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FIAT V EUROPEAN COMMISSION: FIAT AND LUXEMBOURG'S GREAT FISCAL AUTONOMY VICTORY COMES AT A GREAT COST TO THE COMMISSION

ANIS RASSAM*

The Court of Justice of the EU (CJEU) handed the European Commission a significant defeat in its objective to stop multinational enterprises from benefitting from illegal state aid, mainly through unilateral transfer pricing agreements. The CJEU corrected the Commission's analysis and asserted that conferring a selective advantage from a state policy was only possible by comparing inconsistencies with the Member State's legislation rather than a harsher EU-wide OECD arm's length principle. This article will analyse the issues caused by the case's outcome, such as parity and uncertainty in the Commission's analysis for future cases. Additionally, the article will analyse the mostly unsuccessful use of the state aid provision by the Commission in its other cases and how the amendment of EU laws is needed to turn the tide in the Commission's favour.

I. INTRODUCTION

On 8 November 2022, the Court of Justice of the European Union (CJEU) overturned the decisions of the European Commission and the General Court of the European Union.¹ The CJEU held that the Grand Duchy of Luxembourg's tax ruling in favour of Fiat-Chrysler did not constitute illegal state aid.

The CJEU's decision prevents the Commission from using the standard arm's length principle in determining whether a Member State's tax ruling constituted illegal state aid under Article 107(1) of the Treaty of the Functioning of the European Union (TFEU) unless it was incorporated into the national law of the relevant Member State.

This article examines how the decision hinders the Commission's effort to tackle illegal state aid across the EU in a uniform and effective manner and explores the harmful consequences of the disparity in transfer pricing policies between using the Organisation for Economic Co-operation and Development's (OECD) approach and Luxembourg's more lenient approach. By critically analysing both the CJEU's reasoning and the encompassing body of state aid case law, this article will also assess the several issues that will arise for the Commission due to the CJEU's emphasis on examining the national law as part of the Commission's state aid analysis.

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¹ *Fiat Chrysler Finance Europe and Ireland v European Commission* (Court of Justice of the European Union, C-885/19 P, C-898/19, ECLI: EU:C:2022:859, 8 November 2022) [124] (*'Fiat Chrysler'*).

II. *FIAT* CASE AND FACTUAL BACKGROUND

Fiat-Chrysler's corporate group uses the Luxembourg-based Fiat Finance and Trade Ltd. (FFT) as its group finance subsidiary to manage finances for Fiat's operations in the United States, Canada, and Europe, aside from Italy.² Group finance subsidiaries, such as FFT, borrow from independent sources on the parent entity's credit and provide cash through loans to group members.³ Effectively, the group finance subsidiary allows the related entities in high-tax jurisdictions to transfer their profits to a low-tax rate jurisdiction, like Luxembourg, in interest payments.⁴

A. *Advanced Pricing Agreement*

In 2012, FFT sought and received an advance pricing agreement (APA) through a tax ruling with the Grand Duchy of Luxembourg that granted it a fixed tax base for five years until 2016. In response, the Commission released a lengthy decision stating that the tax ruling constituted incompatible state aid under Article 107 of the TFEU. Article 107 of the TFEU regulates Member States' behaviour that grants selective advantages to specific companies that are not given to other comparable companies, and that effectively results in harmful tax competition. It ordered Luxembourg to recover €23 million from Fiat.

B. *Fiat's Inaccurate, Fixed Tax Base*

In its reasoning, the Commission firstly accused Luxembourg of accepting a decreased, inaccurate, and fixed tax base of €2.5bn per year without regard to FFT's performance fluctuations throughout the five years of the ruling.⁵

C. *Transactional Net Margin Method*

Secondly, the Commission's decision was critical of FFT's choice to use the Transactional Net Margin Method (TNMM) to calculate its taxable profit. The TNMM indirectly calculates taxable gain by comparing the net profit margin from a controlled transaction with a related entity to an uncontrolled transaction with an independent party based on an appropriate base, such as costs, sales, or assets.⁶ The Commission rejected the TNMM approach in favour of the Comparable Uncontrolled Price method (CUP) that directly compares the price charged for a service in a controlled transaction to the price charged for a service in a comparable uncontrolled transaction conducted between independent enterprises.⁷ The Commission noted that FFT could have directly compared its transaction prices to Chrysler, the US company of the Fiat Group, which carried out similar transactions to FFT.⁸

² Lee A. Sheppard, 'Fix it Again, Commission - CJEU 'Transfer Pricing Defeat' (2022) 108 *Tax Notes International* 791, 792.

³ *Ibid.*

⁴ *Ibid.*

⁵ *Ibid.*

⁶ OECD *Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations* (OECD Publishing, 2022) 26 ('OECD Transfer Pricing Guidelines').

⁷ Commission Decision (EU) 2016/2326 of 21 October 2015 on State Aid S.A. 38375 (2014/ C ex 2014/ NN) *Which Luxembourg Granted to Fiat* [2016] OJ L 351/1[132] ('Commission Fiat Decision').

