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Google Faces a Fight in France Over Its Tax Bill

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An era of conflict between Europe and technology's superpowers. National governments and regulators are pursuing American tech firms over issues ranging from their handling of personal data to their marketplace power. The European Union on Tuesday said it would probe Amazon.com Inc.'s tax arrangements with Luxembourg, just a week after the EU attacked tax deals granted by Ireland to Apple Inc. as illegal state aid.

No tech company is more in the glare than Google. France's data-protection watchdog is leading a European fight to change Google's privacy practices. Germany leads an effort to undo a tentative EU settlement of a complaint that Google uses its search engine to favor its own businesses. The EU's top court has ordered Google to implement a "right to be forgotten" giving people a way to remove material about them from searches for their names.

The French tax dispute is one of the more fundamental conflicts because it takes aim at a structure in such widespread use. The structure channels most revenue from various European countries to a single corporate unit in a country that has favorable tax laws.

This is a crucial first step in a process that some companies take further by ultimately routing much of the income to where it faces no tax at all.

For Google to lose could have ripple effects for multinationals across Europe, potentially leading to other investigations and pressures to change structures.

"This could open the floodgates," says Edward Kleinbard, a law professor at the University of Southern California and former chief of staff for Congress's Joint Committee on Taxation. "If France falls, so do Germany and the rest."

The case hinges on what goes on at a unit called Google France. It employs more than 500 people, who Google says work as engineers or as marketers of Google services such as search ads and business software.

Under tax treaties, including one between France and Ireland, business units such as Google Ireland—the company's headquarters for Europe, the Middle East and Africa—don't have to pay income tax in a country where orders come from if they have no "permanent establishment" there.

Well-Traveled Revenue

In Google's tax structure, income from customers in European countries is reported not there but in Ireland—and then is moved further.

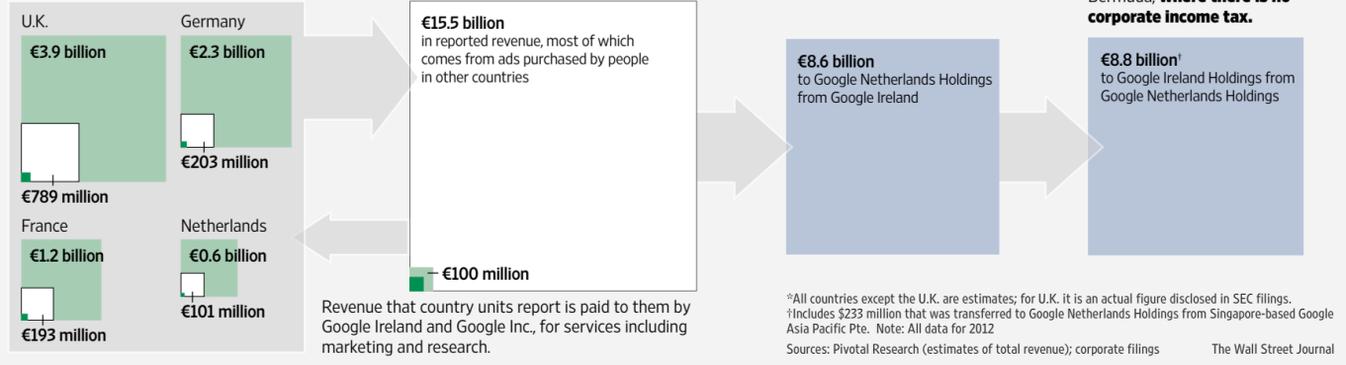
Google's estimated revenue from many European countries is much higher than the revenue its units there report, resulting in smaller tax bills.

Revenue from country*
Revenue that country unit reports
Tax the unit pays

Clients in France, Germany, the Netherlands and the U.K. actually buy their ads from **Google Ireland Ltd.**, not the country units. That boosts the revenue of Google Ireland.

Google Ireland pays royalties for intellectual property to **Google Netherlands Holdings**.

