14.5 billion sounds like – and is – a lot of money. However, it merely reflects requiring Apple to pay the 12.5 percent Irish tax rate, instead of effectively zero, on more than $100 billion in profits (over ten years) that it otherwise had succeeded in placing in tax havens. So the EC penalty does not reflect applying a cripplingly high effective tax rate. Apple also has a lot of free cash that is (metaphorically, even if not literally) sitting in tax havens, and that should enable it to pay the tax, if it ultimately loses the litigation, without extreme hardship. These considerations might call for un-cueing the violins a bit, so far as the impact on Apple is concerned, even if one sides with it in the dispute.

[31] See White Paper at 15 ("None of the companies under investigation had identified the risk of Stat e aid investigations in audited financial disclosures made prior to June 11, 2014 …. Moreover, it is out understanding that, until the Commission had started its inquiries and investigations, neither internal review nor third-party review and audit of the affected firms by tax and audit professionals gave rise to any determination that their tax treatment could potentially be subject to State aid rules").

is true, as the White Paper emphasizes, that this may create legal uncertainty that, considered in isolation, is undesirable, it also has other effects that can be desirable. Consider again *Gregory v. Helvering* and *Knetsch v. United States*. The application of the doctrines from these cases to taxpayers who had acted before they were decided – including, obviously, the litigants – created an incentive to anticipate how the government would respond to tax planning schemes that the Supreme Court found were contrary to broad legislative intent. It also avoided rewarding taxpayers who had aggressively pursued tax avoidance by identifying opportunities that had not as yet expressly been addressed by the authorities. These concerns certainly might apply to U.S. companies' negotiating advance transfer pricing agreements that reportedly did not even involve much of a pretense of genuinely applying arm's length principles (elastic though such principles are).[32]

The White Paper draws an analogy between the current state aid cases and an earlier case in which the EC invalidated a particular scheme but "did not impose a retroactive recovery because 'it can be argued' that the Commission's … previous public statements … [concerning a similar] scheme conferred a legitimate expectation" of approval.[33] It concedes, however, that "in the State Aid Cases the Commission did not issue any public statement that the tax rulings in question did *not* constitute State aid."[34] This leaves it in the awkward position of arguing that nonetheless "the principle is the same" simply because the Commission had neither previously acted in this way nor offered "hints of its new approach in previous guidance."[35]

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[32] See Kleinbard, supra.
[33] Id. at 16.
[34] Id.
[35] Id.

In support of the White Paper's argument, it surely would have been better had the EC issued earlier warnings regarding the possibility of legal challenges to advance transfer pricing rulings. This does not, however, mean either that it acted in any way in bad faith – to no evident advantage to itself or its policy aims – or that its hands should necessarily be deemed to have been tied by this omission.[36] Requiring legal authorities to pre-announce new positions that they are considering taking might not only subject them to political pressures that would complicate their doing their jobs, but would also give them an incentive to preserve their flexibility by systematically over-announcing every possible adverse policy change (from taxpayers' standpoint) that they might conceivably adopt thereafter. This would not promote legal certainty as a value.

All this being said, it is true that both the magnitude and the apparently unanticipated character of the penalties that the taxpayers in the four state aid cases may face are equitable factors that weigh in favor of a decision that the EC evidently rejected – i.e., to apply the newly announced doctrine only to post-announcement advance transfer pricing agreements. But the EC's decision not so to exercise its equitable discretion does not, in my view, amount to the sort of impropriety that would justify the White Paper's threatening statement that the Treasury will "continue[] to consider potential responses should the Commission continue its present course."[37] The United States can and should respond strategically, to the state aid cases and anything else that the EC or other EU

[36] In *Knetsch*, the IRS had actually issued at least eight favorable private letter rulings addressing the very scheme that it successfully challenged in the case. See Daniel Shaviro, *The Story of Knetsch*, in Paul Caron (ed.), TAX STORIES: AN IN-DEPTH LOOK AT TEN LEADING FEDERAL INCOME TAX CASES 327 (2003). While all tax experts are quite familiar with the point that IRS private letter rulings, as they say on their face, have no precedential value as to other taxpayers, this could reasonably have – and surely did – create subjective confidence on taxpayers' part that the schemes would not be struck down "retroactively." Indeed, the taxpayer in *Knetsch* purchased the tax shelter that was stuck down from a promoter who regularly made a point of showing his own favorable ruling to prospective customers. See *id.*
[37] White Paper at 25.

