THE FIRST EU GENERAL COURT JUDGMENT ON STATE AID THROUGH TAX RULINGS – ARE THERE WIDER IMPLICATIONS?

On 14 February 2019, the EU General Court annulled the European Commission's State aid decision relating to the Belgian excess profit ruling system. The General Court found that the European Commission was wrong to consider that aid was granted by means of a general "scheme," with all individual tax rulings being merely a technical application of that scheme. The Court held that the European Commission should rather have assessed separately whether each of the individual rulings gave rise to State aid. The judgment is the first relating to the European Commission's enforcement of State aid rules in the area of transfer pricing tax rulings.

Key issues

- The General Court's annulment of the EC's decision on the Belgian excess profit scheme is based on the finding that the relevant measures did not qualify as a collective aid "scheme."
- Next steps available to the EC include appealing the General Court's judgment or re-issuing similar decisions for each individual tax ruling concerned.
- The impact on other State aid cases relating to tax rulings is likely limited.

Context: EC's State aid investigations into tax rulings

Since 2013, the European Commission (EC) has launched a number of investigations surrounding tax ruling practices across various EU Member States. The EC's investigations have mostly focused on individual tax rulings granted to multinationals (Apple in Ireland; Fiat, Amazon, Engie, McDonald's, and Huhtamäki in Luxembourg; and Starbucks, Ikea, and Nike in the Netherlands). The EC's recent decision on the Belgian excess profit ruling (EPR) system, however, concerned what the EC considered to be a general tax exemption scheme that was merely implemented through individual tax rulings. The EC found that a taxpayer fulfilling the conditions set under the scheme would be granted a tax ruling automatically upon request, with the Belgian tax authorities enjoying only a limited margin of discretion in relation to the application of the scheme to that taxpayer's situation. The scheme significantly reduced the corporate tax base of the companies in question to discount for "excess profits" given that the taxpayer was part of a multinational group.

The Belgian EPR system

In 2005, Belgium implemented a tax regime that excluded certain "excess" profits of taxpayers from the taxable base. The regime deemed that certain profits resulting from the taxpayer being part of a multinational group should not be included in an entity's taxable base. This "excess" profit corresponded to the difference between the actual recorded profit of a Belgian entity

belonging to a multinational group and the hypothetical average profit that a standalone company, in a comparable situation, would have made.

To benefit from the EPR regime, the taxpayer had to obtain a tax ruling from the Belgian tax authorities. The filing determined whether the taxpayer fulfilled the conditions required to benefit from the regime, and confirmed the amount of the "excess" profit and the corresponding reduction of the taxable base.

The EC's 2016 decision finding illegal State aid

EU law prohibits Member States from granting subsidies to companies, including through selective tax breaks, unless authorised. This prohibition covers both grants of aid in individual cases, as well as so-called "aid schemes" (*i.e.*, the establishment of general regimes on the basis of which aid may be granted in individual cases without the need for further implementing measures).

To show that a measure constitutes illegal State aid, the EC must demonstrate that the State grants a selective advantage to one or more beneficiaries. The assessment of the criteria for selectivity and advantage depends on whether the measure is a scheme or an individual measure that only applies to a specific beneficiary. Because the legal criteria differ, the assessment of an alleged State aid measure requires the EC to qualify it either as a scheme or as an individual measure.

Although the taxpayer had to obtain a tax ruling to benefit from the exclusion of the "excess" profit from the taxable base, the EC did not consider the individual rulings to be the aid measures - unlike, *e.g.*, the rulings at issue in the EC's *Fiat*, *Starbucks*, *Apple*, *Amazon*, and *Engie* decisions, which the EC held to be individual measures (all of these decisions are currently under appeal). Instead, the EC held that the aid measure was the general scheme allowing the taxpayers in question to have their taxable base reduced. While the EC acknowledged that the rulings granted under the EPR system each concerned different facts, it considered that these rulings were merely the instrument through which the scheme was applied because the general circumstances under which the rulings were granted were the same (*e.g.*, they involved big multinationals, the request for a ruling was justified by an increase of activities in Belgium). The EC further considered that the margin of discretion enjoyed by the Belgian tax authorities was restricted to what was necessary to ensure a consistent application of the "excess" profit exemption, so that the authorities' rulings were merely the technical application of an aid scheme to an individual situation.

In its decision, the EC examined whether the deduction of the excessive profit under the EPR system had resulted in a departure from the "arm's length" principle. The EC found that multinationals, domestic groups and standalone companies are all in a similar legal and factual situation from the perspective of corporate income taxation. According to the EC, the EPR system enabled taxpayers that were part of multinationals to be taxed based on a reduced taxable base that did not represent an arm's length profit. The EC concluded that the excess profit exemption derogated from normal practice under Belgian company tax rules and the arm's length principle. Therefore, the excess profit exemption unlawfully differentiated between entities that were part of a multinational group for which an exemption was available, and standalone entities for which no exemption was available.

The EC identified 35 beneficiaries under the EPR scheme. It estimated the total amount to be recovered to be around EUR 700 million.

