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EUROPEAN STATE AID:
THE MAKINGS OF A GLOBAL TRADE WAR

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A YEAR IN REVIEW

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E.U. STATE AID – THE SAGA CONTINUES

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The drama continues with the E.U. State Aid[1] investigations by the European Commission for Competition (the "Commission"). In the past month, the competition commissioner, Margrethe Vestager, met with Luxembourg officials to discuss the outcome of the Amazon investigation, and the Commission ordered Fiat Chrysler Automobiles to pay about €30 million in back taxes to Luxembourg and released a public letter regarding the investigation of McDonald's alleged State Aid violations in Luxembourg. An even more bold attack on multinational tax practices came not from the Commission but from the French authorities, who raided the offices of Google and McDonald's in May.

As the Commission's probe expands, E.U. Member States are increasingly expressing objections to being forced to recoup back taxes from multinational enterprises ("M.N.E.'s") that allegedly received illegal State Aid. States, including the United States, question whether the Commission is acting beyond its authority and impeding Member States' sovereignty to directly tax persons within their jurisdictions.

The European Parliament has even formed a special tax committee to investigate the Commission's role, as well as Member States' roles, in failing to enforce laws that would have prevented entities and individuals from sheltering money in offshore havens to avoid paying taxes.[2] Although the Commission itself will be a subject of these investigations, a Commission spokesperson applauded the creation of a special tax committee to assist in combatting harmful tax practices.

The Commission has argued that it is acting within the authority granted by E.U. law and that it has not infringed on the jurisdiction of Member States, the U.S., or any other country. Since 2013, the Commission has been investigating various Member States' individual tax rulings with U.S. companies, including Starbucks in the Netherlands,[3] Apple in Ireland, Google in the U.K., Amazon in Luxembourg, and McDonald's in Luxembourg. The Commission has alleged that these companies' tax arrangements with different Member States amount to unjustifiable State Aid in violation of E.U. anti-competition laws. If the Commission determines that a Member State provided a selective tax advantage, and thus illegal State Aid, to an entity, the Member State is forced to retroactively, not prospectively, recoup taxes from the

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1 For the definition of E.U. State Aid see Beate Erwin and Christine Long, "Apple in Europe – The Uphill Battle Continues," *Insights* 2 (2016), pp. 9-15; and Beate Erwin, "Tax Rulings in the European Union – State Aid as the European Commission's Sword Leading to Transparency on Rulings," Insights 6 (2015), pp. 13-14.

2 Joe Kirwin, "EU Parliament to Probe Intermediaries, Members on Havens," *BNA International Tax Monitor*, June 2, 2016.

3 Although the Commission's ruling was issued In October 2015, the text of its decision was first released in late June 2016.

entity over a ten-year period. Enforcement of this requirement to recoup back taxes is arguably beyond the Commission's regulatory power.

LATEST ON U.S. REACTIONS

The U.S. reaction to the Commission's State Aid investigations has also intensified. Several U.S. senators and Treasury Department officials continue to express concern and frustration with the Commission's probe into U.S. M.N.E.'s, arguing that the Commission has overstepped its bounds, as the retroactive imposition of tax "is improper and plainly undermines legal certainty and the rule of law."[4] In a May 23 letter to the Treasury Department, Senators Hatch, Wyden, Portman, and Schumer contended that the Commission "appears to be ignoring the national practice and law of its Member States and to be imposing its own new standard for transfer pricing determinations."[5] Furthermore, the Commission's actions confirm "our suspicion that these cases are about more than objectively enforcing existing competition policies."[6] The targeting of U.S. enterprises could potentially undermine U.S. rights in bilateral tax treaties with Member States and the retroactive payment for back taxes would likely prevent a U.S. M.N.E. from receiving a tax credit towards its U.S. income.

U.S. officials have been asserting that Commissioner Vestager is unfairly targeting U.S. M.N.E.'s and that the Commission has no right to claim the offshore profits of U.S. companies. Commissioner Vestager has repeatedly rejected such criticism, claiming that potential State Aid violations involving several non-U.S. companies are currently being examined. U.S. senators have been encouraging the U.S. Treasury Department to strike back by increasing taxes on European companies through enforcement of Internal Revenue Code (the "Code") §891.[7] Code §891 was implemented in U.S. tax law in1938, but it has never been invoked.[8] Under this rule, the tax rates for foreign citizens and corporations could be doubled in "retaliation" against unfair treatment of U.S. persons by these countries.