authorities might decide, pursuant to our national self-interest, and taking account both of our longstanding warm relationships with EU countries and of the fact that our interests both overlap with and diverge from theirs. This should not, however, be done in a spirit of self-righteous fulmination against steps that the EC has taken that we might well, in their shoes, have wanted to take ourselves.

V. THE STATE AID CASES AND INTERNATIONAL TAX NORMS

A final prong in the White Paper's critique of the state aid cases holds that "the Commission's actions undermine the international consensus on transfer pricing standards, call into question the ability of Member States to honor their bilateral tax treaties, and undermine the progress made under the BEPS project."[38] Although these three distinct sub-complaints are linked, I will address each separately in turn.

Effect on the "international consensus" on transfer pricing – The White Paper asserts that international consensus regarding how to make transfer pricing determinations, based on the hoary arm's length principle, is vital to "minimize the risk of double taxation and disputes between countries" regarding the allocation of multinationals' income.[39] This, however, ostensibly is undermined if "the Commission [is] now … an arbiter of when a transfer price relevant for determining taxable income in a Member State satisfies the arm's length principle."[40]

On its face, the assertion is paradoxical. Whether rightly or wrongly, the state aid cases strike down transfer pricing determinations that are found to be so unreasonable under the arm's length method that they must have reflected selective favoritism, and more particularly the aim of providing largesse. Moreover, while it is true, as the White

[38] Id. at 17.
[39] Id. at 18.
[40] Id. at 19.

Paper notes, that EC personnel often lack the close familiarity with transfer pricing practice that one would expect from national-level tax authorities,[41] the former are also well-positioned to exercise a check on any tendency of the latter to engage in what is deemed undesirable intra-EU tax competition at the expense of making good-faith efforts to apply a true arm's-length methodology.[42] To put it charitably, therefore, the White Paper is not closely grounded in a realistic assessment of the actual background to the state aid cases.

More fundamentally, however, the White Paper seems addressed to an alternative reality, far from our actual one, insofar as it lauds supposed decades of success in the transfer pricing area,[43] and treats the prevention of double taxation (as distinct from double non-taxation) as the area's properly preeminent concern.[44] Admittedly, its over-focus on double taxation, relative to double non-taxation, might come to seem more prescient if the existing regime, dysfunctional though it is, sufficiently unravels. I have heard public statements by Treasury officials, in response to comments noting the widespread consensus among experts that the arm's length standard is both intellectually

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[41] Id. at 20.

[42] The White Paper criticizes particular technical details of how the EC appears to approach transfer pricing issues, in support of the conclusion that the EC's "view of the arm's length standard depends on the relative tax rates of the countries on either side of a transaction," id. at 21, an approach that it disparages as "outcome-determinative" and "inconsistent with the logic of the arm's length principle." Id. at 22. While the arm's length standard is indeed, as the White Paper notes, "neutral as to which jurisdiction ends up with the income," id., no sophisticated review of particular transfer pricing claims or determinations could reasonably ignore the background relevance of tax rate differences that help to elucidate the relevant taxpayer incentives.

[43] More precisely, the White Paper states that the arm's length standard and associated institutions "have succeeded for decades in maintaining a consensus regarding minimizing double taxation and resolving disputes." *Id.* at 18. Even if one accepts that this is literally true, the problem is that "minimizing double taxation and resolving disputes" are not the only relevant policy aims here.