⁸ *Ibid.*

D. *Arm's Length Method*

Thirdly, and most importantly, a major dispute between the Commission and Fiat erupted over choosing the appropriate transfer pricing measurement. Fiat had claimed that the Commission erred in law by failing to consider Luxembourg's Article 164(3) of its Tax Code and the Circular L.I.R. No 164/2 administrative memorandum with its transfer pricing guidelines before determining whether Luxembourg had breached Article 107 of the TFEU. The Commission rejected Fiat and Luxembourg's view. It ruled that FFT's transfer pricing analysis was invalid because it was not carried out under the arm's length principle codified in Article 9 of the OECD Model Tax Convention 2017.⁹ The OECD Model Tax Convention is the international standard for negotiating and implementing most double taxation agreements. Article 9 dictates that when two parties related by management, control, or capital of an enterprise engaged in cross-border transactions, they must transact with each other as if they were two wholly independent enterprises dealing with each other at an arm's length level.¹⁰

The General Court upheld the Commission's decision despite Fiat's objections. It endorsed the Commission's arm's length approach as a tool and agreed that Luxembourg's Fiat tax ruling had granted a selective advantage to the beneficiary not given to comparable companies. Fiat subsequently appealed the decision to the CJEU.

III. THE DECISION

The case had amassed considerable interest among EU Member States, and Ireland intervened on Fiat's and Luxembourg's side and argued for the Member States' fiscal autonomy. Ireland is embroiled in a state aid dispute with the Commission over granting Apple a selective advantage, and Fiat's outcome would subsequently influence its upcoming CJEU case.¹¹

A. *State Aid*

In a landmark ruling, the CJEU accepted Ireland's arguments and ruled that the Commission and the General Court erred in law in determining Luxembourg granted illegal state aid. The Court classified *State Aid* as the following within the meaning of Article 107(1): firstly, there must be an intervention by the State or through State resources; secondly, the intervention must be liable to affect trade between Member States; thirdly, it must confer a selective advantage on the beneficiary; and fourthly, it must distort or threaten to distort competition.¹²

B. *Selective Advantage*

The Court then explained how to find the selective advantage, considered the most contentious element, and how the Commission and the General Court's determination of the selective advantage was an error of law. In identifying a selective measure, the Commission must begin by identifying the reference system, also known as the *normal* tax system applicable in that Member

⁹ Ruth Mason, 'Ding-Dong! The EU Arm's-Length Standard Is Dead' (2022) 108 *Tax Notes International* 1249, 1250.

¹⁰ OECD (2019), Model Tax Convention on Income and on Capital 2017 (Full Version), OECD Publishing. <http://dx.doi.org/10.1787/g2g972ee-en>

¹¹ Mason (n 9) 1249.

¹² *Fiat Chrysler* (n 1) [66].

State concerned; secondly, the Commission must demonstrate that the relevant tax issue derogates from that reference system, as it differentiates from other operators in a comparable factual and legal situation; and thirdly, the differentiation cannot be justified because the measure was not a natural by-product of the system's general structure.¹³

C. Reference System

Critically, the Commission determined that the reference system was Luxembourg's general tax system objective to tax profits of all resident companies regardless of whether they were standalone or integrated entities. The Commission's analysis dismissed Luxembourg's Article 164(3) of the Tax Code & Circular No 164/2 transfer pricing guidelines and instead applied an arm's length principle different from what was incorporated into Luxembourg's law. The CJEU rejected the analysis and held that reference systems must be determined by objectively examining the content, structure, and effects of that Member State's national law. Unless an EU-wide arm's length principle has been ratified and agreed upon through harmonisation, the Member States still exercise their fiscal autonomy in direct taxation.¹⁴ The Commission's error was fatal to its analysis and its case. In further illustrating this principle, the CJEU corrected the Commission and the General Court's interpretation of *Belgium & Forum 187 v Commission (Excess Profits)*,¹⁵ and clarified that *Excess Profits* did not support the proposition of the arm's length principle being applied irrespective of whether that principle had been incorporated into law. Instead, the Court clarified that the OECD arm's length principle was used in *Excess Profits* because Belgium's transfer pricing guidelines had explicitly incorporated the OECD guidelines into its legislation.

IV. THE IMPLICATIONS

It must be noted that the Court's decision did not absolve multinational enterprises (MNEs) or Member States from the scope of the TFEU's state aid provision. The Court required the Commission to establish that the national law's policies are inconsistent with the objective of taxing all resident companies equally, regardless of whether they are standalone or integrated companies, by systematically leading to an undervaluation of transfer prices of the integrated companies compared to market prices for comparable transactions carried out by standalone companies.¹⁶ While the Court's decision was a significant victory for Member States' fiscal autonomy powers concerning direct taxation, the author submits that the outcome inadvertently creates parity issues and long-term uncertainty in establishing illegal state aid liability. This section of the article will analyse the immediate ramifications of CJEU's decision. It will also show the upcoming disadvantages facing the Commission in its goal to punish harmful tax practices due to the Court's emphasis on determining selective language through derogation from the national law rather than OECD guidelines.

