

Selectivity in Fiscal Aids: Recent Developments

by

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Abstract

The notion of fiscal aid is becoming crucial in determining the relationship between supra-national integration and national tax sovereignty; the selectivity criterion is often key in the assessment of compatibility of fiscal measures with Article 107(1) TFEU. Therefore, the notion of selectivity as defined by the recent case-law of the CJEU and decision-making practice of the Commission is fundamental in order to understand the actual allocation of powers in direct taxation matters. Against this backdrop, the aim of the present article is to establish what the current notion of selectivity is in fiscal aids, assessing whether the approach used by the CJEU and the Commission share common patterns, and evaluating the impact of such interpretation on the division of competences within the EU. In particular, this article offers a critical reading of the recent *European Commission v. World Duty Free* case and of the so-called Tax Rulings Decisions.

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Résumé

La notion d'aide fiscale est en train de devenir cruciale dans la détermination des relations entre l'intégration supranationale et la souveraineté fiscale nationale. Le critère de la sélectivité joue souvent un rôle fondamental dans la détermination de la compatibilité des mesures fiscales avec l'article 107 (1) TFUE. Par conséquent, la notion de sélectivité, comme déterminée par la récente jurisprudence de la CJUE et la pratique décisionnel de la Commission, est fondamentale pour comprendre la répartition des pouvoirs en matière de taxation directe. Dans ce contexte, le but du présent article est d'établir quelle est la notion actuelle de sélectivité dans les aides fiscale, en évaluant si les approches utilisées par la CJUE et la Commission partagent un modèle commun et l'impact de cette interprétation sur la répartition des compétences au sein de l'UE. En particulier, cet article offre une lecture critique du récent arrêt Commission européenne c. World Duty Free et des soi-disant «Tax Rulings».

Key words: State aid; fiscal aid; selectivity, Spanish Goodwill; tax rulings; allocation of powers; tax harmonization

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I. Introduction

Article 107(1) TFEU lays down the requirements that qualify a State intervention in the economy as an aid incompatible with the internal market, which is therefore forbidden. In particular, it provides that 'any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods shall, in so far as it affects trade between Member States, be incompatible with the internal market'. The notion of State aid mostly derives from the interpretation of these criteria, as elaborated by the Court of Justice of the European Union (hereinafter; CJEU).¹ By analysing the CJEU case-law, it is self-evident that these requirements have a different impact on State aid assessment, even though they are cumulative criteria that formally have the same importance on the evaluation (Boccaccio, 2016).

In determining the compatibility of a tax measure with State aid rules, selectivity is often the crucial element, since other conditions laid down in

¹ For an overview of settled case-law on State aid, see European Commission, *Commission Notice on the notion of State aid as referred to in Article 107(1) of the Treaty on the Functioning of the European Union*, OJ C 262, 19.7.2016, p. 1–50.

Article 107(1) TFEU are almost always satisfied (Bartosch, 2009; Lovdahl Gormsen, 2016). The notion of selectivity was developed by the CJEU and the Commission mostly in cases where the measure at stake was a fiscal benefit, also because of the importance of the requirement in this context.

Moreover, fiscal aids ‘lie on the boundary of the division of competence’ between the EU and its Member States (Nicolaidis, 2007). Therefore, the selectivity criterion plays a pivotal role in this division of powers in direct taxation matters, since it draws a red line between what is left to the discretion of the Member States and what is covered, instead, by the notion of State aid subjected to the control of the Commission. On this ground, the notion of selectivity in fiscal aids as defined by the most recent CJEU case-law and Commission decision-making practice is key in determining the extent of the EU Institutions’ ‘interference’ with the national fiscal sovereignty of the Member States.

In the light of the above, the aim of the present article is to establish what the current notion of selectivity for the purpose of Article 107(1) TFEU is in relation to tax measures; assessing whether the approaches used by the CJEU and the Commission share a common pattern; and if they could truly impinge upon the fiscal sovereignty of the Member States. Therefore, section II purports to define the concept of selectivity in fiscal aids, section III and IV focus on recent developments in the CJEU case-law and Commission decision-making practice respectively, with specific reference to the *World Duty Free* judgment and the Commission decisions on tax rulings. Lastly, in section V, some conclusions will be drawn from the framework provided.

II. Selectivity in fiscal aids: the background

The extension of the notion of selectivity takes a decisive role in determining the scope of the application of Article 107(1) TFEU with regard to fiscal measures. The notion has been mostly shaped by the CJEU, which contributed to the development of the concept of selectivity by identifying its constitutive elements. Moving from the assumption that the evaluation of selectivity should be made on the grounds of the practical effects produced by the measure, without taking into account its formal structure,² the CJEU identified two types of selectivity: geographical (or regional or territorial) and material selectivity.

