



JAVA SIREN: Starbucks is a major presence in European countries such as France, Germany and the UK.

REUTERS/LUKE MACGREGOR

Like its UK operation, Starbucks's units in France and Germany use transfer pricing to keep taxes low

Starbucks's continental de-tax cafe culture

BY TOM BERGIN

LONDON, NOVEMBER 1, 2012

Starbucks told investors its European businesses made a \$40 million profit in 2011, but accounts filed for its UK, German, and French units, which make up 90 percent of European revenues, showed a loss of \$60 million.

Did the coffee giant lose \$100 million in the year between advising investors and filing its returns to European tax men?

Far from it. An examination of Starbucks's compa-

ny accounts in Germany and France shows the firm employed the same tactics there that Reuters recently showed it has used in the UK: reporting losses to the taxman while boasting healthy cashflows to investors.

Starbucks Chief Financial Officer Troy Alstead said the company simply used a different measure of profit when reporting its performance to investors and when filing its tax returns.

If the chain had reported its Europe, Middle East

TAXES STARBUCKS IN FRANCE AND GERMANY

and Africa (EMEA) region profit of \$40 million in the UK, France, Germany or the Netherlands, where its EMEA headquarters is based, it would have faced a tax liability of around \$11 million, according to Reuters calculations.

Instead, accounts for its European units show it paid around \$1.2 million in Dutch taxes and racked up millions of dollars worth of accounting losses it can use to reduce future German, French or British tax bills.

There is no evidence the firm has broken tax rules in any of the countries where it operates, and investors naturally expect companies to manage their tax bills.

“If you’re not finding ways to mitigate your tax responsibilities to the best of your ability, that’s something that will impact shareholders,” said RJ Hottovy, an analyst who covers Starbucks for Morningstar.

Alstead said that while Starbucks tried to optimise its tax bill, the company followed the rules and was not an aggressive tax avoider.

“Our intent is to be absolutely fair taxpayers everywhere,” he said.

But muscular tax planning also brings risks. A YouGov survey conducted days after Reuters reported earlier this month that Starbucks had paid just 8.6 million pounds (\$13.9 million) in British corporation tax on 3.1 billion pounds of sales over the past 13 years, showed that Britons now take a much more negative view of the firm.

The story prompted a wave of media criticism and British members of parliament called for an inquiry by the tax department. Prime Minister David Cameron, asked in parliament about the tax paid by Starbucks and other companies, said: “I am not happy with the current situation. I think the HMRC (UK tax authority) needs to look at it very carefully. We do need to make sure we are encouraging these businesses to invest in our country, as they are, but they should be paying fair taxes as well.”

In France and Germany, where Starbucks has not paid income tax in a decade



COFFEE MAN: Howard Schultz, president of Starbucks Coffee Company, opens the chain’s first outlet in France in 2004.

REUTERS/CHARLES PLATIAU

of operations, some politicians now say their tax men should also investigate the coffee chain’s affairs. Tax structures that allow corporations to shift money around to minimise taxes “is a form of corporate welfare”, said Sven Giegold, Member of the European Parliament for the German Green Party. He said he would raise the issue of Starbucks tax record with tax authorities in Bavaria, where Starbucks’s German unit is based.

A spokesman for Germany’s left-of-centre Die Linke party said it would ask the finance ministry to investigate whether Starbucks had complied with German tax rules.

The finance ministry said it did not comment on individual taxpayers. French and German tax authorities also declined to comment, citing taxpayer confidentiality.

Starbucks said in a statement it was “totally committed” to the UK, France and Germany. The company said that though it paid no corporation tax in what it called “three

of our largest and most important markets” in 2011, it had paid value added taxes, social security costs and business rates.

Alstead said the primary reason the French and German units didn’t pay corporation tax was because high rental rates and labour costs made it hard to turn a profit. The CFO said German tax authorities had expressed concern about the large accumulated tax losses Starbucks Coffee Deutschland had built up and was pressing the firm to agree not to use them to offset any future taxable income.