¹³ Ibid [68].

¹⁴ Ibid [73].

¹⁵ *Kingdom of Belgium v European Commission* (General Court of the European Union, T-131/16, ECLI:EU:T:2023: 561, 20 September 2023) '*Kingdom of Belgium*'.

¹⁶ Min Shi, 'Fiat Emerges Victorious in State Aid Battle with European Union: What's Next?' (2023) 63(2/3) *European Taxation* 124, 128.

A. *Parity*

Firstly, the CJEU's decision effectively creates a two-tier European jurisdiction system, dividing EU Member States into tax haven jurisdictions with flexible transfer pricing guidelines, such as Luxembourg, and non-tax haven jurisdictions that have fully incorporated the OECD's arm's length principle into their domestic laws. Previously the Commission had targeted tax havens and insufficiently regulated international financial centres in non-EU countries whose lack of transparency was found to have facilitated tax evasion, tax fraud, and tax avoidance.¹⁷ However, the CJEU's decision risks market Member States having their tax base eroded, and their revenues shifted to lower tax rate jurisdictions within the EU, such as Luxembourg.

The Commission's threshold for proving a grant of illegal state aid is raised in cases involving Member States of lower tax rate jurisdictions with lax transfer pricing guidelines as they do not incorporate the stricter OECD arm's length principle into national law. Although Member States will have an observable corporate tax rate of more than 20% on taxable profits, the Member State, as seen in *Fiat*, can elect to decrease the company's tax base by legislating transfer pricing guidelines that do not enforce the arm's length principle to the standard mandated by the OECD. Ultimately, the effective paid tax rate will remain low. As a result, countries will start competing to offer these tax incentives through discreet tax rulings to lure MNEs into establishing tax residency in their country in what is seen as a race to the bottom. The discrepancy between the Member States' transfer pricing guidelines could lead to resentment and division between Member States over the perceived harmful tax practices generating less revenue overall for the EU.

B. *EU Blacklist*

Secondly, the author submits that the case's outcome is also problematic amidst the backdrop of the expansion of the EU blacklist. Formally known as the EU list of non-cooperative jurisdictions for tax purposes, the EU blacklist is defined by the unilateral imposition of EU standards in tax and non-tax areas to force compliance by typically low-income non-EU countries.¹⁸ It has been criticised for creating an uneven playing field through its excessive punishment of low-income countries such as Dominica, which was blacklisted for being a tax haven after suffering the devastation of two natural disasters.¹⁹ The EU holds an immense amount of power in influencing lower-income jurisdictions to comply with its guidelines, and it uses the blacklist to project soft power. Nonetheless, using the blacklist against non-EU countries is hypocritical, given the EU's prolonged failure to contain tax havens among its Member States. The Court's decision will further increase the appeal for Member States such as Ireland and Luxembourg to be seen as tax haven locations of choice, given their immunity from the blacklist and their stable political and economic systems. This development puts the EU's use of the blacklist into the spotlight and prompts more questions regarding its fairness. Optically, it is unpleasant for the EU to continue admonishing low-income countries attempting to attract foreign investment to boost their struggling economies for being tax havens when the EU's legislatures and highest courts continue to facilitate tax havens within the EU.

¹⁷ Stefanie Geringer, 'Dissemination of Tax Good Governance Standards by the European Union and the OECD: A Comparative Analysis of Changes in Treatment and Tone' (2023) 77(4) *Bulletin for International Taxation* 1, 2.

¹⁸ *Ibid* 1-2.

¹⁹ *Ibid* 9.

C. *OECD Arm's Length Contrasted with Luxembourg's Arm's Length*

Thirdly, examining state aid grants through the lens of the incorporated national law instead of an EU-wide OECD-based arm's length principle causes greater uncertainty in determining a Member State's liability. The OECD transfer pricing guidelines (OECD TPG) are regarded as the global standard in creating guidelines that combat tax avoidance by MNEs.²⁰ In conjunction with the G20 and following extensive consultations, the OECD released a Base Erosion and Profit Shifting (BEPS) 15-point action plan to tackle and restrict base erosion profit shifting tools used by MNEs to lower their tax liability.²¹ Although the Article 9 Commentary of the latest OECD Model Tax Convention did not explicitly reference the BEPS Action Plan, the latest OECD Model Tax Convention underwent significant changes to address base erosion and profit-shifting activities that have damaged the global economy.²² In particular, Action 5 of the 2015 BEPS Report aims to encourage fair tax competition, levelling the playing field and preventing the race to the bottom caused by harmful tax practices such as illegal state aid grants.²³ The OECD reports provide thorough commentary and rationale behind the proposed guidelines to prevent further global economic losses.