[44] As I discuss below, the White Paper elsewhere states that the Treasury "understands and shares the Commission's strong interest in preventing multinational companies from achieving double non-taxation." Id. at 24. This, however, swiftly turns into an apparent suggestion that the BEPS project has now put all such concerns to rest.

and practically flawed, to the effect that, even if that is true,[45] at least it offers a constraint on how aggressively foreign countries can seek to claim tax jurisdiction over large, and potentially overlapping, shares of the global profits of U.S. multinationals. While this is a legitimate U.S. international tax policy concern, and one that it makes sense for the Treasury to have in mind, the state aid cases involve the EC playing defense, not offense.[46] Accordingly, this is not an occasion on which the Treasury needs to imply that it is ready to go to the mattresses – a threat that it cannot needlessly invoke without undermining its credibility when there really is such a problem.

Effect on reliance on bilateral tax treaties – Next, the White Paper asserts that "the Commission's approach in the State Aid Cases raises serious concerns about the ability of EU Member States to honor their obligations under bilateral tax treaties."[47] After all, just because a given country makes a particular advance transfer pricing agreement with a particular company does not mean that the agreement will end up being respected, once the EC has had its say. The White Paper does not assert, however – perhaps because it cannot – either that the EC is recommending treaty-inconsistent transfer pricing outcomes, or that the U.S. taxpayers at issue were in a position to claim

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[45] To be clear, I have not heard Treasury officials endorse the proposition that the arm's length standard is intellectually and practically flawed, but I would presume that they hear it asserted frequently when engaged in public outreach.

[46] Moreover, despite the Treasury's seemingly exclusive devotion to the arm's length standard throughout the White Paper, under relevant U.S. tax law it is merely a tool, and not the exclusive one, for ensuring that income allocations between related parties will "clearly … reflect the income" of each party. Internal Revenue Code section 482. With respect to income from intangibles – a central issue in the four state aid cases, and one that the White Paper emphasizes in its discussion of the EC's burgeoning involvement in transfer pricing issues – the U.S. Congress thirty years ago amended this provision to establish a "commensurate with income" standard that supplements, and is intellectually distinct from, the arm's length principle as such. See section 482; Brief of Amici Curiae Anne Alstott et al in Support of Appellant in *Altera Corp. v. Commissioner*, U.S. Court of Appeals for the Ninth Circuit, Docket Nos. 16-70496 and 16-70497, July 5, 2016, at 3-4. The Treasury has expressly relied on its commensurate-with-income authority, distinctly from its reliance on the arm's length standard, when issuing transfer pricing regulations. See id. at 17-18.

[47] White Paper at 23.

treaty protection, or that the treaties, as they stand, would not be able to address any inconsistencies, such as via arbitration proceedings.

The force of the White Paper's concern about treaties is further undercut by its elsewhere acknowledging, as of course it must, that "EU State aid law may sometimes preempt conflicting Member State law, including income tax law …. [and] that Member States cannot apply their tax rules in a way that violates State aid law."[48] Thus, while the White Paper is clearly correct in discerning a possible tension between EU-level oversight and reliance on the treaties, this is simply a fact about the current international tax environment. Our bilateral tax treaties with EU countries generally pre-date, often by many decades, the rise of the EU in its current form. Yet if Europe's project of achieving greater economic integration remains operative (despite challenges, such as that from the United Kingdom's recent "Brexit" vote), or indeed even continues to advance, the mismatch between the bilateral tax treaty structure and the shift of EU legal authority to a supranational level will simply have to be accepted by American taxpayers and policymakers. On the whole, this shift may well be good for the United States on balance, despite any adverse effect on bilateral tax treaties and/or reliance on agreements with individual countries' tax authorities.[49]

Even insofar as the EU state aid cases needlessly undermine treaty reliance, U.S. readers of the White Paper should be prepared for a caustic or even sardonic response from EU and other foreign policymakers. The United States is fairly unusual in having a

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[48] Id.