² Court of Justice, Judgment of 2 July 1974, Case C-173-73, *Italian Republic v Commission of the European Communities*, para. 13.

Geographical selectivity concerns measures that grant more favourable treatment to undertakings of a specific part of the national territory compared to others. The turning point in the CJEU case-law on regional selectivity occurred with the judgment on the *Azores* case³ (Moreno González, 2017). In this judgment, the Court of Justice considered the extent to which the low tax regime applied to the Autonomous Region of the Azores, and adopted by an infra-State body, constituted a selective measure compared to the general Portuguese tax system. The Court of Justice stated that for the assessment of the selectivity of a measure, there must be an examination of whether the infra-State body detained a sufficiently autonomous power (institutional, procedural and financial) with respect to the central authority, detailing the criteria that shall be used for this evaluation, and whether the measure actually applies to all undertakings of the territory under the infra-State body's competence (Stuart, 2017; Lindsay-Poulsen, 2008; Bousin and Piernas, 2008; Da Cruz Vilaca, 2009). This approach towards regional selectivity was confirmed and specified in the subsequent case-law of the CJEU, such as the *UGT Rioja* case⁴, which discussed the compatibility of a fiscal scheme approved by the Historical Territories of the Basque Country that entailed a lower tax rate compared to the rest of Spain.

The legal framework seems less certain with regard to material selectivity where the case-law is more casuistic (Moreno González, 2017; Pérez-Bernabeu, 2017). Material selectivity affects measures that are aimed at granting an advantage to a limited number of beneficiaries on the ground of discriminatory criteria. The assessment of selectivity relies on the well-known, three-step analysis⁵ developed by the CJEU. Over the years, the analysis has been refined and clarified, but it still involves a certain degree of uncertainty due to some interpretative difficulties and the discrepancy between the case-law of the CJEU and the Commission practise (Pérez-Bernabeu, 2017). The three-step analysis, or 'derogation test', consists of the following stages. First, it is necessary to identify the 'the common or normal regime under the tax system applicable in the geographical area constituting the relevant reference framework.'⁶ Since fiscal aids can be considered as a relief from a burden (instead of a positive benefit), it is extremely important to identify the reference framework that

³ Court of Justice, Judgment of 6 September 2006, Case C-88/03, *Portuguese Republic v Commission of the European Communities*.

⁴ Court of Justice, Judgment of 11 September 2008, Joined cases C-428/06 and C-434/06, *Unión General de Trabajadores de La Rioja (UGT-Rioja) and Others v Juntas Generales del Territorio Histórico de Vizcaya and Others*.

⁵ *Commission Notice on the notion of State aid*, cit., para. 126–128.

⁶ General Court, Judgment of 18 December 2008. Cases T-211/04 and T-215/04 *Government of Gibraltar (T-211/04) and United Kingdom of Great Britain and Northern Ireland (T-215/04) v Commission of the European Communities*, para. 143.

makes it possible to compare the contested measure with normal tax, or the tax that would have otherwise been paid by the beneficiary (Nicolaidis, 2015; Arena, 2017c). The second step of the assessment concerns the comparison of the measure with the benchmark established in the prior stage of the analysis, as well as demonstrating that the measure derogates from that common regime by imposing a different treatment for economic operators that, in light of the objective assigned to the tax system of the Member State concerned, are in a comparable factual and legal situation.⁷ Third, even if it is selective, the measure can nonetheless be considered as being compatible with the internal market. Indeed, this stage calls for an inquiry into whether the measure is justified by the nature or the general scheme of the system and is thus ‘not selective in nature even though it gives an advantage to the undertakings which are able to benefit from it.’⁸

The so-called *de facto* selectivity constitutes a peculiar type of material selectivity. *De facto* selectivity characterizes measures that, despite being formally general, have selective effects. The CJEU first elaborated this notion in the *Gibraltar* case⁹, where the contested measure was a corporate tax reform that involved: company registration fee, payroll tax and business property occupation tax (the BPOT). Moreover, according to the so-called profit cap, undertakings had to pay due taxes only when achieving the minimum threshold of profits fixed at 15%. The CJEU considered the corporate tax system in itself to be *de facto* selective, since it was designed to give preferential treatment to the group of the beneficiary undertakings that, because of their nature, fulfilled the requirements (Aalbers, 2017). Hence, with the *Gibraltar* judgment, the Court of Justice definitely established the principle of the effect of the measure as the cornerstone of state aid assessments.