IS THE COMMISSION EXCEEDING ITS AUTHORITY?

In addition to the U.S., an increasing number of E.U. Member States are concerned that the Commission is overstepping its bounds by retroactively, rather than prospectively, imposing Member State taxation of M.N.E. earnings, particularly those of U.S. entities. Many states argue that the Commission is using the State Aid investigations as a disguise to impede on Member States' taxing power. Therein lies the difficulty with the E.U. system – balancing the right of Member States to directly tax, with the right of the Commission to protect the E.U. single market from anti-competitive tax practices.

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4 "Hatch, Wyden: EU State Aid Probe Violates Rule of Law," *BNA Daily Tax Report*, May 24, 2016.

5 Letter to Secretary Jacob Lew, U.S. Senate Committee on Finance, May 23, 2016.

6 *Id.*

7 Erwin and Long, "Apple in Europe," pp. 9-15.

8 It appears that this rule was intended rather as a tool in treaty negotiations to achieve reciprocal concessions than a weapon for unilateral use.

The Commission has since argued that it is acting within its authority. As if to justify this position, in May the Commission released "Commission Notice on the Notion of State Aid as Referred to in Article 107(1) TFEU" (the "Notice").[9] The Notice should provide guidance to clarify the definition of State Aid.

The Notice is allegedly a reaction to pleas made by the Netherlands in its appeal of the Starbucks outcome. The Netherlands has argued that the arm's length principle is not covered by E.U. law and, thus, could not be subject to State Aid infringement proceedings. To better understand the context of the Notice, the Commission's investigation of Starbucks's arrangement in the Netherlands is outlined below.

The Starbucks Case

In 2008, the Netherlands issued a tax ruling for Starbucks, approving the company's transfer pricing methods. The Commission alleged that the Dutch transfer pricing ruling provided a selective advantage to Starbucks in violation of E.U. anti-trust laws and began investigating the case in 2013. In October 2015, the Commission issued a final decision, finding that Starbucks received illegal State Aid because the Dutch transfer pricing ruling artificially lowered the company's tax burden in the Netherlands, thereby distorting competition. As a result, the Commission has ordered the Netherlands to recoup between €20 and €30 million in back taxes from Starbucks.[10]

The Dutch Finance Ministry appealed the Commission's decision in December 2015 and argued that Starbucks did not benefit from illegal State Aid. The Dutch appeal included five "pleas in law," alleging:

(A) Incorrect application of Article 107(1) TFEU to the extent that the European Commission finds that the transfer pricing ruling (specifically, an APA) is selective in nature, as the Commission referenced the wrong Dutch tax legislation and failed to demonstrate that the selectivity criterion was fulfilled;

(B) Incorrect application of Article 107(1) TFEU in relation to the European Commission's assessment of the existence of an advantage by reference to the arm's length principle under EU law, as no arm's length principle exists under E.U. law and is not part of the EU State aid assessment;

(C) Incorrect application of Article 107(1) TFEU in relation to the European Commission's finding that the transfer pricing ruling confers an advantage on Starbucks due to the selection of the 'Transactional Net Margin Method' to establish pricing;

(D) Incorrect application of Article 107(1) TFEU in relation to the European Commission's statement that the transfer pricing ruling confers an advantage on Starbucks as a result of the manner under which the 'Transactional Net Margin Method' was applied; and

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9 European Commission, "Commission Notice on the Notion of State Aid as Referred to in Article 107(1) TFEU," (Brussels: 2016)

10 "European Commission Reclarifies the Scope of EU State Aid Rules," *Checkpoint International Taxes Weekly* 21 (2016).

(E) Breach of the duty to exercise due care in so far as the European Commission did not assess and include all the relevant information in the decision and also uses as a basis anonymous information, or at least information that has never been shared with the Netherlands government.[11]

The pleas articulated by the Netherlands reflect the positions of other Member States, which argue that, through State Aid decisions, the Commission is acting beyond its capacity and forcing Member States to retroactively impose tax on multinationals. In particular, the fact that pricing methods and the arm's length principle are not doctrines of E.U. law puts them beyond on the scope of the Commission's assessment.