[49] Although American political leaders on both sides of the aisle responded to the Brexit vote by "express[ing] respect for the decision of British voters and vow[ing] to stand with America's 'special relationship' ally Britain…. there was no hiding the concern behind the scenes" (other than from Donald Trump) that it would prove disruptive and adversely affect global U.S. policy aims. Nicole Gaouette and Stephen Collinson, *Why the U.S. is freaked out about Brexit*, CNN, June 25, 2016, available online at http://www.cnn.com/2016/06/24/politics/donald-trump-brexit-scotland-press-conference .

legal regime under which treaties are not considered more authoritative than statutes. Instead, inconsistencies between the two are resolved through a “last-in-time” rule. This means that any U.S. treaty, including our bilateral tax treaties, is instantly modified, for U.S. legal purposes, as soon as Congress passes a conflicting statute (and does not expressly subordinate the provision to contrary treaties).[50] Against this background, American tsk-tsking about the importance of honoring treaties risks being met with raised eyebrows.

Effect on post-BEPS progress – Lastly, the White Paper expresses concern that the state aid cases will undermine what has ostensibly been a great triumph in the realm of international tax policy. Specifically:

> “In light of the increase in double *non*-taxation, the international community embarked on the BEPS project to reform the existing international tax architecture. After several years of negotiation and compromise, this project achieved consensus on a broad set of measures aimed at international corporate tax avoidance. Countries and companies around the world are responding by reforming their policies and behavior. This has all been done in a spirit of mutual cooperation without seeking retroactive recoveries like those being proposed by the Commission in the State Aid Cases.”[51]

Now, however, there ostensibly is the threat that all this will fall apart, given the recriminations and retaliations that are bound to follow upon this act of unilateral and backward-looking aggression by the EC on behalf of the EU.[52]

[50] See, e.g., Julian G. Ku, *Treaties as Laws: A Defense of the Last-in-Time Rule for Treaties and Federal Statutes*, 80 Ind, L.J. 319 (2005).
[51] White Paper at 24.
[52] See id. at 24-25.

This concern is not entirely trivial. It reflects the ongoing delicacy of any effort to achieve multilateral cooperation in this area, when countries around the world so clearly differ, in many ways, with regard to their incentives and views regarding international tax policy. In part because of those difficulties, I myself am considerably less sanguine than the White Paper regarding (1) how much the BEPS process has accomplished, (2) the degree to which even such consensus as has emerged will end up being widely implemented, and (3) the extent to which double non-taxation has been prospectively eliminated.[53] Indeed, the very fact that the present dispute has emerged between EU and U.S. actors – hardly the most disparate pair of players on the global international tax scene – strikes me as more of an indicator than an aggravator of where things stand (although it is admittedly some of each). Thus, my own prudential judgment of the net harm to global cooperation that the EU state aid cases risk inflicting stands at a considerably lower level than that expressed by the White Paper.

VI. HOW BAD FOR THE UNITED STATES (AND GOOD FOR THE EUROPEAN UNION) ARE THE STATE AID CASES?

A. The Strategic Substrate

The United States and nations in the EU are close allies, and one hopes will always be so. Yet allies don't always have common interests. An example is tax competition. Quite reasonably, both Americans and Europeans would rather have

[53] I am not alone in this skepticism. See, e.g., Reuven S. Avi-Yonah and Haiyan Xu, *Evaluating BEPS*, U. of Michigan Public Law Research Paper No. 493 (2016); Itai Grinberg, *The New International Tax Diplomacy*, 104 Georgetown L. Rev. 1137 (2016). Lee Sheppard goes further, by assigning much of the blame to "American negotiators for weakening proposals or making them unnecessarily complex: 'It's as if BEPS was being killed off from the inside by letting Americans loose on it.'" The Economist, *New rules, same old paradigm*, October 10, 2015, available online at http://www.economist.com/news/business/21672207-plan-curb-multinationals-tax-avoidance-opportunity-missed-new-rules-same-old . A core complaint is that, "in opting to renovate the existing system, the OECD has stuck with its most deeply flawed pillar: the 'independent entity' principle" – i.e., transfer pricing. Id.

themselves, rather than their good friends across the Atlantic Ocean, be the ones who get the benefit of tax revenues and inbound investment that might yield positive externalities. In short, there are zero-sum elements to the relationship, even though we also both (a) positively value each other's welfare, and (b) have many positive-sum, mutually beneficial interactions.

