

Dear Secretary Lew,

The President of the European Commission, Jean-Claude Juncker, has asked me to thank you for your letter of 11<sup>th</sup> February 2016 concerning the Commission's State aid investigations into tax rulings, and to reply on his behalf.

It is important to state at the outset that the European Commission shares the United States agenda, as you set out in your letter, namely to curtail the erosion of our corporate tax bases through a reform of tax policy and behaviour. It is our common objective to close the loopholes that enable multinational groups to shift profits for tax avoidance purposes. There is no doubt that the United States plays a leading role in these efforts and the Commission appreciates very much our close cooperation both in the OECD and G-20 context. We need to work together and with other international partners to successfully promote our objectives at a global level. I can assure you of our continued commitment in this regard.

In this context of common values and objectives, we should not allow misunderstandings of our respective legal and institutional frameworks to arise. Despite the constructive engagement between ourselves and staff on these matters, your letter suggests that there is still some way to go. I am therefore taking this opportunity to clarify matters as regards the Commission's State aid enforcement actions.

It is our conviction that we must drive the reform agenda forward in our respective jurisdictions, making full use of the tools at our disposal. Therefore, the Commission is using a combination of its tools, namely legislative action and enforcement of EU State aid rules, with the aim of establishing fair tax competition within the European Union.

On the legislative front, the Commission seeks to address the root causes of tax avoidance through targeted proposals removing mismatches across the 28 national corporate taxation systems of EU countries, closing loopholes, and making corporate taxation in the EU more transparent. We have delivered a number of major initiatives over the past year aimed at making corporate taxation fairer, more efficient and more stable for all businesses - large and small - in the EU's Single Market. The most recent initiative was the Anti-Tax Avoidance Package presented on 28<sup>th</sup> January 2016, which proposes legally-binding anti avoidance measures and ambitious new transparency requirements, that will counteract some of the most prevalent forms of aggressive tax planning in the EU. This adds to the Commission's March 2015 Tax Transparency Package, as a result of which EU tax authorities will automatically exchange information on tax rulings and the June 2015 Action Plan for fair and effective taxation, as part of which we plan to re-launch the Common Consolidated Corporate Tax Base (CCCTB) in the course of 2016.

**Mr Jacob J. Lew**  
**Secretary of the Treasury**  
**Department of the Treasury**  
**Washington, D.C.**  
**United States of America**

In parallel to its legislative work, the Commission continues to enforce the rules that protect fair competition in the EU's Single Market, also when it comes to taxation. State aid rules have been in place almost since the beginning of the European Union, because they are a fundamental necessity to protect the EU's Single Market against a Member State engaging in a harmful subsidy race or using public funds to enable selected companies to unfairly outcompete their rivals. To this end, EU State aid rules catch support by the State irrespective of its form – it can for example be granted through direct pay-outs, loans, guarantees, and of course also tax advantages. The rules apply to all companies operating on the EU's Single Market, large or small, irrespective of whether they are European companies or originate from outside the EU.

On average, the Commission adopts around 500 decisions every year on State aid measures. Every case is assessed on its merits, purely from a competition law perspective and in full respect of a legal procedure which guarantees due process. If the Commission concludes that illegal and incompatible State aid has been granted to a company, it can order the Member State to recover the advantage paid out. Since 1999, the Commission has adopted around 170 decisions ordering recovery of illegal State aid from individual companies and only a handful concerned US companies.

This is the context in which the Commission's State aid investigations into tax rulings must be seen. They are part of the Commission's enforcement of fair competition within the EU's Single Market, which is the Commission's responsibility under the EU Treaties. State aid control is clearly specific to the EU and has no direct equivalent in the United States. I would, nonetheless, hope that we agree that if a national tax authority gives certain companies a more advantageous tax treatment than other undertakings in the same country, this can be extremely distortive of fair competition.

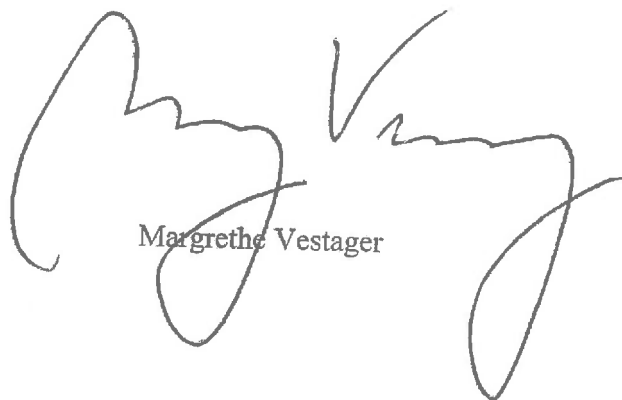
I also hope we agree that the taxation systems of EU Member States entitle them to tax the profits generated by companies operating in their territory, including US companies. The Commission has the duty to ensure that these rules are applied in a non-discriminatory manner by excluding preferential treatment in any form that constitutes incompatible State aid. This does not put into question the US taxation system or go against double taxation treaties concluded by EU Member States.

The Commission's reasoning in its investigations into tax rulings is based on firm legal ground. EU Courts have long established that under EU State aid rules Member States cannot give multinational groups a more favourable tax treatment than standalone companies. For the purpose of determining a group company's taxable profits, the price of transactions between that company and other companies of the group have to be established at market terms, in line with the so-called "arm's length principle". They cannot be based on transfer prices with no economic justification and which unduly shift profits to reduce the taxes paid by the company. This would give the multinational an unfair competitive advantage over standalone companies that are taxed on their actual profits, because they pay market prices for the goods and services they use.

Finally, if the Commission concludes that illegal State aid has been granted, ordering the recovery of such an advantage is an inherent and longstanding feature of EU State aid rules, as the figures above show. This does not penalise the company in question but simply restores equal treatment with other companies.

In conclusion, I can assure you that the EU continues to be fully committed to working with the G-20 and others to curtail base erosion and profit shifting worldwide. It is also in the common interest of the United States and of the European Union to apply these general taxation principles diligently and to ensure that taxation reflects economic reality. The State aid investigations are complementary to this initiative and aim at a proper, non-discriminative, application of tax laws in Europe.

Yours sincerely,



Margrethe Vestager