Google Netherlands Holdings then pays royalties for intellectual property to **Google Ireland Holdings**, an Irish-registered company that is controlled via Bermuda, **where there is no corporate income tax.**



A unit that just does sales preparatory work rather than close deals usually doesn't count. And Google says its French marketers indeed don't close deals such as ad sales, for two reasons: Customers in France buy their ads from Google Ireland, and in most cases they buy the ads themselves using an automated system with auction pricing.

Investigators at France's tax agency, according to people familiar with its probe of Google, argue that this structure is a facade and Google Ireland does have a permanent establishment in France to sell ads.

"We have a hard time believing that some 150 well-paid salespeople with advanced degrees employed by one particular company in France are nothing more than busboys for Ireland," a French tax official, Alexandre Gardette, said last year, without specifying which company he was talking about.

Google says that its structure reflects reality and that the Mountain View, Calif., company complies with tax laws everywhere it operates. Google says its "effective global tax rate" was about 20% in the 2014 first half. It also says it invests in local economies above and beyond its taxes.

"The reality is that most governments use tax incentives to attract foreign investment," according to a spokeswoman, and such incentives are "one of the

reasons Google located our EMEA HQ in Ireland."

The French Tax Authority also is looking at Facebook Inc., Apple, Amazon and others, according to people briefed on its investigations.

Those three companies declined to comment on that, but all have said they comply with tax laws where they operate and pay all taxes they owe. The French Tax Authority, which is often referred to "the Fisc," declined to comment.

France's position in the Google proceeding—which hasn't reached court but involves continuing administrative-level discussions between the agency and Google—runs against the view of some tax experts and of audits in other European countries, which have held that structures like Google's pass muster.

But challenges are becoming more common. A Spanish court recently ruled against Dell Inc. on a tax issue similar to the one in France. Dell is appealing.

Italian tax authorities also have an inquiry into Google, according to an official with Italy's tax police.

These challenges come at a time of broad international pressure to rein in corporate tax-reduction strategies. Last month, the Organization for Economic Cooperation and Development unleashed a volley of recommendations for doing just that. The U.K. plans legislation to make it

harder for multinationals doing business there to route their profits to tax havens. The U.S. government is attacking merger strategies that give companies tax homes in countries with corporate income-tax rates far below America's 35%.

France's corporate tax rate is nearly that high, with a headline rate of 33.3%. Most other EU countries' range between that and 20%. Ireland, to which Google directs the revenue from search ads that French marketers line up, has a 12.5% rate.

Relatively little Google profit remains in Ireland to be subject to even this 12.5% rate. The Irish subsidiary that receives revenue from European marketers turns around and pays billions of euros in royalty fees for Google's intellectual property to a Google unit in the Netherlands. That unit then pays nearly all those fees to another Irish Google unit.

This separate Google Irish unit, although registered in Ireland, is a tax resident of Bermuda. And in Bermuda, there is no corporate income tax.

In 2012, the revenue Google pulled in from customers in the U.K., Germany and France totaled more than €7 billion, or about \$9 billion, according to estimates by equity-research firm Pivotal Research. The Google units in those countries reported total revenue of just €1 billion, and just €26 million in income tax payable for the year, corporate filings show.

France's collision with Google over taxes began in late 2009. Nerves were still raw from a Google plan to scan books in French libraries, which some in France saw as theft of its cultural patrimony. Culture-related businesses started pushing for a tax on search engines. The idea of a "Google tax" took root.

"These companies are currently taxed in the headquarters country, even though they're grabbing a big part of our advertising market," then-President Nicolas Sarkozy said at the time.

His aides had doubts, however, about whether national laws could be effective against a multinational company. As the French Senate prepared hearings on such a proposal, Mr. Sarkozy planned a meeting with Google's Mr. Page to prod the company to invest in France.

"I understand what you're doing fiscally, but politically it's unacceptable," Mr. Sarkozy told Mr. Page at a May 2010 meeting on the terrace of the Élysée presidential palace, according to a person familiar with the meeting. "We have to make a deal."