Starbucks said its overall tax rate, which includes deferred taxes that may or may not be payable in the future, was 31 percent in 2011. This compares with an average U.S. corporate income tax rate of 26 percent from 1987 to 2008, according to the Congressional Budget Office.

CAFE SOCIETY

Starbucks’s Europe, Middle East and Africa division has boasted sales of \$1 billion in each of the past three years. The UK contributed most of that – in 2011, for instance, its turnover was \$636 million.

The company operates in the UK, France and Germany via wholly owned subsidiaries that manage coffee stores and license the brand to other retailers. It also has smaller, wholly owned subsidiaries in Switzerland, Austria and the Netherlands.

Most of the rest of the income generated by the firm’s EMEA division comes from licensing fees paid by partners operating under the Starbucks brand in countries such as Spain, Greece and Russia.

Starbucks entered Germany with a cafe near Berlin’s Brandenburg Gate in 2002 and now operates 150 stores in the country. It opened its first French store, near Paris’s Opera House, in 2004 and now has over 60 branches in France.

Starbucks executives like to recall how critics predicted their failure in France and Germany, which had long-established café cultures that shared little with Starbucks’s

TAXES STARBUCKS IN FRANCE AND GERMANY

uniform interiors, paper cups and whipped-cream-topped concoctions such as Cinnamon Dolce Lattes and Mocha Frappuccinos.

“A lot of people asked if Starbucks would have any relevance in Germany,” Chief Executive Howard Schultz told Germany’s *Frankfurter Allgemeine Zeitung* in 2008. “I think we’ve proven that we’ve been accepted in Germany.”

In December 2010, John Culver, president of Starbucks’s international division, told an investor conference that the German unit “showed a profit on the bottom line” in the year to October. He also said France had turned “cash flow positive”.

Yet the accounts Starbucks Coffee Deutschland GmbH and Starbucks Coffee France SAS filed to local company registers showed losses in 2010 and 2011, as in every previous year.

Starbucks had sales of 117 million euros in Germany last year, accounts for the local unit show. It reported a loss of 5.3 million euros and paid no income tax.

The group had sales of 73 million euros in France, but reported a loss of 2.5 million euros and paid no income tax.

By contrast, the German unit of Mc-

“A lot of people asked if Starbucks would have any relevance in Germany. I think we’ve proven that we’ve been accepted in Germany.”

Howard Schultz
Chief Executive

Donald’s had turnover of 196 million euros in 2010, the most recent year for which accounts are available, and paid tax of 12.6 million euros. McDonald’s France paid tax of 49 million euros last year on 812 million of revenue.

A ROYAL LOSER

Alstead said the accounts its French and German units file could vary from the picture given to investors because of inter-company payments that can be deducted when calculating the units’ taxable income.

Like the UK division, the French and German units use inter-company transfers to shift profit.

In France and Germany, the main deduction is a royalty the two units pay to their immediate parent, Netherlands-based Starbucks Coffee EMEA BV, for “use of the trademark and Starbucks business processes”, according to a spokeswoman.

The fees are equivalent to 6 percent of turnover, and additional charges of \$25,000 are also due when the local units open a new store, accounts for the units show.

Royalty payments helped Starbucks achieve an average tax rate of 13 percent on overseas income in 2011, lower than consumer companies such as Nike, Wal-Mart, Gap, Burger King, Yum Brands and Tiffany.

Other U.S. companies also charge their European units fees to use trademarks or business processes, though not as much as that charged by Starbucks.

McDonald’s and Burger King charge their European units a fee of 4-5 percent of turnover. Supermarket chain Wal-Mart charges its UK subsidiary Asda 0.6 percent

for various services including royalties. A spokesman for Kentucky Fried Chicken, owned by Yum Brands, said it did not charge associated companies money to rent the KFC brand.

Starbucks is unusual among these chains in that the royalty fee it charges European units has consistently eaten up most or all of the profits they would otherwise have earned. Other retailers would not comment on why they don’t charge higher fees.

