Kering's Tax Probe Seen as Benchmark

Legal, fiscal and industry observers take a closer look at Kering's decision to settle with the Italian Revenue Agency.

By Luisa Zargani on May 16, 2019

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MILAN — Kering's decision to settle with the Italian Revenue Agency through the payment of 1.25 billion euros — one of the biggest ever with the Italian authorities — could become a cornerstone decision and have a major effect on similar scenarios, triggering questions about international taxation.

The case confirms "the obsolescence of the traditional criteria of international taxation that are based on transfer pricing theories and the 'permanent establishment' concept, as they continue to fuel uncertainties and litigation between companies and the financial administrations in various countries," said Luigi Perin, CPA, partner at Funaro & Co. P.C.

The investigations of the Italian tax authorities, which focused on Kering's tax payments related to the sales in Italy of Gucci products between 2011 and 2017, identified a tax evasion of 1.4 billion euros. According to the Italian tax authorities, in distributing Gucci products in Italy through a directly operated Switzerland-based company named Luxury Goods International, Kering had intentionally avoided the payment of taxes in Italy.

This is only the latest in a string of similar cases, ranging from Prada Holding BV's alleged subsidiaries in the Netherlands and Luxembourg for a more favorable tax rate to Dolce & Gabbana's Luxembourg-based holding company, Gado Srl, which the Italian tax police reportedly considered essentially a legal entity used to avoid higher corporate taxes in Italy, or Luxottica's tax audit concerning the year 2007 over alleged irregularities in the use of transfer pricing.

Riccardo Molesti, fiscal consultant and tax adviser, said Kering's settlement brought up once again the "usual debate" between the concept of legal headquarters in a country different from Italy and the stable organization — offices, plants, warehouse, commercial network — in Italy. According to the Italian law, "stable organization is sufficient" to be considered an Italian fiscal subject. But the definition of these criteria is not always clear, Molesti contended. "What I believe is lacking is a coordinated European fiscal legislation. Sure, Switzerland is not part of the European Union, but the world is now so globalized, with so many possibilities to be in contact and start activities that I believe harmonizing European fiscal laws can no longer be delayed — at least at the level of member States," argued Molesti. "It's useless to speak of Europe when every country, in a fiscal matter but not only, can establish its own rules with enormous differences of treatment between one country and the other. If [Kering] reached an agreement and accepted to pay such a relevant amount clearly they assumed that a legal litigation would be way too risky," and could even lead to a heftier financial expense.

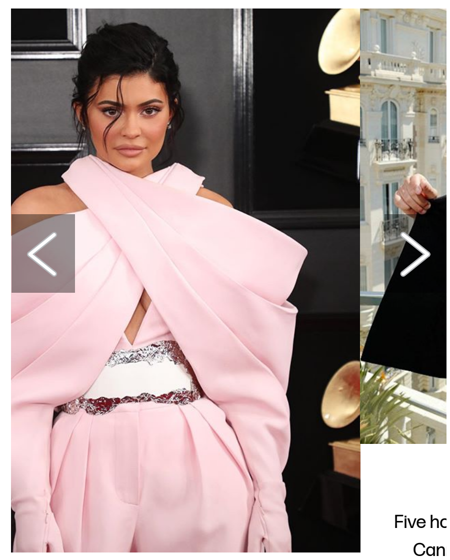
Perin explained that, in the U.S., "formulary apportionment" is employed to avoid both double taxation and tax avoidance by companies that operate in more than one State. This is a method of apportioning profits earned by a corporation or a corporate group to a particular state tax jurisdiction, in which the corporation or group has a taxable presence. The formula is generally based on the ratio of income derived from the sale of goods and services to residents of that state and income derived from the sale of goods and services worldwide.

"The advantage of formulary apportionment is that it does not rely on hypothetical arm's length negotiations of economic conditions to the transfer goods and services between legal entities or branches" that are part of the same multinational group, "with all the uncertainties and distortions that can ensue. The starting point of the system adopted by the majority of American States is in fact more objective: the consolidated taxable income of the entire corporate group."

According to Perin, the unitary tax system of multinational groups could "represent a valid alternative to the current system of taxing multinationals currently in existence in the Organization for Economic Co-operation and Development [or OECD] countries, based on the rules of transfer pricing…despite the evident limitations that require constant and complex legislative interventions to contrast the multinationals' elusive behavior, such as base erosion and profit shifting [or BEPS], which refers to tax avoidance strategies that exploit gaps and mismatches in tax rules to artificially shift profits to low or no-tax jurisdictions."

"The unitary taxation system adopted at the State level in the U.S. would cut tax avoidance techniques at their root, as they depress the tax revenues of OECD countries, effectively neutralizing intercompany transactions that could otherwise erode the taxable base by rerouting profits to low-taxed countries," concluded Perin.