The EU state aid cases present a classic example of interests that may be in conflict despite the underlying alliance and friendship. Thus, consider the $14.5 billion that Apple will have to pay to Ireland if the European courts uphold the EC. Suppose that it is simply a question of who – Americans or Europeans – will end up being collectively, at the margin, $14.5 billion richer. Before one gets to anything about right or wrong, it's clear that the people on each side of the Atlantic have reason to prefer that it be themselves.

This is why it could potentially be in the interest of the United States to threaten EU countries with retaliation if they continue to proceed. One possible playout would be that they back off, leaving the pot of gold (from all the current and potential cases, not just that of Apple and Ireland) in American rather than European hands. Of course, there are also other possible playouts. Suppose, for example, that, whether the Europeans back off or not, the American response triggers a mutually destructive rise in ill-will. Or suppose that American anger, and/or concern about maintaining our credibility when we issue threats, traps us into retaliating in ways that leave both sides worse-off.

The strategic judgments that both sides must make in this type of situation are delicate, and may easily miscarry. Again, the problem lies in a potentially zero-sum and competitive interaction's being embedded in a mainly amicable and cooperative substrate. This makes it important for each side to have as clear an understanding as possible of two particular things. The first is to what extent the other side is acting reasonably and in good faith (even if self-interestedly), which may affect one's own choice of strategic stance. My analysis in this article so far suggests that the EU and EC position is far more reasonable than the arguments in the White Paper suggest – although, again, this does not rebut the possibility that Americans could benefit from the Treasury's taking a hardline stance. The second, which I discuss in this section, is just how strongly (or not) the two sides' interests are actually in conflict. How much does the United States have to lose, and EU countries to gain, if the state aid cases proceed and there are more of them?

B. The U.S. Side

Fiscal stakes to the U.S. Treasury – Let us begin with an argument that is at least partly a red herring. The White Paper notes "the possibility that any repayments ordered by the Commission will be considered foreign income taxes that are creditable against U.S. taxes owed by the companies in the United States…. [Such an outcome would be] deeply troubling, as it would effectively constitute a transfer of revenue to the EU from the U.S. government and its taxpayers."[54]

To illustrate, suppose that Apple indeed ends up being compelled to pay $14.5 billion to Ireland, and that this does indeed qualify, under the foreign tax credit rules, as paying that amount in creditable taxes. (Such an outcome appears plausible, as Ireland would in effect have been compelled to replace its advance pricing agreement under the Irish income tax with a more reasonable one.) Moreover, suppose initially, for descriptive convenience (albeit, as we will see, counterfactually), that Apple could

[54] White Paper at 4.

immediately claim all of the credits, without any problems under the foreign tax credit rules. What might we then expect Apple to do?

At present, Apple reportedly has about $200 billion in unrepatriated foreign profits,[55] a situation that has been described as a "headache" for Apple CEO Tim Cook.[56] If Apple could simply claim an immediate $14.5 billion in newly minted foreign tax credits, it would immediately be able to repatriate about $41.4 billion without triggering any U.S. tax liability (net of the credits). Tim Cook's "headache" would therefore, at one stroke, have shrunk by about 20 percent.

If this happened, then, on the face of things – that is, taking the repatriation as given - $14.5 billion would have been effectively transferred from the U.S. Treasury to that of Ireland, by reason of the state aid verdict plus the U.S. tax consequences of the repatriation. Of course, that is exactly how the foreign tax credit generally works, and indeed is supposed to work if we agree that these are indeed properly creditable foreign taxes. This is one reason why I have long been a critic of the foreign tax credit, and have argued that – absent the incentive effects associated with deferral – it excessively reduces U.S. taxpayers' marginal incentive to seek to minimize their foreign tax liabilities.[57]

The fallacy here, however, lies in taking the repatriation as given. Apple presumably would not have repatriated the funds, but for the hypothesized sudden creation of foreign tax credits that made the repatriation tax-free. Moreover, while there are theoretical conditions under which deferring a taxable repatriation does not reduce its expected present value, those conditions are probably not met in a world where Apple

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[55] Renae Merle, *How U.S. companies are avoiding $695 billion in taxes*, Washington Post, March 4, 2016.
[56] Jim Higgins, *Tim Cook's $181 Billion Headache: Apple's Cash Held Overseas*, Bloomberg, July 22, 2015.
[57] See, e.g., Daniel Shaviro, FIXING U.S. INTERNATIONAL TAXATION (2014); Daniel Shaviro, *Rethinking Foreign Tax Creditability*, 63 Nat'l Tax J. 709 (2010).

may have good reason to believe that it will eventually be permitted by Congress permanently to escape some or all of the repatriation tax.