III. The CJEU case-law: the extension of the notion of selectivity and of limitations on Member States’ sovereignty

The selectivity requirement has been defined by the CJEU mostly in a series of cases concerning tax measures. The notion has an inherently fluid character, since it needs to adapt to new scenarios.

⁷ Ibidem.

⁸ Ibidem, para. 144.

⁹ Court of Justice, Judgment of 15 November 2011, Joined cases C-106/09 P and C-107/09 P, *European Commission (C-106/09 P) and Kingdom of Spain (C-107/09 P) v Government of Gibraltar and United Kingdom of Great Britain and Northern Ireland*.

Against this backdrop, the recent judgment in *European Commission v. World Duty Free*¹⁰ focused on the notion of selectivity and trying to establish its boundaries. The case fell under the scrutiny of the Court of Justice after the appeal of the *Autogrill*¹¹ and *Banco Santander*¹² judgment, decided by the General Court and subsequently joined. The measure brought to the attention of the General Court in *Autogrill* and *Banco Santander* was a Spanish provision that allowed undertakings taxable in Spain – in this case Banco Santander SA, Santusa Holding SL and Autogrill España – to deduct, in the form of an amortisation, the goodwill resulting from the acquisition of shareholdings in foreign companies from the basis of assessment for the corporate tax for which the undertaking is liable.¹³ These shareholdings had to reach at least 5% and they had to be held without interruption for at least one year.¹⁴ The Commission qualified the measure as State aid due to the fact that it was applicable exclusively to undertakings respecting the criteria provided (in particular, the acquisition of shareholdings in Spanish companies was not covered by this benefit).

The General Court annulled the decision of the Commission because of the lack of an evaluation of a specific element, namely the *ex ante* identification of a ‘category of undertakings which are exclusively favoured by the measure at issue’.¹⁵ Indeed, the General Court tried to introduce this new assessment in the original three-steps analysis, focusing on the evaluation of the discriminatory nature of the measure (Jaeger, 2015) and considering that ‘for the condition of selectivity to be satisfied [...] the mere finding that a derogation from the common or ‘normal’ tax regime has been provided for cannot give rise to selectivity’.¹⁶ In other words, the reasoning adopted by the General Court was that if a measure derogates from the reference framework but is open to all undertakings, it is not possible to compare the situation of the beneficiaries and those who are excluded by the field of the application of the measure (Staviczky, 2015). Moreover, the mere application of specific conditions for the granting of the measure – albeit unusual or difficult to be met by undertakings – does not mean that the selectivity requirement is fulfilled (Temple Lang, 2015). In general, scholars considered this approach

¹⁰ Court of Justice, Judgment of 21 December 2016, Joined cases C-20/15 P and C-21/15 P, *European Commission v World Duty Free Group SA and Others*.

¹¹ General Court, Judgment of 7 November 2014, Case T-219/10, *Autogrill España, SA v European Commission*.

¹² General Court, Judgment of 7 November 2014, Case T-399/11, *Banco Santander, SA and Santusa Holding, SL v European Commission*.

¹³ *Ibidem*, para. 14.

¹⁴ *Ibidem*.

¹⁵ *Ibidem*, para. 49.

¹⁶ *Ibidem*.

to be an improvement since it made it possible to overcome the formalistic distinction between beneficiaries and non-beneficiaries of an aid (Nicolaidis, 2015). Furthermore, the judgments seemed to be a good starting point for the CJEU to clarify the controversial notion of selectivity in fiscal aids, also with reference to the so-called selective advantage, by addressing, in particular, the tendency to combine the analysis of the selectivity and economic advantage criteria (Girau and Petit, 2015; Jaeger, 2015).

The cases were joined and submitted to the decision of the Court of Justice that, in accordance with AG Wathelet's Opinion,¹⁷ subverted the judgments of the General Court, which ruled the measure to be State aid. In particular, AG Wathelet stressed the excessively formalistic and restrictive approach of the General Court in seeking to identify a particular category of undertakings exclusively favoured by the measure, instead of giving room to the essential question, namely whether that measure differentiates between undertakings which are in a comparable situation.¹⁸ Moreover, the AG pointed out that 'the fact that the conditions imposed by the measure at issue were not very strict and the benefits which that measure conferred were therefore available to many undertakings does not call into question its selective nature but only its degree of selectivity'.¹⁹