"The Notice is allegedly a reaction to pleas made by the Netherlands in its appeal of the Starbucks outcome."

The Commission Notice on the Notion of State Aid

The Commission published general guidance on all aspects of the definition of State Aid as part of the Notice, which comes under the State Aid Modernisation initiative that was launched in 2012.[12] The Notice clarifies the scope of the State Aid rules, and its stated purpose is to "provide legal certainty and cut red tape for public authorities and companies, and focus the Commission's resources on enforcing State aid rules in cases with the biggest impact on the Single Market."[13] As previously mentioned, the Notice is alleged to have been published in reaction to the Dutch appeal of the Commission's decision in the Starbucks case.

The Notice simplifies the interpretation of T.F.E.U. Article 107(1), as established by the E.U. Court of Justice and the General Court. The Notice explains the Commission's decision-making practice and how the Commission construes the notion of State Aid when issues have not yet been interpreted by the courts.[14] The Notice elaborates on the following fundamental notions of State Aid:

- The presence of a State Aid undertaking with respect to economic activity
- The imputability of a state measure to the Member State in question
- The notion of advantage and financing through State resources
- The selectivity, *i.e.*, selective advantage of the state measure
- The effect of a state measure on trade and competition between Member States[15]

To date, the Commission's State Aid investigations have focused on tax rulings granted by Member States to M.N.E.'s. However, the Commission is expected to expand its State Aid investigations to tax settlements. This adds to the uncertainty taxpayers face when operating within an E.U. Member State.[16]

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11 *Id.*

12 European Commission, "State Aid: Commission Clarifies Scope of E.U. State Aid Rules to Facilitate Public Investment," press release, May 19, 2016.

13 *Id.*

14 "Commission Notice on the Notion of State Aid."

15 *Id.*; "European Commission Reclarifies the Scope of EU State Aid Rules."

16 Ali Qassim, "Uncertainty Ahead: Tax Settlements Seen as Next EU State Aid

Authority of Tax Rulings

A Member State's grant of a tax ruling to a company must respect the State Aid rules. Tax rulings, such as A.P.A.'s or comfort letters, enable Member States to provide taxpayers with legal certainty and predictability on the application of a Member State's general tax rules. The Notice points out that a Member State's tax rulings are best ensured if its administrative ruling practice is transparent and the rulings are published. The Notice reiterates that the Commission has authority where a tax ruling may confer a selective advantage upon a company, in so far as that selective treatment results in a lowering of that company's tax liability in the Member State as compared to companies in a similar factual and legal situation.[17]

The Notice refers to the Court of Justice's rulings as support for the Commission's rationale for investigating individual rulings issued by Member States. The Court of Justice's rulings on transfer pricing cases have held that a Member State's 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 Notice elaborates on the phrase "reliable approximation of a market-based outcome," interpreting it to mean 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.[18]

"If a transfer pricing arrangement complies with the provisions of the O.E.C.D. Transfer Pricing Guidelines . . . a tax ruling endorsing that arrangement is unlikely to give rise to State Aid."

According to the Notice, this arm's length principle necessarily forms part of the Commission's assessment of tax measures granted to group companies under T.F.E.U. Article 107(1), independent of whether a Member State has incorporated this principle into its national legal system and, if so, in what form. A tax ruling that approves of a methodology that produces a reliable approximation of a market-based outcome, ensures that that company is not treated favorably under the ordinary rules of corporate taxation of profits in the Member State as compared to standalone companies that are taxed on accounting profit. The arm's length principle the Commission applies in assessing transfer pricing rulings under the State Aid rules is therefore an application of T.F.E.U. Article 107(1), which prohibits unequal treatment in taxation of undertakings in a similar factual and legal situation. This principle binds the Member States, and the national tax rules are not excluded from its scope.[19]

The Notice explains that, when the Commission examines whether a transfer pricing ruling complies with the arm's length principle inherent in T.F.E.U. Article 107(1), the Commission may refer to the guidance provided by the O.E.C.D., in particular the "O.E.C.D. Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations" (the "O.E.C.D. Transfer Pricing Guidelines"). Those guidelines do not deal with matters of State Aid per se, but they capture the international consensus on transfer pricing. The guidelines also direct tax administrations and M.N.E.'s on how to ensure that a transfer pricing methodology produces an outcome in line with market conditions. Consequently, if a transfer pricing arrangement complies with

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Inquiry Target," *Checkpoint International Tax Monitor*, June 7, 2016.