In comparison, a Member State's sparsely written transfer pricing guidelines offer limited assistance to the Commission in determining the legality of a transfer pricing-related measure under Article 107 of the TFEU.²⁴ On numerous occasions, Luxembourg's laws and guidelines have not provided the clarity and certainty that the Commission requires to determine a granted selective advantage derogated from the reference system. Luxembourg had very limited official transfer pricing guidelines before Circular No 164/2 (2011 Circular), which was only implemented in 2011. Implementing the 2011 Circular was regarded as a marked improvement in providing more transparent guidelines. Still, unlike the Netherlands, the document did not mention calculating arm's length prices for licensing activities,²⁵ nor did it advise for or against using any transfer pricing method in the circumstances. Critically, Luxembourg's resident companies that received royalties from licensing patents, trademarks, copyrights, and trade secrets did not fall under the 2011 Circular's scope.

D. *Difficulty in Determining an Appropriate Reference System*

Without referring to established external parameters such as the OECD guidelines, it is more challenging for the Commission to establish a reference system based on a vague and inconclusive

²⁰ *Objet: Traitement fiscal des sociétés exerçant des transactions de financement intra-groupe* (Luxembourg) [Circular No 56/1, Subject: Tax Treatment of Companies Carrying Out Financing Transactions Intra-Group], 1-2 <<https://impotsdirects.public.lu/dam-assets/fr/legislation/legi16/circulairelirelir561-56bis1-27122016.pdf>> ('Circular No 56/1').

²¹ *Action Plan on Base Erosion and Profit Shifting* (OECD Publishing, 2013) 8.

²² 'Tax Treaties: Update to OECD Model Tax Convention Released', *OECD* (Web Page, 18 December 2017) <[https://www.oecd.org/tax/treaties/tax-treaties-2017-update-to-oecd-model-tax-convention-released.htm#:~:text=18%2F12%2F2017%20%E2%80%93%20The,erosion%20and%20profit%20\(BEPS\)>](https://www.oecd.org/tax/treaties/tax-treaties-2017-update-to-oecd-model-tax-convention-released.htm#:~:text=18%2F12%2F2017%20%E2%80%93%20The,erosion%20and%20profit%20(BEPS)>)>.

²³ *OECD/G20 Base Erosion and Profit Shifting Project: Countering Harmful Tax Practices More Effectively, Taking into Account Transparency and Substance, Action 5 – 2015 Final Report*, (OECD Publishing, 2015) 11-12.

²⁴ Ryan Finley, 'Fiat and the Rejection of External Transfer Pricing Parameters' (2022) 108 *Tax Notes International* 1354, 1358.

²⁵ Séverine Baranger and Geoffrey Scardoni, 'Luxembourg's New Rules for Group Financing Companies' (2011) *Tax Notes International* 1, 2.

set of rules, as in *Fiat*. The Commission's official decision to disallow the tax ruling argued that Circular did not provide any information on how to estimate the expected return of capital, nor did it contain information on how the equity was to be considered except that it must be 'sufficient in order to assume the risks'.²⁶ The Commission argued that the relevant missing explanations from the Circular, coupled with the lack of connection on how the Circular's broad criteria produced FFT's assessment, indicated an illegitimate reference system.²⁷ On this point, the CJEU's decision was unhelpful as it did not demonstrate why the Circular was an appropriate reference system made of a consistent set of rules; it only stated that the Commission erred in law by not considering the incorporated national law in its analysis.

Furthermore, in 2019, Luxembourg adopted new rules to limit interest deduction payments to the greater of 30% of Earnings Before Interest, Taxes, Depreciation, and Amortization (EBITDA) or €3 million.²⁸ However, financial undertakings and standalone entities have been excluded from the scope of the new rules.²⁹ The extent of the exemption applies to all finance subsidiaries established in Luxembourg and not Fiat specifically. The Commission cannot prove that a selective advantage has been granted to the beneficiary that derogates from the reference system because all finance subsidiaries will be eligible for the exemption.

Additionally, Luxembourg's legislation or regulations do not contain any specific guidance regarding the pricing of controlled transactions involving intangibles.³⁰ The latest OECD TPG state the difficulty in determining arm's length remuneration for transactions involving intangibles for the following reasons: the lack of comparability between the intangible-related transactions undertaken between associated enterprises and transactions that can be identified between independent enterprises; the lack of comparability between the intangibles in question; the difficulty in separating a particular intangible from the MNE group's income; and the fact that MNE groups may carry out activities relating to the development, protection, and exploitation of an intangible that is not replicated between independent enterprises.³¹ Given the enormous difficulty in determining the transfer price of intangibles, it is perplexing that Luxembourg has not introduced some much-needed guidelines regarding their pricing. The ambiguity only perpetuates confusion and makes it increasingly difficult for the Commission to establish whether a selective advantage was granted to a beneficiary through state aid.