The most interesting aspect of the *World Duty Free* judgment lies in the analysis of the selectivity requirement made in the light of the *Gibraltar* ruling, giving therefore a kind of 'authentic interpretation' of the latter. In particular, the Court of Justice stated that the introduction of a further assessment in the selectivity test – namely the *ex ante* identification of a specific category of undertakings – is not in line with settled case-law,²⁰ specifying further that it is not possible to derive this principle from the *Gibraltar* case. The Court of Justice pointed out that, as stated in *Gibraltar*, 'the selectivity of a tax measure can be established even if that measure does not constitute a derogation from an ordinary tax system, but is an integral part of that system'²¹ (that is, the so-called *de facto* selectivity) and it does not entail the *ex ante* identification of a specific category of undertakings since it is already consistent with settled case-law of the CJEU to the effect that 'it is sufficient, in order to establish the selectivity of a measure that derogates from an ordinary tax system, to demonstrate that that measure benefits certain operators and not others,

¹⁷ Opinion of Advocate General Wathelet delivered on 28 July 2016, Joined cases C-20/15 P and C-21/15 P, *European Commission v World Duty Free Group SA and Others*.

¹⁸ *Ibidem*, para. 85.

¹⁹ *Ibidem*, para. 88.

²⁰ *World Duty Free*, *cit.* para. 71.

²¹ *Ibidem*, para. 76.

although all those operators are in an objectively comparable situation in the light of the objective pursued by the ordinary tax system.²²

In sum, *World Duty Free* ends up extending the notion of selectivity, by narrowly construing *Autogrill* and *Banco Santander* where the General Court tried to move the evaluation of selectivity to *ex ante* instead of *ex post*. By contrast, in *World Duty Free*, the Court of Justice seems to consider selective measures as those that derogate from the reference framework and that entail a different treatment, regardless of the potential accessibility of the measure. According to some commentators, this approach could lead to a major extension of the notion of selectivity, which could have the effect of increasing the capacity of the Commission to interfere with national fiscal choices (Derenne, 2017). Moreover, this approach arguably turns the selectivity test into an irrelevant evaluation by shifting the focus of the assessment exclusively on the economic advantage granted by the measure.

IV. The Commission decision-making practice: the notion of selective advantage and the identification of the reference framework

Recent Commission decision-making practice had to face the issue of defining the selectivity requirement in dealing with tax rulings. Indeed, since 2013, the Commission has been investigating the tax ruling practice of Member States by setting up a dedicated Task Force Tax Planning Practices, in order to fight the so-called BEPS (base erosion and profit shifting). In December 2014, this inquiry was extended to all Member States and resulted in several decisions to initiate formal investigations. Until now, the Commission adopted five negative final decisions involving Luxembourg,²³ Ireland,²⁴ Belgium,²⁵ the Netherlands²⁶, and there are still four formal investigations ongoing involving

²² *Ibidem*.

²³ European Commission. Decision (EU) 2016/2326 of 21 October 2015 on State aid SA.38375 (2014/C ex 2014/NN) which Luxembourg granted to Fiat in JOCE L/351/2016 and European Commission. Decision (EU) of 04.10.2017 on state aid SA.38944 (2014/C) (ex 2014/NN) implemented by Luxembourg to Amazon, not published yet.

²⁴ European Commission. Decision (EU) 2017/1283 of 30 August 2016 on State aid SA.38373 (2014/C) (ex 2014/NN) (ex 2014/CP) implemented by Ireland to Apple in JOCE L/187/2017.

²⁵ European Commission. Decision (EU) 2016/1699 of 11 January 2016 on the excess profit exemption State aid scheme SA.37667 (2015/C) (ex 2015/NN) implemented by Belgium in JOCE L/260/2016.

²⁶ European Commission. Decision (EU) 2017/502 of 21 October 2015 on State aid SA.38374 (2014/C ex 2014/NN) implemented by the Netherlands to Starbucks in JOCE C/460/2014.

the Netherlands,²⁷ Luxembourg²⁸ and the UK.²⁹ The Commission ordered the recovery of the contested aids mostly on the ground of the conclusion that the advanced pricing agreements at stake, being at odd with the arm's length principle, were selective. The decisions are currently under the scrutiny of the General Court, after challenges brought by both the Member States and the taxpayers involved.³⁰

In order to have a better understanding of the issue of selectivity in relation to the aforementioned Commission decisions, it is necessary to briefly examine the tax ruling instrument as used by the Member States. Since the Treaties do not confer competences onto the EU in the field of direct taxation, Member States retain the power to design their tax system, albeit every fiscal measure must comply with EU law and, in particular, with its State aid rules.³¹ Therefore, Member States can adopt tax rulings, which are binding decisions issued by their tax authorities, at taxpayers' request, in order to find out how applicable domestic tax provisions will be applied to a specific case. Tax rulings are instruments of unarguable importance in providing legal certainty to undertakings;³² they help them foresee future costs that they will have to bear because of taxation of a certain situation or transaction.