17 "Commission Notice on the Notion of State Aid," p. 50.

18 *Id.*, p. 51.

19 *Id.*, pp. 51-52.

the provisions of the O.E.C.D. Transfer Pricing Guidelines, including guidance on selecting the most appropriate method that leads to a reliable approximation of a market-based outcome, a tax ruling endorsing that arrangement is unlikely to give rise to State Aid.[20]

The Notice summarizes that, in particular, a tax ruling confers a selective advantage on an entity where

- the ruling misapplies national tax law, and this results in a lower amount of tax;
- the ruling is not available to undertakings in a similar legal and factual situation;[21] or
- the Member State's administration applies a more favorable tax treatment compared with other taxpayers in a similar factual and legal situation.[22]

The Notice's clarification of a selective advantage supports the Commission's argument that it has legal authority to enforce the State Aid decisions. The bulk of the Commission's State Aid investigations have been on transfer pricing rulings, with a focus on the arm's length principle. Although the arm's length principle may not be codified under E.U. law, it is established in the O.E.C.D. Transfer Pricing Guidelines, which have been adopted by the Member States. The Commission has already decreed that the Starbucks's transfer pricing ruling from the Netherlands amounted to unlawful State Aid, but the Commission is still investigating transfer pricing rulings between Ireland and Apple, Luxembourg and Amazon, and Luxembourg and McDonald's.

Authority of Tax Settlements

The Notice also justifies the Commission's authority to investigate tax settlements between Member States and taxpaying entities, by clarifying the scope of these settlements under E.U. law. Tax settlements have yet to be the subject of State Aid investigations, but the Notice's explanation of how tax settlements provide a selective advantage establishes grounds for future Commission investigations.

The Notice defines tax settlements as a common practice in many Member States that generally occurs in the context of disputes between taxpayers and the tax authorities concerning the amount of tax owed. Tax settlements allow tax authorities to avoid long-standing disputes before the domestic courts and ensure quick recovery

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20 *Id.*, p. 52.

21 The Notice provides, as an example, that this would be the case if some undertakings involved in transactions with controlled entities are not allowed to request tax rulings, contrary to a pre-defined category of undertakings.

22 For instance, this will be the case where the tax authority accepts a transfer pricing arrangement that is not at arm's-length, because the methodology endorsed by that ruling produces an outcome that departs from a reliable approximation of a market-based outcome (as in the Starbucks decision). The same applies if the ruling allows the taxpaying entity to use alternative, more indirect methods for calculating taxable profits (*e.g.*, the use of fixed margins for a cost-plus or resale-minus method for determining an appropriate transfer pricing, while more direct ones are available). ("Commission Notice on the Notion of State Aid," p. 54.)

of the tax due. While the competence of Member States in this field is not in dispute, State Aid may be involved in the conclusion of a tax settlement. In particular, it may arise where the amount of tax appears to have been reduced without clear justification (such as optimizing the recovery of debt) or in a manner that is disproportionately beneficial to the taxpayer.[23]

"As the Commission's State Aid investigations into tax rulings become more robust, it is only a matter of time before the investigations extend to tax settlements."

The Notice explains that a transaction between a Member State's tax administration and a taxpayer may, in particular, entail a selective advantage in the following situations:

> (a) in making disproportionate concessions to a taxpayer, the [Member State's] administration applies a more 'favourable' discretionary tax treatment compared to other taxpayers in a similar factual and legal situation;
>
> (b) the settlement is contrary to the applicable tax provisions and has resulted in a lower amount of tax, outside a reasonable range. This might be the case, for example, where established facts should have led to a different assessment of the tax on the basis of the applicable provisions (but the amount of tax due has been unlawfully reduced).[24]

The Commission is expected to start investigating tax settlements between Member States and multinational taxpayers. For example, many thought the multimillion-pound tax settlement between the U.K. and Google should have been several billion pounds instead. Such tax settlements could be construed as sweetheart tax deals that provide favorable treatment, and thus unlawful State Aid, to multinational taxpayers.[25] The Notice lays out the legal authority for the Commission to examine such settlements. As the Commission's State Aid investigations into tax rulings become more robust, it is only a matter of time before the investigations extend to tax settlements.