Over that summer, the outlines of new Google investments in France became clear. The company would open an engineering hub in Paris and create a cultural center doing such things as working with museums to digitize col-

lections. It would give grants to universities and sponsor the local technology startup scene.

In 2011, Google bought a mansion near the Saint-Lazare train station for €113 million, increased its employee count in France by half and quadrupled its French research and development spending, to €17 million.

The plan for a Google tax foundered. Philippe Marini, a senator who supported such a tax, says Google's investments in France bought it time: "It's what I call charity business."

Not everyone was placated. France's tax agency sought warrants to search Google's Paris offices. Investigators suspected Google Ireland was using the

high hopes for a black-tie event for Paris's cultural elite celebrating an expansion of the cultural center the company had opened.

Aurélie Filippetti, France's culture minister at the time, was to give a speech. But on the morning of the event, she made a surprise disclosure to the newspaper *Le Monde*: She wouldn't attend because she didn't want to endorse the company, given ongoing disputes with it.

A more-junior minister showed up instead, telling the audience that Google wasn't France's enemy but its tax affairs were "unacceptable," said people who attended.

This spring and summer, the France-Google relationship hit a

France is taking aim at a structure that directs revenue from various European countries to just one country, where tax policy is more favorable.

French unit to "engage in commercial activity in France...without making the relevant tax declarations," a court document said.

Early on the morning of June 30, 2011, the tax cops swooped in. For nearly 24 hours, investigators backed by armed police barricaded Google office entrances and carted away hard drives full of digital files.

Google argued in court that the raid violated French procedure by accessing documents stored on servers outside France. The court disagreed.

The 2012 French presidential campaign thrust Google's tax affairs back into the political arena.

François Hollande, as a Socialist candidate, promised to try to tax Internet companies to help fund France's system of cultural subsidies for everything from movies to newspapers.

Elected president, Mr. Hollande met in October 2012 with Google's executive chairman Eric Schmidt at the Élysée and said he wanted the company to settle a spat with French newspapers, which were pushing for a law that would force Google to pay them for each story it linked to.

By February 2013, Google had sealed a compromise: It pledged €60 million over three years to fund newspaper modernization projects. Mr. Hollande said French pressure helped produce the outcome.

Despite the accord, relations deteriorated. French telecom companies jostled with Google over the volume of data sent by Google services such as YouTube. French government officials began angling for more EU regulation of big Internet platforms, envisaging measures ranging from new taxes to an obligation to make personal data portable.

In December 2013, Google had

low ebb. Politicians continued to criticize the company, Economy Minister Arnaud Montebourg describing it as a colonialist. People close to Google said the company might end up slowing its investments in France, where its R&D spending hit nearly €35 million last year.

A French government shuffle in August, however, has sparked hopes of a warming for some at Google and in the government. Mr. Montebourg, a Socialist firebrand, was ousted as economy minister and succeeded by a former investment banker, Emmanuel Macron.

Google's chief legal officer, David Drummond, met with Mr. Macron the same day late last month that Mr. Page met with France's prime minister. "France has tremendous technical and creative talent," Mr. Drummond says. "It's why we've already invested significant amounts here and are looking closely at what's next."

The disagreements continue. French officials are pushing for greater European regulation of Web giants. The government has backed a more aggressive anti-trust stance against Google taken by the EU.

And Google is still fighting within the Fisc to revise the tax assessment levied on it in March. The company is confident of its position that the bill is unjustified, but persuading French tax authorities to lower it could be difficult to pull off, a person close to Google said.

A worry, the person added, is that "there's no solution a la française. If France walks away with a huge chunk of cash, other countries will want their piece, too."

—Alistair Barr and Eric Sylvers contributed to this article.



Inside Google's Paris offices, housed in a mansion bought as the firm raised its French investment in 2011.

Drone Fans Nix Military Moniker, Search for Alternatives

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merical drones.

The Federal Aviation Administration is still working out rules for the commercial use of drones—which U.S. farmers, filmmakers and others have been flying in growing numbers, even without permission. But both the agency and Congress have settled on a name: they use UAS in legislation and official documents.