A peculiar type of tax ruling is known as Advance Pricing Agreement (hereinafter; APA), which is an 'arrangement that determines, in advance of controlled transactions, an appropriate set of criteria (e.g. method, comparables and appropriate adjustments thereto, critical assumptions as to future events) for the determination of the transfer pricing for those transactions over a fixed

²⁷ European Commission, Decision of 18 December 2017 on alleged State aid SA.46470 (2017/NN in favour of Inter IKEA, not published yet.

²⁸ European Commission, Decision of 3 December 2015 on alleged State aid SA.38945 (2015/C) (ex 2015/NN) in favour of McDonald's in JOCE C/258/2016 and European Commission, Decision of 19 September 2016 on alleged State aid SA.44888 (2016/NN) (ex 2016/EO) in favour of GDF Suez in C/36/2017.

²⁹ European Commission, Decision of 26 October 2017 on alleged State aid SA.44896 (2017/C) (ex 2017/NN) regarding the UK tax scheme for multinationals (Controlled Foreign Company rules) in JOCE C/400/2017.

³⁰ For a list of cases related to tax ruling decisions, see: http://ec.europa.eu/competition/state_aid/tax_rulings/index_en.html (last accessed: 14 April 2018).

³¹ See Court of Justice, Judgment of 22 June 2006, Cases C-182/03 and C-217/03, *Kingdom of Belgium (C-182/03) and Forum 187 ASBL (C-217/03) v Commission of the European Communities*, par. 81; Court of Justice, Judgment of 29 March 2012, Case C-417/10, *Ministero dell'Economia e delle Finanze and Agenzia delle Entrate v 3M Italia SpA*, para. 25.

³² European Commission, DG Competition, *Internal Working Paper – Background to the High Level Forum on State Aid of 3 June 2016 ('Working Paper on State Aid and Tax Rulings')*, available at: http://ec.europa.eu/competition/state_aid/legislation/working_paper_tax_rulings.pdf (last accessed 14 April 2018), para. 5.

period of time'.³³ Unlike transactions between non-integrated companies (that is, companies which are not part of a group) that are assumed to be conducted under market conditions, intra-group transactions may be at odds with market terms, as they are estimated by the corporate group itself. Therefore, this system can lead to the manipulation of profit allocation in order to shift revenues to low tax countries. In order to avoid such a distortion, the OECD has formulated the so-called 'arm's length principle', which can be applied by means of five reliable methods that make it possible to calculate the correct transfer pricing for intra-group transactions.³⁴ The selection of the method is often ambiguous and complicated and it can lead to very different outcomes. Although the source of the arm's length principle is non-binding,³⁵ it is considered to be a globally recognized standard (Iliopoulos, 2017; Joris and De Cock, 2017).

APAs are considered practices that enhance taxation transparency and predictability as well as prevent double taxation. Therefore, they are not *per se* incompatible State aids, as long as they do not confer a selective economic advantage. The mere fact that the advantage granted derives from an agreement, and therefore a negotiation, between a company and the tax authorities of a Member State does not imply the selectivity of the measure. Indeed, it is necessary to prove that the tax ruling was issued on the ground of non-objective or custom-made criteria³⁶ (Iliopoulos, 2017). In order to make this evaluation, the Commission Notice on the Notion of State Aid³⁷ and the Working Paper on State Aid and Tax Ruling both recall the arm's length principle as allegedly endorsed by the Court of Justice in the case *Forum 187*,³⁸ where it was used to determine whether a fiscal measure prescribing a method for an integrated group company to determine its taxable profit gives rise to a selective advantage for the purpose of Article 107(1) TFEU.³⁹

³³ European Commission, *Communication from the Commission to the Council, the European Parliament and the European Economic and Social Committee on the work of the EU Joint Transfer Pricing Forum in the field of dispute avoidance and resolution procedures and on Guidelines for Advance Pricing Agreements within the EU*, COM/2007/0071 final, p. 9.

³⁴ OECD, *transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations*, 22 July 2010, available at: <http://www.oecd.org/publications/oecd-transfer-pricing-guidelines-for-multinational-enterprises-and-tax-administrations-20769717.htm> (last accessed 14 April 2018).