OBSERVATIONS FROM A U.S. PERSPECTIVE

The Commission's State Aid decisions raise various complex issues with significant importance to U.S. companies currently or potentially under investigation.

E.U. Law Superseding Income Tax Treaties with Non-E.U. Countries

Within the E.U., E.U. law supersedes the domestic laws of the Member States. If the Commission finds that a Member State provided a taxpayer with illegal State Aid, that state must act without delay to recover that aid from the taxpayer.[26] Generally, rules on State Aid therefore trump bilateral income tax treaties. From a U.S. legal perspective, the T.F.E.U. and State Aid-related rules are not, and cannot, be granted this quasi-constitutional status.

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23 *Id.*, p. 53.

24 *Id.*, p. 55.

25 Ali Qassim, "Uncertainty Ahead."

26 "Council Regulation (EC) No 659/1999 of 22 March 1999 laying down detailed rules for the application of Article 93 of the EC Treaty," *Official Journal of the European Communities* L 083 (1999), art. 14, para. 3.

U.S. Foreign Tax Credit on State Aid Assessment Payments – Timing

Under U.S. Federal income tax law, a foreign tax credit is subject to the condition that all legal remedies, including appeals, have been exhausted.[27] Consequently, a foreign tax credit, if deemed applicable in this context,[28] may not be available under U.S. tax rules as long as the appeals procedures are pending. Another interesting aspect is that, upon an appeal of the Commission's State Aid decision, the courts may only accept or reject the Commission's decision in its entirety. If the decision is accepted, the courts are not entitled to decide on adjustments of the amount of State Aid that must be recovered by the Member State.

A New Arm's Length Standard Introduced by the Commission

In the Commission's decisions on Belgian tax rulings and the Luxembourg Fiat case, it made a notable statement, which based on the Netherland's reaction, also appears in the Starbucks decision:

> The arm's length principle therefore necessarily forms part of the Commission's assessment under Article 107(1) of the TFEU of tax measures granted to group companies, independently of whether a Member State has incorporated this principle into its national legal system. It is used to establish whether the taxable profits of a group company for corporate income tax purposes has been determined on the basis of a methodology that approximates market conditions, so that that company is not treated favourably under the general corporate income tax system as compared to non-integrated companies whose taxable profit is determined by the market.[29] *Thus, for any avoidance of doubt, the arm's length principle that the Commission applies in its State aid assessment is not that derived from Article 9 of the OECD Model Tax Convention, which is a non-binding instrument, but is a general principle of equal treatment in taxation falling within the application of Article 107(1) of the TFEU, which binds the Member States and from whose scope the national tax rules are not excluded.*[30] [emphasis added]

Does this mean the European Commission introduces a new arm's length standard? If so, how would it deviate from the standard found in the O.E.C.D. Model Convention and O.E.C.D. Tranfer Pricing Guidelines? Does the T.F.E.U. provide authority for the Commission on Competition – previously a non-tax focused body – to set forth an arm's length standard for transfer pricing (*i.e.*, tax purposes)? According to

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27 Treas. Reg. §1.901-2(e)(5).

28 Note that it is still unclear whether assessment payments under State Aid procedures should qualify as creditable tax payments for U.S. foreign tax credit purposes or as (non-creditable) damages.

29 The same language appears in Commission Decision no. SA.37667 (*Belgium*), para. 150 (January 1201, 16), except that it refers to the O.E.C.D. Transfer Pricing Guidelines in addition to Article 9 of the O.E.C.D. Model Convention.

30 "See Joined Cases C-182/03 and C-217/03, *Belgium and Forum 187 v. Commission*, ASBL ECLI:EU:C:2006:416, paragraph 81. See also Case T-538/11 *Belgium v. Commission* EU:T:2015:188, paragraphs 65 and 66 and the case-law cited." (Commission Decision no. SA.38375 (*Luxembourg Fiat*), para. 228 (October 21, 2015))

the view held by the Netherlands in its appeal, this is definitely not the case. That the Notice includes clarifications in this respect is unlikely to provide sufficient legal basis and thus change the Dutch view. The constraints that the State Aid decisions put on the taxing authority of the Member States have already been pointed out. With these State Aid decisions, this would rise to another – international – level, in particular in view of dismantling competent authority procedures with non-E.U. countries.