International tax rules allow companies to deduct royalty payments to associated entities, provided they are at “arms length”. In other words, a Starbucks unit has to establish it would have agreed to pay an unrelated company 6 percent of turnover to rent a comparable brand and business processes.

Starbucks said it followed industry practice and that it abides by the “arms length” rule at all times.

In 2009, though, after a decade of losses, the British taxman challenged Starbucks’s deduction of a 6 percent royalty and told the company it could deduct just 4.7 percent from taxable income in future, Alstead said. HMRC would not say what prompted the examination.

DUTCH WINNER

Though the Starbucks brand was developed in the United States, the brand fees the French and German units pay do not go back there, where they might face tax at 35-39 percent, but to the Netherlands.

Dutch corporation tax is 25 percent, but tax experts say few of the many multinationals that transfer royalties from European units to a related company in the Netherlands pay tax there at that rate.

Dutch tax officials declined to comment on Starbucks, citing taxpayer confidentiality.

European Union rules allow the transfer of such fees within the bloc without tax deductions, but require withholding taxes to be levied when the fees are moved outside the bloc. But Dutch tax law allows companies to send royalty fees earned in other countries



HOT BREW: A customer in the chain’s Mayfair Vigo branch in central London.

REUTERS/ANDREW WINNING

TAXES STARBUCKS IN FRANCE AND GERMANY

on to tax havens without incurring taxes.

In September, the European Parliament voted to close this loophole. But its views on tax matters are only advisory, and rule changes require unanimity among member states.

Despite the royalties it receives, Starbucks Coffee EMEA doesn't make much profit either. On revenues of 73 million euros in 2011 it managed a profit of just 507,000 euros.

When asked how the unit burnt up its revenue, Alstead cited staff costs – the HQ has 97 employees – and rent. Average gross earnings are 44,800 euros per head in the Netherlands, according to Eurostat, while rent on an Amsterdam office to house 100 employees would typically cost about 300,000 euros a year, said Michael Hesp of real estate firm Jones Lang LaSalle Netherlands.

Even if Starbucks Coffee EMEA BV paid twice those average wages and rents, that would account for only 13 percent

of revenues.

Alstead said the unit also paid other group companies for unspecified services, including a Swiss-based associate he declined to identify.

The French and German units also run up big losses thanks to their large debts.

Rather than investing cash in these units, Starbucks Coffee EMEA lends them money to fund growth. The interest on those loans – charged at a higher rate than the group pays to borrow – reduces the taxable income of the national units, according to tax rules in both jurisdictions.

Starbucks itself has a conservative debt-to-equity ratio of 12.5 percent, meaning its business is mostly financed by shareholders' capital and retained profits. Its French and German units, however, are overwhelmingly financed by debt, with ratios of 156 percent and 764 percent, respectively.

Alstead said the high debt levels were a

function of the French and German units' weak profitability, which required the parent to extend loans to help them cover their bills.

The Dutch unit has also taken on loans, but the company declined to identify the lender.

Without royalty fees and interest payments, Starbucks's French and German units would have generated a profit of over 10 million euros in the past two years and faced a tax liability of 3.4 million euros, the units' accounts show.

Instead, Starbucks Coffee EMEA BV and the group's Amsterdam-based roasting unit, Starbucks Manufacturing EMEA, declared profits of 2 million euros in 2011 and paid taxes of 870,000 euros.

Starbucks declined to say where the rest of its 2011 EMEA profit ended up or how much tax was paid on it.

Edited by Editing by Will Waterman and Simon Robinson



FOR MORE INFORMATION

Tom Bergin, European Corporate Strategy Correspondent

tom.bergin@thomsonreuters.com

Simon Robinson, Enterprise Editor, Europe, Middle East and Africa

simon.robinson@thomsonreuters.com

Will Waterman, Top News

William.waterman@thomsonreuters.com

Michael Williams, Global Enterprise Editor

michael.j.williams@thomsonreuters.com

GERMAN APPEAL:

A branch in Germany's financial centre

Frankfurt. **REUTERS/**

RALPH ORLOWSKI