E. Satisfying Criteria Required to Adopt OECD Arm's Length

Finally, the Court's distinguishment of the *Excess Profits* case from *Fiat* was not explained sufficiently well. The Court corrected the Commission's interpretation and asserted that *Excess Profits* did not support the proposition that the OECD arm's length principle could be used even if it was not incorporated into the Member State's national law. The CJEU endorsed using the OECD arm's length principle as the reference system only if it was explicitly incorporated into that Member

²⁶ *Commission Fiat Decision* (n 7) [323].

²⁷ *Ibid* [326]-[336].

²⁸ Katerina Pantazatou, 'Critical Review of the ATAD Implementation: The Implementation of the ATAD in Luxembourg', (2022) 50(1) *INTERTAX* 56, 57.

²⁹ *Objet: Limitation de la déductibilité des intérêts*, (Luxembourg) [Circular No 168/1, Limitation of Interest Deductibility], 32 <<https://impotsdirects.public.lu/dam-assets/fr/legislation/legi21/2021-06-03-LIR-168bis-1-du-262021.pdf>>.

³⁰ 'Luxembourg Transfer Pricing Country Profile', *OECD* (PDF, February 2022) 3 <<https://www.oecd.org/tax/transfer-pricing/transfer-pricing-country-profile-luxembourg.pdf>>.

³¹ *OECD Transfer Pricing Guidelines* (n 6) 256.

State's national law. However, the Court's refusal to explain why Luxembourg's 2011 Circular text did not constitute an endorsement of the OECD arm's length principle despite several references to OECD guidelines puzzled some experts.³² The 2011 Circular referred to calculating the transfer price by approximating what two independent parties would have agreed to transact in comparable circumstances.³³ Moreover, the 2011 Circular emphasises the need to examine whether the transactions are comparable by analysing the functions performed, the terms and conditions of the contract, the economic circumstances of the parties and the business strategies pursued by those parties.³⁴ The 2011 Circular also affirms the need to calculate a transaction's remuneration by evaluating the risk taken by the lender to lend the money.³⁵ Similarly, to *Excess Profits*,³⁶ both legislative materials in question explicitly mentioned and endorsed the OECD guidelines as the benchmark yet the results were the opposite. There was a tacit understanding that Luxembourg had finally aligned itself with OECD's transfer pricing guidelines, yet the Court's decision rescinded that without much explanation. The Court has not elaborated why 2011 Circular's multiple references to OECD's conditions were insufficient to implement the OECD's arm's length principle as the reference system for the Commission's selective advantage analysis. Additionally, the interpretation of Circular No 56/1 (2016 Circular), which was adopted in 2016 and replaced the 2011 Circular, is now also equivocal as it is unclear how the law should be drafted in order to endorse the OECD guidelines. Despite 2016 Circular's multiple references to the OECD guidelines in regard to its price analysis,³⁷ the CJEU's failure to elaborate on how legislation can clearly adopt OECD material renders the Commission's analysis even more difficult in the foreseeable future.

F. *Summary of the Commission's Upcoming Challenges*

In short, *Fiat's* outcome is a sizable setback in the Commission's efforts to fight harmful tax practices. Not only does it attract attention to the uneven tax regimes of the Member States, but it also perpetuates considerable uncertainty in the Commission's selective advantage analysis because the Member States' national laws do not provide the clarity nor precision that the OECD guidelines do. It is burdensome or sometimes impossible for the Commission to establish a derogation from the reference system when it is not well defined for intra-group finance companies or ceases to exist in the case of Luxembourg's intangible guidelines. This article has analysed chiefly the case's outcome on the Commission's ability to prosecute state aid grants against Luxembourg. It must also be mentioned that *Fiat's* outcome will naturally complicate the Commission's state aid pursuits in other tax haven jurisdictions within the EU, such as Ireland, Netherlands, and Belgium. The judgment's focus on preserving the Member States' fiscal autonomy rather than guiding the Commission in interpreting national laws has made prosecuting state aid under Article 107 of TFEU almost impossible.

³² Finley (n 24) 1355.

³³ *Objet: Traitement fiscal des sociétés exerçant des transactions de financement intra-groupe* (Luxembourg) [Circular No 164/2, Subject: Tax Treatment of Companies Carrying Out Financing Transactions Intra-Group], 2 <https://impotsdirects.public.lu/dam-assets/fr/legislation/legi11/Circulaire_L_I_R_n__164-2_du_28_janvier_2011.pdf>.

³⁴ *Ibid.*

³⁵ *Ibid.*

³⁶ *Commission Decision (EU) 2016/1699 of 11 January 2016 on the Excess Profit Exemption State Aid Scheme S.A.37667 (2015/C) (ex 2015/NN) Implemented by Belgium* [2016] OJ L 260/61, [33] ('*Commission Excess Profits Decision*').

³⁷ Circular No 56/1 (n 20) 1-2.