One highly placed legal source said that, following Kering's decision to pay, prosecutors are "securing" the amount, and doubted a trial would follow. A criminal investigation in Italy takes place separately and independently even if a company has agreed to settle. As reported, Domenico Dolce and Stefano



Gabbana were cleared first at the penal level in 2014 and, last year, at the fiscal level, with the judges of Italy's highest court, the Cassazione, believing Gado was actually an active company in Luxembourg and that it had its own organization, although the decisions were made at the group's headquarters in Milan.

In 2016, Milan prosecutor Gaetano Ruta asked a judge here to dismiss an investigation targeting Miuccia Prada and Patrizio Bertelli for alleged tax evasion. A legal source at the time said Ruta believed the couple "are objectively not to be punished" because they have paid back their fiscal debt, following a "voluntary disclosure" the couple made to tax authorities in December 2013 that resulted in an agreement with Italian tax officials.

It is understood that Bertelli and Prada in 2013 paid 400 million euros to the tax office. Legal sources at the time emphasized that the designer and Bertelli had advised on the existing tax anomalies, brought back the legal headquarters of the company to Italy and paid the back taxes.

The designer and Bertelli "spontaneously decided to move all the foreign holding companies to Italy, submitting to the Italian tax authorities a complete analysis of the foreign structures they owned and determining the tax burden under Italian tax law pertaining to the preceding decade," noted the company on Wednesday. "This voluntary procedure in no way concerned the Prada Group. On the contrary, in 2017, the Italian Tax Authority admitted Prada SpA, along with a few other Italian companies, to a program of Cooperative Compliance [under Legislative Decree 128/2015], consisting of a new form of transparent dialogue with the tax authorities."

In addition, Prada SpA was "selected to participate in a similar international compliance and assurance program, launched and coordinated at the OECD level, to which only one other Italian group and very few foreign groups have been admitted so far. Participation in these cooperation programs is the result of positive long-term interaction with the tax authorities in the countries where the Group operates, based on full legal compliance. Prada SpA also signed the first Advanced Price Agreement with the Italian tax authorities in 2008, in full compliance with the group's tax strategy, based on transparency and cooperation. The Prada Group feels that compliance with tax legislation is not just a legal obligation but also an ethical principle and social duty."

To be sure, Giovanna Brambilla, partner at Milan-based executive search firm Value Search, had another take on Kering's agreement to regularize its fiscal position. "I want to think and hope that the sustainability theme is not only a concept regarding the environment, but also one of transparency and ethic," Brambilla said. "Consumers and companies are increasingly more attentive to sustainability and this could also mean a simpler reading of financial operations." Companies today are increasingly judged not only on whether they pollute less, save energy and earn top certifications, but also on moral grounds, noted Brambilla.

In January, Kering ranked as the second most sustainable company in the world across all industries in Corporate Knights Global 100 Index unveiled at the World Economic Forum in Davos rocketing up from 47th place just a year ago. The luxury goods firm, owner of brands including Gucci, Alexander McQueen and Balenciaga, was the leader in the ranking in the luxury, apparel and accessories category for the second year in a row. Kering has made corporate social responsibility a pillar of its strategy in recent years, and is notably aiming to reduce its environmental footprint by 40 percent between 2017 and 2025, as reported. This week, the company is releasing detailed guidelines on animal welfare — a several-hundred page document outlining standards for cattle, calves, goats, sheep, ostriches, crocodiles and alligators, pythons, farmed fur and abattoirs — open-sourced, in keeping with other company efforts related to sustainability.

In any case, one source admitted that such high fines have triggered a rethinking for many brands as the government installed last year and the Italian Revenue Agency have become increasingly more aggressive toward fiscal elusion.

Armando Branchini, deputy chairman of Milan-based consultancy InterCorporate, said that, "absolutely," companies have become much more attentive to tax regularity. "Companies posting medium- and large-sized revenues that are considered 'big contributors' are monitored annually and verified every three or four years — five at the most. Verifications are made within the company by agents of the Italian tax police and officials of the Internal Revenue Agency and can last months, even more than one year," said Branchini, noting that companies with "famous brands" that have over the past few years registered sales and profit growths "above average," are "privileged targets. Surely others will be induced to think that not even these big and famous companies succeed in saving on tax money."

Gucci Kering Prada

Kristin • 3 hours ago

I usually raking in roughly $9517 /on monthly basis from the internet . It is wonderful source of income to change my previous life sucking cubical work , Along with neatest thing related to it is actually that I now complete all my business only a couple of hr day by day which simply leaves me a great deal more of free moments than I had before with my kids. Here's