³⁵ The arm's length principle is defined in Article 9 of the OECD Model Tax Convention and it is further elaborated in the OECD Transfer Pricing Guidelines.

³⁶ Court of Justice, Judgment of 4 June 2015, Case C-15/14 P, *European Commission v MOL Magyar Olaj- és Gázipari Nyrt.*

³⁷ *Commission Notice on the notion of State aid*, *cit.*, par. 172.

³⁸ *Kingdom of Belgium and Forum 187 ASBL v. Commission*, *cit.*

³⁹ *Working Paper on State Aid and Tax Rulings*, *cit.*, para. 4.

The introduction of the arm's length principle in the evaluation of the selective advantage of fiscal measures gave rise to a number of criticisms. At first, it is necessary to remark that the *Forum 187* judgment does not make an explicit reference to the arm's length principle. Instead, the Court of Justice merely affirmed that in order to assess whether a fiscal scheme (in this case a Belgian tax regime for authorized coordination centers) was to be considered a derogation from the reference framework granting an economic advantage, it had to be compared with 'the ordinary tax system, based on the difference between profits and outgoings of an undertaking carrying on its activities in conditions of free competition'⁴⁰ (Joris and De Cock, 2017). Therefore, it has been noted that it is not straightforward to consider the arm's length principle as an implied corollary of the evaluation *ex Article 107 TFEU* 'independently of whether a Member State has incorporated this principle into its national legal system'⁴¹ solely on the ground of the reference made in the *Forum 187* judgment to the 'conditions of free competition'. Indeed, it is not possible to derive from that statement the notion of the arm's length principle, such as the one adopted by the Commission (Gormsen, 2016; Joris and De Cock, 2017; Kyriazis, 2016).

Another controversial issue is the fact that the introduction of such a vague concept could lead to legal uncertainty for companies, which is exactly the opposite of what APAs try to reach. Indeed, as seen above, the calculation of the correct transfer pricing according to the arm's length principle is a hard task since it depends on several factors. This exercise consists of assessing something that is purely formal since transfer prices are, because of their nature, exempt from market influences (Giraud and Petit, 2017).

Moreover, the arm's length principle is used for the identification of both the requirements of economic advantage as well as selectivity, merging them into the so-called 'selective advantage' test. More specifically, the Commission considers that if APAs lead to an unjustified reduction of the tax liability a companies; such a 'reduction constitutes both the advantage granted by the tax measure and the derogation from the system of reference'.⁴² On this matter, in the *Commission v. MOL* case,⁴³ the CJEU has recently highlighted the autonomy of the selectivity criterion stating that 'the requirement as to selectivity under Article 107(1) TFEU must be clearly distinguished from the concomitant detection of an economic advantage, in that, where the Commission has identified an advantage, understood in a broad sense, as

⁴⁰ *Kingdom of Belgium and Forum 187 ASBL v. Commission*, *cit.*, para. 95.

⁴¹ *Commission Notice on the notion of State aid*, *cit.*, para. 172.

⁴² See Decision on State aid implemented by the Netherlands to Starbucks, *cit.*, par. 253 and Decision on State aid which Luxembourg granted to Fiat, *cit.*, para. 217.

⁴³ *European Commission v MOL*, *cit.*

arising directly or indirectly from a particular measure, it is also required to establish that that advantage specifically benefits one or more undertakings'.⁴⁴ Nevertheless, in the subsequent paragraph, the Court of Justice specified that 'the selectivity requirement differs depending on whether the measure in question is envisaged as a general scheme of aid or as individual aid. In the latter case, the identification of the economic advantage is, in principle, sufficient to support the presumption that it is selective'.⁴⁵ However, it should be noted that this judgment does not entail the conflation of the two requirements; it merely establishes that, for individual aids, there is a rebuttable presumption of fulfillment of the selectivity requirement when the economic advantage is already assessed (Arena, 2017a; Kyriazis, 2016). Indeed, even if they share some similarities, these two requirements have a different function: whereas the economic advantage test requires a comparison between the advantage deriving from the measure and market terms, the selectivity test involves a comparison between the beneficiary's treatment and the treatment of other undertakings in a similar legal and factual situation (Joris and De Cock, 2017). Some scholars argued that the Commission approach toward this presumption could lead to a 'potentially dangerous development in EU State aid law' under many perspectives. First, economic advantage and selectivity are two separate conditions, and thus they require two separate analyses. Second, the arm's length principle is not 'well equipped' to assess whether the measure is selective, but only to assess the economic advantage (Joris and De Cock, 2017; Lovdhal Gormsen, 2016).