V. THE COMMISSION'S OFFENSIVE AGAINST MNEs

The lengthy *Fiat* investigation and subsequent litigation are not outliers but are instead part of a broader strategy on the Commission's behalf to ensure MNEs pay their fair share of tax. Since Margrethe Vestager assumed office as the head EU Commissioner for the Competition portfolio in November 2014, the Commission has aggressively prosecuted perceived harmful tax practices committed by large MNEs.³⁸ The Commission's efforts were concerned with the transfer of profits to and from tax haven Member States through intra-company transactions.³⁹

However, the Commission's adoption of the illegal state aid provision under Article 107 of the TFEU to tackle unlawful tax practices, also known as 'Vestager's doctrine', has produced mixed outcomes.⁴⁰ As explored in this section, the EU Courts have mostly dismissed the Commission's investigations for not satisfying the required state aid criteria.

A. Starbucks Case

In a case concerning Starbucks (*Starbucks*), the Commission alleged that the Dutch tax authorities supplied a selective advantage to Starbucks Manufacturing BV (SMBV, a Dutch resident) by artificially lowering its tax contributions and ordered the recovery of that aid.⁴¹

The General Court annulled the Commission's decision, but its judgment also provided the Commission with a silver lining. The General Court held that 'mere non-compliance with methodological requirements did not necessarily lead to a reduction of the tax burden' and 'the Commission would have to demonstrate that the methodological errors identified in the APA did not allow for a reliable approximation of an arm's length outcome leading to a reduction of the tax burden'.⁴² In other words, minor deviations from the standard do not satisfy the high threshold for proving an illegal state aid grant. However, the General Court accepted the Commission's adoption of the arm's length principle as a tool to assess the legitimacy of intra-group transaction prices and its use regardless of whether the Member State had incorporated it into its national legal system (this aspect of the Court's decision is now uncertain in the wake of CJEU's *Fiat* judgment).⁴³

Despite its defeat, the *Starbucks* judgment was perceived as a victory for the Commission because the Court endorsed the Commission's stricter interpretation of the arm's length principle over the more lenient approach incorporated into the Netherlands' national law.⁴⁴ The *Starbucks* judgment emboldened the Commission to advance and continue its investigations using the state aid provision.

³⁸ Guido Bellenghi, 'The General Court in *Amazon* and *Engie*: A New Effect-Based Approach Aimed at the Endorsement of the "Vestager Doctrine"?' (2021) 6(2) *European Papers* 1097, 1098.

³⁹ *Ibid* 1099.

⁴⁰ *Ibid* 1114.

⁴¹ *Commission Decision (EU) 2017/502 of 21 October 2015 on State Aid S.A. 38374 (2014/C ex 2014/NN) implemented by the Netherlands to Starbucks* [2017] OJ L 83/38.

⁴² *Netherlands v. European Commission* (General Court of the European Union, T-760/15, T-636/16, ECLI:EU:T:2019:669, 24 September 2019) [201].

⁴³ Patricia Lampreave Márquez, 'Key Developments Regarding Court Cases on Tax Rulings' (2023) 63(6) *European Taxation* 247, 250.

⁴⁴ Dimitrios Kyriazis, 'Why the EU Commission won't appeal the Starbucks judgment', *MNE Tax* (Web Page, 10 December 2019) <<https://mnetax.com/why-the-eu-commission-wont-appeal-the-starbucks-judgment-37043>>.

B. *Apple Case*

In a landmark decision, the Commission held that Ireland's grant of two APAs in favour of two companies of the Apple group unjustly reduced their tax liability in Ireland during the rulings and ordered the recovery of €13 billion in state aid.⁴⁵

However, the General Court annulled the Commission's decision again. In line with its judgment in *Starbucks*, the Court affirmed that the Commission was authorised to use its interpretation of the arm's length principle to calculate the independent transfer price of intra-group transactions.⁴⁶ Critically, the Court ruled that the Commission did not demonstrate that Apple intellectual property ('IP') and its associated profits should have been attributed to Apple's Irish branches or that insufficient profits were allocated to Apple's Irish branches.⁴⁷ The Commission failed to satisfy the high threshold required to prove the grant of a selective advantage.

Similar to *Fiat*, the issue of state autonomy has also arisen. Apple and Ireland have both alleged that the Commission erred in law by applying the OECD arm's length principle in its assessment since it was not incorporated into Irish law then and was hence not applicable in Ireland.⁴⁸

Nonetheless, in preparing his advisory opinion for the CJEU, Advocate General Pitruzella found that the General Court committed several legal errors in assessing the Commission's decision by incorrectly applying the arm's length principle and misidentifying the standard of proof required to prove a selective advantage. The contrasting outcome of the advisory opinion from the General Court judgment reflects the difficulty in determining the objectivity and the existence of a selective advantage. The usage of the state aid provision is setback by uncertainty and confusion as to what amounts to a selective advantage.