The General Court's annulment of the EC's decision

Belgium and 28 alleged beneficiaries appealed the EC's decision before the General Court (the lower tier court of the EU). On 14 February 2019, the General Court handed down its judgment in the appeals lodged by Belgium and Magnetrol International (Joined Cases T-131/16 and T-263/16), annulling the EC's decision.

Both Belgium and Magnetrol raised a number of pleas in their appeal, but the General Court only examined two of them.

First, the General Court dismissed Belgium's arguments alleging that the EC encroached upon Belgium's exclusive powers in the area of direct taxation. The General Court recognised that direct taxation falls within the competences of the Member States, but held that the exercise of such competence must be consistent with EU law. According to the General Court, any measures imposed by public authorities which grant certain undertakings advantageous tax treatment and place the beneficiaries in a more favourable position than other taxpayers, can constitute unlawful State aid. As the EC is competent to oversee and ensure compliance with State aid rules, it cannot be accused of exceeding its powers merely because the alleged aid measure relates to direct taxation.

Second, the General Court assessed whether the EC correctly qualified the alleged aid measure as a scheme. It found that the EC erred in characterising the measure as a scheme for three main reasons. First, the relevant Belgian legal acts did not define all essential elements of the EPR system, so aid could not be granted on the basis of these legal acts. Second, the Belgian tax authorities had a margin of discretion allowing them to influence the amount and the characteristics of the exemption and the conditions under which it was granted. Thus, the authorities did not merely carry out a technical application of the applicable regulatory framework, but, rather, took implementing measures which required a qualitative and quantitative assessment of each individual case. Third, the beneficiaries of the EPR system were not defined in a general and abstract manner by the acts on which the EPR system was based. Each of these reasons precluded the qualification of the aid measure as an aid scheme, given that a scheme presupposes that aid may be granted in individual cases without the need for further implementing measures. As a result of this error in the EC's assessment, the General Court annulled the EC's decision.

Significance

The General Court's annulment of the EC's decision is based on a technical point. The General Court did not exclude that individual tax rulings granted under the EPR system might constitute illegal State aid. It merely criticised the EC for wrongly qualifying the relevant measure as a scheme. The EC can, in principle, still adopt new decisions relating to each individual tax ruling granting the excess profit exemption. The General Court's judgment is also open to challenge before the Court of Justice.

The General Court's judgment is the first judgment arising out of the EC's tax ruling decisions. Further appeals are now pending before the Court in the *Starbucks* (the Netherlands), *Fiat* (Luxembourg), *Apple* (Ireland), *Amazon*

(Luxembourg), and *Engie* (Luxembourg) cases. The General Court's judgment could be read to suggest that the General Court will not be convinced by arguments relating to Member States' sovereign powers in the area of direct taxation.

In contrast, the General Court's judgment offers little insight into the Court's views on the EC's controversial approach to assess the existence of selectivity and advantage in individual tax rulings cases, as the General Court did not address these questions. However, the General Court recognised that the Belgian tax authorities enjoyed a margin of discretion in implementing a specific tax framework (the EPR system). It also remains to be seen whether the EC is required to demonstrate that the national tax authorities exceeded the margin of discretion afforded by the national rules to show that an individual tax ruling departs from the arm's length principle, as the General Court has equally not addressed this question. Nevertheless, this question will be particularly relevant in transfer pricing cases, as the EC itself acknowledged that transfer pricing is not an exact science, and leaves room for discretionary assessment.

EC's State aid investigations into tax rulings to date

Country	Company	Measure	Beginning of investigation	Decision	Amount to be recovered (EUR)	Appeal
Issued decisions						
Luxembourg	Fiat	2012 ruling	11 June 2014	21 October 2015	23.1 million	Pending
Netherlands	Starbucks	2008 ruling	11 June 2014	21 October 2015	25.7 million	Pending
Belgium	At least 35 companies	2004 scheme involving tax rulings between 2004 and 2014	3 February 2015	31 January 2016	Approx. 700 million	Decision annulled by the General Court
Ireland	Apple	1991 and 2007 rulings	11 June 2014	30 August 2016	14.3 billion	Pending
Luxembourg	Amazon	2003 ruling	7 October 2014	4 October 2017	282.7 million	Pending
Luxembourg	Engie	2008 and 2010 rulings (and amendments)	19 September 2016	20 June 2018	Approx. 120 million	Pending
Luxembourg	McDonald's	2009 ruling	3 December 2015	19 September 2018	No aid decision	-
Gibraltar	Five multinationals	Five rulings between 2011 and 2012	16 October 2013	19 December 2018	Approx. 100 million	Pending
Formally opened investigations						
Netherlands	IKEA	2006 and 2011 rulings	18 December 2017	Pending	-	-
Netherlands	Nike	Five rulings between 2006 and 2015	10 January 2019	Pending	-	-
Luxembourg	Huhtamäki	2009, 2012 and 2013 rulings	7 March 2019	Pending	-	-

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