"If the FAA calls these things bullfrogs, then I'll call them bullfrogs," said Michael Toscano, chief executive for the Association for Unmanned Vehicle Systems International, the trade group that urged reporters not to say "drones" last year.

Mr. Toscano said the term drone makes most people think "weaponized, hostile, large and autonomous." He prefers UAS because it encompasses the entire system, including "the technology on the ground with the human at the controls," he told

Congress last year. "As I like to say, there's nothing unmanned about unmanned systems."

Sen. Patrick Leahy (D., Vt.) responded at that hearing: "I appreciate you telling us what we should call them, but...why don't you leave that decision to us? We'll decide what we'll call them. You call them whatever you'd like to call them."

But it isn't hard to find advocates who drone on about why they don't like the term UAS and its "unmanned" cousins. "I hate the word unmanned," said Don Wirthlin, a drone-pilot instructor in Douglas, Ariz. "Last time I checked, I was a human flying a UAV."

Ben Gielow, the former general counsel of the unmanned-aircraft trade group, said that "unmanned" isn't ideal. "We have to stop defining the technology by what it's not," he said. "They used to call the car a horseless carriage."

Some of the aerospace companies that shy away from using "drone" assign their devices intimidating-sounding names such as the Wasp, TigerShark, Predator and Reaper.

Other technical names for the devices touch on the number of propellers they have, such as a quadcopter or an octocopter. And then there's Deutsche Post DHL's delivery drone, which the company calls the Paketkopter.

The name confusion is a headache for some. "You try to explain what you do to your families on Thanksgiving...and no one knows what the hell a UAV is," said Zach Rosenberg, a freelance journalist who covers drones.

Even the military can't seem to agree on a name. For example, on their websites, the Army has used drone, the Navy has used UAV and the Coast Guard has used UAS. The Air Force's preferred term, RPA, recently received endorsement from top brass.

"You will never hear me use the word 'drone,' and you'll never hear me use the term 'unmanned aerial systems,'" Gen. Martin Dempsey, chairman of the Joint Chiefs of Staff, told reporters in May. "Because they are not. They are remotely piloted aircraft."

However, it was the military that originally nicknamed the devices "drones," said Ben Zimmer, a lexicographer who has researched the history of the term. In 1935, the U.S. Navy began using unmanned aircraft as aerial targets for shooting practice. The British Royal Navy had named its unmanned target aircraft the Queen Bee, Mr. Zimmer said, so in homage, the Navy called its targets "drones," which means male bee.

Many unmanned-aircraft enthusiasts say that is why the term drone is inaccurate—because it should refer only to aircraft used for target practice.

But Mr. Zimmer disagrees, saying the military began arming unmanned aircraft and calling them "assault drones" in World War II.

As early as 1946, the media had picked up the term. "Drones, as the radio-controlled aircraft are called, have many potentialities, civilian and military," the magazine *Popular Science* wrote that year.

During a question-and-answer session with U.S. Rep. Frank LoBiondo (R., N.J.) at a drone conference this year, Dick Rumpf, head of a consulting firm, took the congressman to task for using the term drone. "If you guys stop using the word drone...the press won't poison the minds of John Q. Public with thinking we're going to be hitting them with weapons," he said to applause.

"I totally agree with you," Rep. LoBiondo replied. "I will try to sensitize my colleagues."

Not everyone in the industry dislikes the word. Andrew Petersen, a drone videographer, named his Los Angeles company Drone Dudes. Sven Juerss, CEO of German drone maker Microdrones GmbH, said having the word in a company name helps customers find a firm. "Everyone types drones into Google, not UAV," he said.

U.S. residents generally searched more for the term UAV than drone from 2004 through 2009, according to data from Google Trends, which tracks search-term volume. But in 2010, Google searches for "drone" soared past the alternatives and the term remains by far the top choice today, the data show.

Popular Science writer Kelsey Atherton, who writes weekly roundups of unmanned-aircraft news called "Keeping up with the drones," said opponents of the term should give up. "The battle is over and drone won," he said.