Now let us revise the above illustration to take account of the actual planning issues that the foreign tax credit claim would pose. One can only claim credits by repatriating the associated income. Here the $14.5 billion tax penalty presumably would have been computed by applying Ireland's 12.5 percent corporate tax rate to $116 billion in newly minted Irish income. Given the 35 percent U.S. corporate rate, repatriating $101.5 billion (i.e., $116 billion net of the $14.5 billion Irish tax) would leave Apple with a residual U.S. tax bill of $26.1 billion on the repatriation (i.e., $40.6 billion minus the credits). Accordingly, for the trick to work, Apple would have to gin up extra foreign tax credits somehow – a feat which it would already be doing, if this were feasible, given the size of Tim Cook's current "headache." So perhaps Apple *wouldn't* repatriate any funds, and claim any extra foreign tax credits, after all, thereby eliminating the above-described nominal cost to the U.S. Treasury, in the form of credits actually claimed.

The White Paper addresses such concerns by noting the possibility that, even absent voluntary repatriations, a scenario such as the above one would reduce net U.S. tax receipts if companies' offshore earnings were "treated as repatriated as part of possible U.S. tax reform."[58] This point is analytically correct, but judgments may vary as to how high an expected value we should actually place on it. While there has been widespread discussion of imposing a deemed repatriation in connection with shifting prospectively to a mainly territorial system, it is far from clear that any such change will take place. And even if it did, the soundest betting odds would probably favor the adoption of a very low tax rate on the deemed repatriations.

[58] White Paper at 4.

Thus, suppose again that Apple could find a way to repatriate just $41.4 billion tax-free, while somehow still getting to claim all of the newly minted credits, in the aftermath of the Ireland state aid case. If this money would otherwise have stayed abroad until the U.S. imposed, say, a 7 percent deemed repatriation tax in connection with shifting to a mainly territorial system, then Apple's U.S. tax saving by reason of the credits would end up being only about $2.9 billion, rather than $14.5 billion. Even this, however, might exceed one's probabilistic estimates regarding what is actually likely to happen.

Effect on U.S. individuals who own shares in U.S. companies – A more substantial American stake in the state aid cases might be discerned as follows. Suppose we assume that the stock in U.S. companies, such as Apple, Amazon, and Starbucks, is mainly owned by U.S. individuals – as is widely believed, under the view that there is still widespread home equity bias in capital markets, although it is surprisingly hard either to know for sure, or to demonstrate it convincingly.[59] Just for simplicity, let's take the Apple-Ireland example again and assume (inaccurately, but for expositional simplicity) 100 percent ownership of Apple by U.S. individuals.

Now what happens, when Apple hypothetically pays $14.5 billion to Ireland, is that these American shareholders, through their residual claim to Apple's net assets, are effectively $14.5 billion poorer (if all other taxes remain the same). This gets mitigated by any increase in Apple's after-tax profitability that results if it is somehow able to engineer any tax-free repatriations to the U.S., but there is still presumably a net loss.

[59] See Chris William Sanchirico, *As American as Apple, Inc.: International Tax and Ownership Neutrality*, 68 Tax L. Rev. 207 (2015).

This admittedly is not trivial. Indeed, while the real loss to Americans, with respect to the $14.5 billion, would be reduced by the fact that Apple also has foreign shareholders, there are also other EU state aid cases to think about, both current and perspective. This is the core reason why the White Paper represents a not entirely misdirected effort to advance the U.S. national interest. One readily understands why the Treasury, like Professor Chirelstein's students all those years ago, might be making so many weak arguments here. It is doing so "for a fee" – defined public-spiritedly, rather than crassly, as doing what legal advocates are supposed to do, i.e., advance their clients' interests, even if this requires making weak arguments as well as good ones, while being careful (as the White Paper indeed is) to avoid arguments that would have been downright preposterous.