These arguments are not fully convincing. The use of 'selective advantage' in Commission practice is not a novelty and it traces back to its 1998 Direct Business Taxation Notice⁴⁶ (Arena, 2017b); there is also a trend in the case-law of the CJEU to treat these two criteria together (Joris and De Cock, 2017). Moreover, since APAs are usually individual aids, the issue of the conflated analysis of the two requirements is not relevant (Arena, 2017a; Douma and Kardachaki, 2016; Iliopoulos, 2017) since the presumption of selectivity, deriving from the assessment of the economic advantage, is in line with the CJEU case-law.⁴⁷ Therefore, the Commission seems to follow the way paved by the CJEU, without adding any further elements or widening its scope.

Major concerns derived also from another core aspect of the selectivity test: the identification of the reference framework. Indeed, this is a crucial element for the aforementioned three-steps analysis, because it is the benchmark

⁴⁴ Ibidem, para. 59.

⁴⁵ Ibidem, para. 60.

⁴⁶ European Commission, *Commission notice on the application of the State aid rules to measures relating to direct business taxation*, OJ C 384, 10.12.98, p. 3–9.

⁴⁷ Ibidem, para. 60.

against which the measure is compared to and, hence, it can strongly affect the outcome of the analysis. At first, it should be noted that APAs are theoretically possible for every group of companies, whilst non-integrated companies are excluded since they are not part of a group and therefore, by definition, they are not involved in transfer pricing issues. In recent Commission practice related to APAs, general corporate income tax was identified as the reference framework. However, identifying such a benchmark seems rather theoretical and illogical. Since corporate groups and non-integrated companies are clearly in a different legal and factual situation in relation to transfer pricing (the latter by definition do not need to face this issue), it would have been more reasonable to identify the reference framework in corporate tax rules applied to corporate groups, that is, in specific transfer pricing rules (Giraud and Petit, 2017; Verschuur and Stroung, 2017). Indeed, this narrower framework enabled some multinational companies to benefit from more lenient treatment in the evaluation of their transfer pricing as compared to other corporate groups that were in a similar legal and factual situation. This legal threshold would have been harder for the Commission to meet, but it would have led to the same result by following a line of reasoning that is more logical, concrete and coherent with State aid rules (Giraud and Petit, 2017).

V. Conclusions

The requirement of selectivity, as applied in the domain of State aid law and in relation to tax measures, is a complex notion. Indeed, assessing whether a tax benefit (that is, derogation from the normal tax system) can be seen as an expression of a Member State's discretionary power on fiscal policies, or if it falls within the scope of the application of Article 107(1) TFEU, is controversial. The definition of selectivity in fiscal aid involves politically sensitive issues, such as the allocation of powers between Member States and the EU in matters concerning direct taxation.

The analysis suggests that the extension of the notion of selectivity is a common trend shared by the CJEU and the Commission – as noted above, both tend to broaden the notion of selectivity. Indeed, on the one hand, the Court of Justice rejected the attempt of the General Court to limit the notion and, on the other hand, the Commission identified a broad benchmark as a reference framework, blurring the lines between selectivity and the existence of an advantage. Since selectivity is the most relevant criterion to be assessed in tax measures, an extensive interpretation will inevitably result in a limitation of national fiscal sovereignty in direct taxation by modifying the division of

powers between the EU and its Member States, while it is settled-case-law that direct taxation (which clearly includes corporate taxation) falls within the competences of Member States. In particular, Member States can design their corporate tax systems in a way they consider most appropriate and best suited to their economies (Verschuur and Stroungi, 2017; Joris and De Cock, 2017);⁴⁸ their discretion in this field is limited by their duty to ensure effective application of EU law and, hence, shall be exercised consistently with the latter⁴⁹ (Arena, 2017a; Azoulai, 2011; Iliopoulos, 2017). Limiting the analysis to these considerations – that are common ground among scholars – it does not seem that the EU is overreaching its powers within the scope of the application of Article 107(1) TFUE. However, there are some issues that cast some doubts upon the validity of such a strong interference of the EU into the tax sovereignty of its Member States.