"The only certainty for M.N.E.'s operating in the E.U. is that there is uncertainty in the outcome of any tax ruling or tax settlement that these entities may have with Member States."

CONCLUSION

The Commission has great latitude in investigating all aspects of State Aid, including when a Member State provides an individual tax ruling or tax settlement to a multinational taxpayer. As the Commission's State Aid probe expands, more Member States are taking the position that the Commission is impeding domestic sovereignty and acting beyond the scope of E.U. law. The tension is growing between protecting the right of a Member State to directly tax its constituents and the Commission's mandate to protect the E.U. single market from anti-competitive tax practices. From a U.S. legal perspective, the impact of the State Aid decisions is far reaching – timing of foreign tax credits, if applicable at all; dismantling of income tax treaties; and a new arm's length standard are just some examples. The only *certainty* for M.N.E.'s operating in the E.U. is that there is *uncertainty* in the outcome of any tax ruling or tax settlement that these entities may have with Member States.

TREASURY ATTACKS EUROPEAN COMMISSION ON STATE AID – WHAT NEXT?

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On August 30, 2016, the European Commission ("the Commission") ordered Ireland to claw back €13 billion ($14.5 billion) plus interest from Apple after favorable Irish tax rulings were deemed to be illegal State Aid by the Commission. Not only did the Commission issue this decision, but at the same time, it invited other nations to consider whether profits that flowed through Apple's nonresident Irish branch should instead be taxed in their respective jurisdictions.[1]

This interpretation was shared by O.E.C.D. Secretary-General Angel Gurria,[2] and France may follow suit. In a statement on September 9, 2016, French Finance Minister Michel Sapin called the decision against Apple "completely legitimate," but left it open as to whether France would assess back tax on the company.[3]

The offices of Google and McDonald's in France were raided by French authorities in May of this year. In Italy, Apple paid €318 million in a settlement of a ruling by the Italian tax authorities that the company had improperly booked €880 million in profits to an Irish subsidiary from 2008 to 2013. Apple is also believed to be the subject of investigations by Spanish tax authorities.[4]

European Tax Commissioner Pierre Moscovici defended the European Union's Apple ruling as neither "anti-U.S." nor "arbitrary." Upon his arrival in Slovakia for the Economic and Financial Affairs Council ("E.C.O.F.I.N.") meeting at the beginning of September, the commissioner told reporters that the ruling "is based on facts and data which apply to all companies wherever they come from, and especially from European Union countries." On another occasion, Competition Commissioner Vestager pointed out that BP Plc was forced to pay additional taxes, but was reluctant to comment on the investigation into IKEA.[5] Wherever one's the stance on

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1 In particular, two comments by E.U. Competition Commissioner Margrethe Vestager were noted: The first was that "the money belongs to Ireland," and the second was that "anybody who thinks they have a claim, bring the claim forward and tell us why you think you have a claim."

2 Secretary-General Gurria made the comment in response to a question posed during a September 10 news conference held at the conclusion of a two-day meeting of European Union finance ministers in Bratislava.

3 Notably, France has already had internet multinationals on its radar. In 2013, Amazon revealed that it was contesting a French assessment of $252 million in back taxes. In May of this year, the Paris offices of Google were raided by French officials in the course of a probe into whether Google's Irish unit has a permanent establishment in France.

4 Neither Apple nor representatives of the Spanish tax authorities confirmed the existence of a Spanish investigation.

5 Investigations were initiated by the Swedish Green Party, which provided information to the European Commission.

the U.S.-European debate, it is indisputable that, with limited exception,[6] the most recent tax-related State Aid cases ruled upon by the Commission have focused exclusively on U.S. multinationals' European operations.

THE APPLE CASE: BACKGROUND AND FURTHER DEVELOPMENTS

On June 11, 2014, the European Commission initiated an investigation into advance pricing arrangements provided by the Irish tax authorities to Apple, regarding the attribution of profits to an Irish branch of an Irish company that, under Irish law, was treated as nonresident. The company was not managed and controlled in Ireland. According to the E.U., Apple Sales International allocated the vast majority of its profits to a "head office" that, in the European Commission's opinion, was an entity without economic substance. Apple's tax plan reduced its taxable income considerably. The European Commission's view was that these Irish arrangements with Apple constituted State Aid.

