Beyond Goals: Fairness in State Aid Cases

Fairness and selectivity – testing the limits of State aid rules?

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Fairness, State aid & selectivity

In the current context of tight public budgets, **it is particularly important that large multinationals pay their fair share of taxes.**

Competition Commissioner
Joaquín Almunia
on the FFT & Starbucks
opening decision
in June 2014

A fair playing field also means that in Europe, consumers are protected against cartels and abuses by powerful companies. And that every company, no matter how big or small, has to pay its taxes where it makes its profits. […]

Commission President
Jean-Claude Juncker
2016 State of the Union Address

Competition Commissioner
Margrethe Vestager
speech, High Level Forum on State Aid Modernisation, Brussels, 28 June 2017

The state aid rules have also **helped banks to compete on fair terms**. […]
Special tax treatment can also undermine competition, when it gives some companies a benefit which their rivals can't get.
That **special tax treatment** for a handful of companies doesn't support the economy. It just **denies other companies a fair chance to compete**. So when we make companies pay back those special benefits, we're helping to **make competition fairer across Europe**.

Selectivity & (un-)fairness

- General State aid prohibition of Art. 107(1) TFEU, 2nd criterion

  "*favouring certain undertakings or the production of certain goods*"
- Selectivity (eg *Adria Wien Pipeline*, C-143/99, para. 34 & 35)

  "an economic benefit [advantage] granted by a Member State constitutes State aid only if, by displaying a degree of selectivity, it is such as to favour certain undertakings or the production of certain goods."
  "A State measure which benefits all undertakings in the national territory, without distinction, cannot therefore constitute State aid."
- Do some/does someone enjoy an advantage as compared to others in a comparable legal and factual situation?

Question

Is a selective advantage unfair by definition?
(Differentiation, unequal treatment, discrimination)

Selectivity applied

- Selectivity can be relatively straightforward (e.g. individual/*ad hoc* aid)
- *World Duty Free*, C-20/15 P, para. 54 and cases cited

  "*selectivity … requires a determination whether, under a particular legal regime, a national measure is such as to favour "certain undertakings …" over other undertakings which, in the light of the objective pursued by that regime, are in a comparable factual and legal situation and who accordingly suffer different treatment that can, in essence, be classified as discriminatory*"
- Three-step test:
  1. Identify the ordinary or normal regime as benchmark or reference system (*NOx*, Case C-279/08 P, AG Bobec in *BSE/TSE*, Case C-270/15 P, par. 40-51)
  2. Are undertakings treated differently that are, in view of the objectives pursued by the reference system, in a comparable situation (facts & law)? No *prima facie* selectivity if the undertakings are in a different factual or legal situation by reference to the benchmark's objectives
  3. Is the *prima facie* selective treatment justified/in line with nature/logic/general structure of the reference system? (*World Duty Free*, C-20/15 P, para. 58 and cases cited)

Selectivity & non-discrimination

- Discrimination
  - Different treatment of undertakings in a comparable legal and factual situation and
  - Absence of objective justification
- Selectivity
  - Narrower approach "justification" of different treatment in step 2 and 3 limited to the parameters of the reference system
  - Allows wider political objectives to be considered only in the context of the compatibility assessment

Questions:

- Is the narrower approach to differentiation in State aid enforcement fair?
- Why not? State aid addresses competition distortions by Member States in markets in which companies should compete strictly on the merits
- Is direct company taxation different? Maybe? Fiscal autonomy of Member States; bilateral double taxation treaties apply cross-border

Selectivity & the arm's length principle

What is in the arm's length principle?

- Art. 9 of the OECD Model Tax Convention:
  Transactions between related parties should be valued as if they had been carried out between unrelated parties (OECD TPGL: 5 methods)
- Commission's Notice on the Notion of Aid (July 2016):
  "[…], *a tax ruling which endorses a transfer pricing methodology for determining a corporate group entity's taxable profit that does not result in a reliable approximation of a market-based outcome in line with the arm's length principle confers a selective advantage upon its recipient. The search for a 'reliable approximation of a market- based outcome' means that any deviation from the best estimate of a market-based outcome must be limited and proportionate to the uncertainty inherent in the transfer pricing method chosen or the statistical tools employed for that approximation exercise.*" (para. 171)

  "*The arm's length principle the Commission applies in transfer pricing rulings under the State aid rules is therefore an application of Art. 107(1) of the Treaty, which prohibits unequal treatment in taxation of undertakings in a similar factual and legal situation*" (para. 172)

Testing the limits in the tax rulings cases

- Reference system
  - Normal system of corporate income taxation?
  - Transfer pricing rules for related companies and transactions and accounting profit for unrelated companies and transactions?
  - Separate for resident companies (taxed on worldwide income) and non-resident companies (taxed on local income of agency or branch)?
- Differentiation – comparing apples with apples or apples with oranges?
  - Unrelated (arm's length transactions) and related companies (TP), resident/non-resident, cross-border/in-country transaction
  - In TP cases: best estimate of a market-based outcome (any deviation limited and proportionate to the uncertainty inherent in the method chosen or the statistical tools used for approximation)
- In line with objective/nature/general structure of the reference system? Wide reference systems render differentiations very difficult to justify

Does selectivity contribute to fairness …

- By making State aid enforcement fairer?
- By making competition between undertakings fairer?
- By being applied testing the limits of State aid rules?

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