The first concern that arises is whether there is a limit to the stretching of the notion of selectivity. Indeed, if there are no limits to the extension of this notion, the Commission would play the role of a ‘supra-national tax authority’, as the US Treasury claimed.⁵⁰ That would add further uncertainty, since undertakings will not be able to rely on national measures fearing a subsequent intervention by the Commission. Moreover, in tax ruling cases, the Commission relied on a notion – the arm’s length principle – that is not univocal. A clarification of the notion of the arm’s length principle, as adopted by the Commission, would be necessary in order to increase predictability; a specification of the legal basis on which this soft law concept is turned into hard law would also be necessary. Indeed, the reference made to the *Forum 187* judgment does not resolve the doubts arising from such a use of the arm’s length principle.

Secondly, over the years we have witnessed a convergent evolution, on one side, of the international soft law concept of harmful tax competition between Member States and, on the other side, of the notion of fiscal aid for the purpose of State aid control meant to fight unfair competition among undertakings (Traversa and Flamini, 2015). Nowadays State aid rules are openly used to tackle harmful tax competition, and its collateral phenomena

⁴⁸ *European Commission and Kingdom of Spain v Government of Gibraltar and United Kingdom of Great Britain and Northern Ireland*, *cit.*, para. 97.

⁴⁹ Court of Justice, Judgment of 19 June 2014, Joined Cases C-53/13 and C-80/13, *Strojírny Prostějov, a.s. and ACO Industries Tábor s.r.o. v Odvolací finanční ředitelství*, para 23 and Court of Justice, Judgment of 3 October 2006, Case C-290/04, *FKP Scorpio Konzertproduktionen GmbH v Finanzamt Hamburg-Eimsbüttel*, para 30.

⁵⁰ U.S. Department of the Treasury, White Paper of 24 August 2016 ‘*The European Commission’s Recent State Aid Investigation of Transfer Pricing Rulings*’, available at: <https://www.treasury.gov/resource-center/tax-policy/treaties/Documents/White-Paper-State-Aid.pdf> (last accessed: 14 April 2018), p. 9.

such as fiscal dumping, aggressive tax planning and international tax evasion and avoidance, but this specific aim has already been clear since 1998 when the Commission Notice on Direct Business Taxation⁵¹ was adopted (Jeager, 2017). State aid rules, although being a useful instrument to fight harmful tax competition, cannot (and should not) be used as a full substitute for the positive approximation of the corporate tax systems of EU Member States (Traversa and Flamini, 2015). Indeed, Commission decision-making practice seems to pursue the approximation of national corporate tax laws, even though it would be necessary to follow the procedure provided by Article 115 TFEU.⁵² The efforts of the EU in this field (that is, coordination of corporate tax systems) are clear, as demonstrated by the number of instruments proposed or adopted in this regard⁵³ (Cachia, 2017).

The impression is that these decisions, at least to some extent, pursue a political aim with a risk of a ‘backdoor’ tax harmonization (Stuart, 2016). All tax-ruling decisions are now under the scrutiny of the General Court, but the formulation of reliable predictions about their outcome would be extremely difficult. Nevertheless, it is certainly desirable for the CJEU to provide a clear and solid position towards the various issues previously pointed out, such as in relation to the identification of the correct reference framework, the assessment of the ‘selective advantage’, and the use of the arm’s length principle. Irrespective of the approach that the CJEU will choose to follow, its judgments will be a strong indicator of the actual allocation of powers between Member State and the EU in the area of direct taxation.

⁵¹ Commission notice on the application of the State aid rules to measures relating to direct business taxation, *cit.*

⁵² Article 115 TFEU provides that: ‘Without prejudice to Article 114, the Council shall, acting unanimously in accordance with a special legislative procedure and after consulting the European Parliament and the Economic and Social Committee, issue directives for the approximation of such laws, regulations or administrative provisions of the Member States as directly affect the establishment or functioning of the internal market.’

⁵³ See, for example: European Commission, *A Fair and Efficient Corporate Tax System in the European Union: 5 Key Areas for Action*, 17 June 2015, COM(2015) 302 final; Council Directive 2014/86/EU of 8 July 2014 amending Directive 2011/96/EU on the common system of taxation applicable in the case of parent companies and subsidiaries of different Member States, 25.7.2014, OJ L 219, p. 40–41; Council Directive (EU) 2015/121 of 27 January 2015 amending Directive 2011/96/EU on the common system of taxation applicable in the case of parent companies and subsidiaries of different Member States, 28.01.2015, OJ L 21, p. 1–3; Tax Transparency Package, 18 March 2015, see https://ec.europa.eu/taxation_customs/business/company-tax/tax-transparency-package_en (last accessed 14 April 2018); European Commission, Proposal for a Council Directive laying down rules against tax avoidance practices that directly affect the functioning of the internal market, 28.01.2016, COM(2016) 26 final.

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