"In an unprecedented procedure, the U.S. Treasury Department released a white paper shortly before the European Commission's Apple decision was issued."

Both Apple and Ireland[7] confirmed that they will appeal the European Commission's decision. It may take years until the case is settled and may ultimately be decided by the European Court of Justice ("E.C.J."). Interestingly, the E.C.J. can merit the Commission's decision or reject it in its entirety, but it cannot revise the amount of the claw-back. It should also be noted that an appeal does not affect the obligation to pay the claw-back amount stipulated in the Commission's decision.[8] To date, the European Commission has initiated State Aid investigations against Apple, Amazon, Starbucks, and Fiat (now Fiat Chrysler Automobiles). Appeals against the Commission's decisions in the Starbucks and Fiat cases are already pending at the European General Court.[9] The Commission has not yet reached a final decision in the Amazon case.

As has been previously noted, the fairness of the European Commission's examination of U.S. multinationals has been questioned. Robert Stack, Deputy Assistant Secretary for International Tax Affairs at the U.S. Treasury Department, believes that American companies are being unfairly targeted in the investigations.

In an unprecedented procedure, the U.S. Treasury Department released a white paper[10] ("White Paper") shortly before the European Commission's Apple decision was issued. It expressed profound concern with the European Commission's

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6 One case was directed at the Belgian excess profit scheme and not at a particular company. Another case is being pursued against French utility company Engie SA, formerly GDF Suez.

7 On September 7, 2016, Irish Finance Minister Michael Noonan issued a statement to the House of Representatives (*Dáil Éireann*), seeking support to appeal the European Commission's decision that tax rulings issued by Ireland to Apple in 1991 and 2007 constituted illegal State Aid. On the same date, the Irish Department of Finance issued an explanatory memorandum for Parliament detailing House support of the Irish government's plans to appeal the decision.

8 The amount may be held in escrow until the final decision.

9 Prior to the Lisbon Treaty becoming effective on December 9, 2009, known as Court of First Instance.

10 U.S. Department of the Treasury, "The European Commission's Recent State Aid Investigations of Transfer Pricing Rulings," August 24, 2016.

investigations. The White Paper focused on three points:

- The investigations departed from prior E.U. case law and decisions.
- Retroactive recoveries through the investigation process is inappropriate.
- The European Commission's approach is inconsistent with O.E.C.D. transfer pricing guidelines.

The U.S. Treasury Department believes that the European Commission's investigations undermine the development of transfer pricing norms, the B.E.P.S. Project, and the ability of countries to honor their bilateral tax treaties with the U.S. It additionally notes that any repayment ordered by the European Commission will be entitled to a foreign tax credit in the U.S., thereby reducing U.S. tax liability and effectively transferring tax revenue from the U.S. to the E.U. Finally, the U.S. Treasury Department believes that the investigations will freeze cross-border investment between the E.U. and the U.S. and that retroactive penalties will hinder the ability for companies to plan for the future.

TREASURY'S ANALYSIS OF STATE AID AND THE EUROPEAN COMMISSION INVESTIGATIONS

State Aid exists when a national measure is financed by the state or through state resources in a way that (i) provides an advantage for a business undertaking, (ii) is selective in its application, and (iii) as a result, affects trade between member states by distorting competition.[11] The White Paper focuses primarily on the selectivity and business advantage elements of the definition.

"Advantage" was defined in prior case law to mean "any economic benefit which an undertaking could not have obtained under normal market conditions." For an advantage to be found, it had to be granted in a "selective way to certain undertakings of categories or to certain economic sectors."[12] According to the White Paper, once an advantage has been found, an analysis must be performed to determine whether the advantage is "selective." To be selective, a measure must provide a benefit to certain undertakings in comparison with other comparable undertakings.[13]

The White Paper concludes that prior European Commission rulings stated that measures available to companies with foreign affiliates but not available to domestic companies without foreign affiliates did not constitute "selective measures." Based on these prior rulings, a U.S. multinational would reasonably assume that a transfer pricing ruling granted in good faith by an E.U. Member State would not constitute a "selective measure" simply because a multinational has foreign affiliates whereas a

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11 *Air Liquide Industries Belgium SA v. Ville de Seraing a.o.*, Joined Cases C-393/04 & C-41/05, ECLI:EU:C:2006:403, ¶28. See also "Tax Rulings in the European Union – State Aid as the European Commission's Sword Leading to Transparency on Rulings," *Insights* 6 (2015).