Might there, however, be countervailing factors that reduce the detriment to Americans of having the EU impose tax increases on U.S. companies (with U.S. shareholders) through the state aid cases? If so, this might affect the strategic judgment that should guide how U.S. policymakers, in the White House and Congress as well as the Treasury, behave in the months to come. I believe that there are countervailing benefits, and that these should tend to reduce our concern about the cases.

Countervailing benefits? – In the world of multinationals' tax planning, domestic and foreign tax avoidance often are complements. For example, a U.S. firm derives greater benefit from profit-shifting out of the United States if it can locate the profits in a tax haven with a zero tax rate, rather than in a foreign country with a statutory tax rates that is non-trivial, albeit lower than our own. This presumably is why not just the U.S. subpart F rules, but the controlled foreign corporation (CFC) rules of numerous peer countries, commonly impose tax on foreign source income that is highly mobile and thus likely to end up in a tax haven (or actually observed in one). These rules reflect the tradeoff between the domestic benefits to minimizing foreign taxes, on the one hand, and the "tagging" concern that tax haven income has been stripped out of the domestic tax base, on the other hand.[60]

From this standpoint, the United States has something to gain from the EU state aid cases. Starting with the purely prospective side, these cases may reduce U.S. firms' ability to locate stripped U.S. profits in tax havens, in cases where the profits would most conveniently, at least as an accounting matter, pass through an EU country (such as Ireland, Luxembourg, or the Netherlands) along the way. This is why the United States, as to the long run, might welcome what the EC is doing – although there is a tradeoff here, too, given that greater ease of avoiding EU taxes would have been good for U.S. shareholders, leaving aside the issue of complementary U.S. profit-shifting.

This does not address the "retroactive" aspect, however. Even insofar as the EC's imposing penalties that relate to past behavior is not improperly *legally* retroactive – given that this is how judicial verdicts that purport to interpret existing law are meant to apply – it is *economically* retroactive, in the sense that the behavior has already occurred. Even here, however, there may be some degree of countervailing U.S. benefit. If U.S. multinationals conclude, by reason of the "retroactive" changes, that they cannot place as much trust as they had thought they could in favorable deals that they negotiate with accommodating EU Member States, this might have a feedback effect both on where they actually invest in the future, and on how they arrange their tax planning. So the United

[60] See Daniel Shaviro, *10 Observations Concerning International Tax Policy*, 151 Tax Notes 1705, 1706 (June 20, 2016)

States might, in the future, potentially gain both actual investment and reported profits, by reason of the state aid cases.

This is not to say that Americans would actually benefit on balance from the state aid cases, given the wealth effects on U.S. shareholders and the possibility of a small adverse fiscal effect by reason of the foreign tax credits. However, the prospect of realizing these benefits might affect our strategic calculations as the state aid cases move forward.

B. The EU Side

This brings us to the EU side. While it merits less attention here, since I am an American individual writing mainly to an American audience about a U.S. Treasury publication, it is worth noting that any zero-sum element to the U.S.-EU interactions has (by definition) opposite implications on the two sides of the Atlantic Ocean. Thus, it is good for EU individuals, all else equal, to have money go to their national treasuries at the expense of U.S. individuals who are shareholders of companies that are targets of the enforcement actions. On the other hand, if the EU collectively loses ground in tax competition, because U.S. and other firms become less enthusiastic about investing or locating profits in the EU, this could reduce the net gain from the up-front fiscal transfer.

The EU also faces a question of how much it benefits from restraining the ability of EU countries to offer generous tax benefits for inbound investment. Restraining intra-EU tax competition seems likely to be a good thing, considered in isolation. On the other hand, EU countries that offer generous tax breaks to foreign firms are competing not only with their EU colleagues, but also with non-EU countries that presumably lie outside the EU social welfare calculus. These judgments are independent, however, of how much umbrage the United States chooses to take with regard to the state aid cases and the imposition of “retroactive” tax penalties.