C. *Amazon Case*

LuxOpCo, an Amazon company incorporated in Luxembourg, paid significant royalties to LuxSCS, a US company in the group, in exchange for the right to use the e-commerce platform used by the Amazon group in Europe.⁴⁹ The Commission alleged that the arrangement shifted profits to the US, resulting in double non-taxation. The Commission contended that LuxSCS merely held the legal ownership of IP assets but did not incur any risks or undertake any functions to merit receiving large remuneration sums from LuxOpCo.⁵⁰

The General Court nullified the Commission's decision on the basis that the Commission failed to discharge its burden of proof. Following the reasoning in *Apple* and *Starbucks* judgments, the Court asserted that mere non-compliance with methodological requirements did not necessarily result in a reduction in the tax burden; the Commission had to demonstrate further that the tax ruling did

⁴⁵ *Commission Decision (EU) 2017/1283 of 30 August 2016 on State Aid S.A. 38373 (2014/C) (ex 2014/NN) (ex 2014/CP) Implemented by Ireland to Apple* [2017] L 187/1.

⁴⁶ *Ireland and Others v European Commission* (General Court of the European Union, T-778/16, T-892/16, ECLI:EU:T:2020:338, 15 July 2020) [323].

⁴⁷ *Márquez* (n 43) 252.

⁴⁸ Beckett Cantley and Geoffrey Dietrich, 'Apple v. European Commission: Losing the War on Corporate International Transfer Pricing' (2022) 45(1) *Loyola of Los Angeles International and Comparative Law Review* 1, 6.

⁴⁹ Bellenghi (n 38) 1098.

⁵⁰ *Commission Decision (EU) 2018/859 of 4 October 2017 on State aid S.A.38944 (2014/C) (ex 2014/NN) implemented by Luxembourg to Amazon* [2018] OJ L 153/1 [430].

not allow a reliable approximation of an arm's length outcome and that reduced the taxable profit in comparison to an undertaking placed in a comparable factual situation and where the taxation rules are normally applied.⁵¹

The CJEU agreed with Advocate General Kokott and upheld the General Court's finding, albeit for different reasons. The Court vitiated the Commission's selective advantage analysis, again, for considering OECD transfer pricing guidelines that were not incorporated into Luxembourg's tax law. Referring to its *Fiat* analysis, the Court reiterated the principle of state autonomy. Without the harmonisation of the OECD arm's length principle into EU transfer pricing law, the Commission is forced to consider cases on a country by country basis.

D. Belgian Excess Profit Rulings

The central issue in the *Excess Profits* case was whether the excess profit ruling with a transfer pricing component involved an aid scheme.⁵² Magnetrol International received a profit ruling exempting some of their profits from being subject to the Belgian Corporate Income Tax (CIT) through a downward profit adjustment on their transactions.⁵³ The Commission contended that the ruling satisfied the definition of an aid scheme because the profit exemptions were granted without requiring further implementing measures, and the ruling defined the beneficiaries in a 'general and abstract manner'.⁵⁴

The General Court nullified the Commission's decision for wrongly concluding that the excess profit exemption constituted an aid scheme. Nevertheless, the CJEU allowed the Commission's appeal and remitted the issue back to the General Court to determine the existence of selective advantage and the breach of state aid law. The CJEU established the existence of the aid scheme for the following reasons: firstly, the systematic application of excess profit exemptions for multiple companies prevented the tax authorities from implementing further measures; secondly, the Belgian authorities exercised little discretion because they granted the profit exemption after certain conditions were met; and finally, the beneficiaries were defined in a general and abstract manner since every company received the tax ruling after applying for it.⁵⁵

The General Court ruled in favour of establishing that the Belgian tax authorities' rulings produced a selective advantage. The Court found that the Belgian Corporate tax system intended to tax all realised profits, and the impugned provision allowed the authorities to grant tax rulings that reduced the tax liability of a corporate group member to a lower portion than what they otherwise had to pay.⁵⁶ While Belgium and the individual companies still reserve the right to appeal, the case is a significant yet rare victory for the Commission. It will provide it with momentum for its upcoming appeal to the CJEU concerning the *Apple* case.

⁵¹ *Luxembourg and Amazon v European Commission* (General Court of the European Union, T-816/17, T-318/18, ECLI:EU:T:2021:252, 12 May 2021) [125].

⁵² Márquez (n 43) 253.

⁵³ Ibid.

⁵⁴ *Commission Excess Profits Decision* (n 36) [94]-[96].

⁵⁵ Márquez (n 43) 254.

⁵⁶ *Kingdom of Belgium* (n 15) [[97]-[101].)

E. *Review of EU's Tax Ruling Saga*

Under Vestager's rule, the Commission has embarked on an offensive against MNEs and facilitating Member States to confront anti-competitive harmful tax practices. However, its usage of the state aid provision is mainly unsuccessful for two reasons.