The issue of continuing strategic interactions with the United States is inevitably on the agenda (whether or not it directly affects the resolution of the state aid cases). However, since emotion as well as calculation may tend to influence strategic behavior, EU policymakers truly might benefit, not just from taking the American pulse, as to which the White Paper is certainly an indicator, but also from making the case to Americans, as convincingly and dispassionately as they can, that what they are doing in these cases is indeed reasonable. In particular, they must address American suspicions, however ill-founded, that the EU’s actions reflect any deliberate targeting of U.S. companies.[61] Where it seems that American companies are being targeted, Americans may be all too ready to infer not just fiscal opportunism, but even an underlying European resentment of the companies’ success and/or of associated American popular culture. And we are not a people who like feeling resented (although then again, who is?).

Suppose the EU is targeting U.S. companies, not because they are American, but because (a) they are non-EU and (b) as the bank robber Willie Sutton famously said with respect to banks, “that’s where the money is.” Residence of a jurisdiction generally benefit (by being collectively enriched) from taxing foreigners if the latter bear the incidence of the tax and do not sufficiently respond by exiting. This, however, is a very familiar line of behavior around the world, and moreover is not exactly alien to U.S.

[61] The White Paper expressly declines to “elaborate on the concern,” previously expressed in a letter by Secretary Lew, that the EC might be “targeting U.S. companies disproportionately.” White Paper at 5 n. 14.

policymakers.[62] A natural way to respond, especially if it is actually in our unilateral self-interest, might be by taking a closer look at profit-shifting out of the United States by foreign companies, including those from the EU.

VII. CONCLUSION

The state aid cases are a good illustration of the point that friends – such as the United States and the nations of the EU – not only may disagree, but may have genuinely adverse interests in particular respects, even if they continue, on the whole, to benefit greatly from cooperating. How they *should* resolve these disagreements, from the standpoint of maximizing their own degrees of benefit, depends on strategic calculations. How they *will* resolve them in practice may depend also on emotional factors.

The White Paper may be viewed as a step in the strategic dance. One can therefore understand its making what are, on the whole, weak arguments, with an eye to strengthening the American hand as EU policymakers decide what to do next. However, I myself am agnostic about the strategic benefit to American interests, and downright skeptical (or worse) regarding the neutral analytical merits of what the White Paper says. The fact that, in my view, the EC's actions appear to be reasonable from an EU standpoint affects my view of how aggressively the U.S. should respond, although it does not eliminate the possibility of U.S. benefit if we were to succeed in bluffing the EU into a retreat without creating too much of a residue of newly generated ill-will.

However, with regard to discerning what is actually in America's interest here, one last point is worth adding. By issuing the White Paper, the Treasury is, in effect, actively campaigning on behalf of the interests of U.S. companies. There may be good

[62] Consider, for example, the enactment of the branch profits tax (section 884), which presumably was expected to increase tax burdens on foreign companies that were likely to be predominantly owned by non-U.S. individuals, and that violated existing treaties when enacted.

reason for this. Despite the cynicism that rightly attaches to arguments along the lines of "What's good for General Motors is good for America," here there really is a link, given the possibility of wealth effects on U.S. shareholders.

It also is worth noting, however, that, despite this point, one should be leery of assuming that the companies' interests and ours as a nation are fully aligned. One point is that the companies benefit from profit-shifting out of the United States, but the country as a whole does not necessarily benefit. A second is that the companies have less reason to care than we do as a whole about the tradeoff between (a) the monetary stakes in the state aid cases, considered in isolation, and (b) the broader future of the U.S.-EU relationship. From our collective standpoint, they have every reason to over-weight (a) relative to (b).

I also believe, based on years of observation, that U.S. multinationals' influence, not just on policy outcomes but even on the broader tenor of U.S. international tax policy debate, is more likely to be too strong than too weak. The companies are important, and deserve to be heard, but their money, sophistication, and strong connections to both policymakers and academics almost guarantee that they will always be heard, and indeed quite loudly. This can be a good thing, but only if other voices and interests are sufficiently heard as well.