Firstly, EU Courts have strongly qualified the establishment of a selective advantage, as seen in *Apple*, *Amazon*, and *Starbucks*. Mere non-compliance with state aid's methodological requirements is not enough to determine the grant of a selective advantage to a company; the Commission must prove a manifest error in each Member State's tax rulings that causes intra-company transactions to fall outside the approximate range of an arm's length outcome, leading to a lower tax burden. The Commission has struggled to discharge its burden of proof and that has weakened the potency of the state aid provision. Critically, the cases of *Apple*, *Amazon*, and *Starbucks* have established a higher threshold for proving a grant of selective advantage. However, the *Fiat* case offers no guidance on how the Commission can carry out their analysis based on vague and sparse transfer pricing guidelines.

Secondly, *Fiat* makes it clear that the Commission's success in proving the existence of a selective advantage depends on the tax authorities sanctioning a ruling contrary to the objective and content of their tax systems instead of the stricter OECD principle. The Commission is thwarted where the Member State has lenient transfer pricing guidelines that provide tax exemptions to particular groups or standalone undertakings, as was the case in *Fiat*. The Commission only succeeded in the *Belgium Excess Profits* case because the Belgian law expressly mandated tax payment on the entirety of profits for both standalone and group entities.

VI. THE COMMISSION'S NEXT STEPS

The Commission will avoid using Article 107 of TFEU to confront state aid for the above reasons. It will instead seek other approaches to combat MNEs' tax avoidance in its upcoming high-profile cases. Currently, the Commission is appealing the General Court decision involving *Apple's* state aid case to the CJEU. As *Fiat's* issue concerning the applicability of an OECD arm's length principle is also present in the *Apple* case, the Commission must quickly rely on new arguments to turn the tide in its favour, given what is at stake.

Logically, if the Commission cannot win its cases through the courts, it should level the playing field by introducing new legislation to increase its powers. The *Fiat* decision stated that the Commission could use the OECD arm's length principle as the reference system in state aid cases if the EU unanimously ratifies the OECD's arm's length principle in a process referred to as harmonisation.⁵⁷ There has been a growing appetite for homogenous EU laws on the tax base calculation, minimum tax rate, and the formulary apportionment of profits between EU Member States to replace the much-debated proposal for a common consolidated corporate tax base.⁵⁸

According to Benjamin Angel, the director of direct taxation at the Commission's Directorate-General for Taxation and Customs Union, The Business in Europe: Framework for Income Taxation (BEFIT) initiative aims to codify OECD transfer pricing guidelines into Union law to

⁵⁷ *Fiat Chrysler* (n 1) [93].

⁵⁸ Elodie Lamer, 'EU Official Wants Tax Avoidance Enablers to Lose Business' (2023) *Tax Notes International* 1, 2.

counter the *Fiat* decision and institute an EU wide arm's length principle based on the OECD Article 9 standard.⁵⁹

The transfer pricing proposal will apply to all companies established in an EU Member State. In future cross-border transactions with an associated enterprise, EU entities are expected to determine the amount of taxable profits in a manner consistent with the OECD arm's length principle.⁶⁰ The proposal also regulates the use of each transfer pricing method in light of the circumstances, and it gives the Commission the power to criticise the usage of a particular method by a Member State and recommend another method.⁶¹

The new proposals grant much-needed ammunition to the Commission in its campaign against MNEs and address the parity issues caused by the *Fiat* judgment. Nonetheless, it is uncertain whether all the Member States will unanimously agree upon the proposal.

VII. CONCLUSION

The *Fiat* decision significantly set back the Commission's state aid prosecution. It took away its power to automatically apply the stricter OECD arm's length principle without considering the state's transfer pricing guidelines incorporated into its national law. This consequently risks dividing the EU into jurisdictions that facilitate tax avoidance through lax regulations and Member States that insist on incorporating the OECD standard into their national law.

Furthermore, the Commission will find it increasingly challenging to establish a selective advantage through the lens of the limited and vague national laws that sometimes provide little or no guidance on determining an appropriate arm's length price. Lastly, the *Fiat* decision did not explain why Luxembourg's Circular No 164/2, despite all its references to Article 9's commentary, was not regarded as incorporating the OECD arm's length principle into its law.

The *Fiat* judgment is not an isolated result. Instead, it cements the state aid provision's shortcomings in tackling harmful tax practices for two main reasons. Firstly, the Courts have emphasised a high threshold for proving the grant of a selective advantage; mere errors are not sufficient to establish a derogation from the reference systems. Secondly, the Commission's success often depends on proving a selective advantage in tax haven member states that have normalised the non-taxation of entities in their legal systems. Accordingly, the weaknesses of the state aid provision significantly hinder the Commission's prospects of success.

Consequently, the Commission has now been forced to advance harmonisation of the OECD arm's length principle to shift the momentum back to its side. However, there is no guarantee of whether the Commission can convince the EU to adopt its ambitious goals unanimously. The question also remains whether the Commission can achieve its goals expeditiously.

⁵⁹ Ibid.

⁶⁰ Jasper Korving, "BEFIT and HOT: Faster and SAFE!" EU Law or Slogan for Slimming Pills' (2023) 63(12) *European Taxation* 1, 5.

⁶¹ Ibid 6.