12 Commission Notice on the notion of state aid as referred to in Article 107(1) of the TFEU, 2016 O.J. C 262/1, ¶¶5, 66 and 117.

13 *Portugal v. Commission*, Case C-88/03, ECLI:EU:C:2006:511, ¶54 (citing, among others, *Adria-Wien Pipeline*, Case C-143/99, ECLI:EU:C:2001:598, ¶41).

standalone European company has no affiliates.[14]

The White Paper notes that the European Commission previously separated its advantage analysis from its selective analysis in 65 prior cases. Now, however, in cases involving U.S.-based multinationals, the European Commission has merged the concepts of advantage and selectivity to conclude that a transfer pricing ruling is a selective advantage for a company that is part of a multinational group. According to the U.S. Treasury, the European Commission expanded protection of local companies because "selectivity" was often the largest barrier to finding the existence of a State Aid violation.

Observation

On this point, the U.S. Treasury Department is in line with the applicants in their appeal against the Commission's decisions in Starbucks and Fiat, focusing on the Commission's assessment of the two key State Aid conditions, *i.e.* advantage and selectivity. The Commission's new approach of collapsing the advantage and selectivity requirements has important substantive significance. Now, the Commission can find advantage if it disagrees with the Member State's application of the arm's length principle to a particular set of facts that are often highly complicated. The Commission's new approach reduces a State Aid inquiry to the question of whether the Commission believes that a transfer pricing ruling satisfies its view of the arm's length principle.[15]

RETROACTIVE RECOVERY

For a violation of State Aid regulations, the European Commission may require recovery for up to 10 years, with interest accruing for the period that the illegal aid was granted until the aid is recovered. According to the White Paper, U.S. multinational groups could not have foreseen the European Commission's new approach. Consequently, the recovery amount is a retroactive penalty.

In effect, because the transfer pricing was held to be valid in certain countries and due to the fact that the European Commission had tacitly accepted such arrangements for a long period, multinationals could not know that they would be considered to be infringing E.U. law. The U.S. Treasury Department notes that such a retroactive penalty is a fundamental violation of the principles stated by the G-20, the E.U., and the B.E.P.S. Project, which provide certainty to taxpayers while respecting each country's domestic transfer pricing agreements.

Finally, while the European Commission rulings make reference to an "arm's length principle," the U.S. Treasury Department notes that such a term remains undefined in the rulings. The White Paper implies what most U.S. tax advisers believe: that the

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[14] Treatment by the Netherlands tax authorities of a technolease agreement between Philips and Rabobank, Commission Decision 2000/735/EC, 2000 O.J. L 297/13, ¶36

[15] In a summary of its claims, Fiat stated:

> The contested decision breaches the principle of legal certainty since the commission's novel formulation of the arm's length principle introduces complete uncertainty and confusion as to when an advance pricing agreement, and indeed any transfer pricing analysis, might breach EU state aid rules.

investigations are politically motivated to punish E.U. countries with low tax rates or favorable practices, and multinationals that plan structures using those jurisdictions.

Observation

The introduction of a new arm's length standard by the European Commission has been previously noted in *Insights*.[16] The U.S. is joined in this assessment by Fiat and the Netherlands. In their appeals, Fiat touched the heart of the matter when it accused the Commission of failing to show how it derived the arm's length principle from Union law, or even what the principle is. These are harsh words, and a similar argument was put forward by the Netherlands in an even more unequivocal manner, when it was argued that there is no arm's length principle in E.U. law and that that principle is not part of a State Aid assessment.

In addition, the claw-back of taxes poses the following question: who is bearing the cost? Eventually, it will be the U.S. taxpayer, due to the foreign tax credit system in effect in the U.S. Under the U.S. tax system, foreign income taxes imposed on foreign subsidiaries of U.S. companies may be credited by their U.S. parent company when dividends are paid.[17] Within the limitations of U.S. tax law,[18] the credit reduces U.S. tax imposed on foreign-source income.

Some believe that the State Aid cases brought by the European Commission will invite a transatlantic trade war, which is of concern to the U.S. Treasury Department. In the White Paper, the following comment was made:[19]

> A strongly preferred and mutually beneficial outcome would be a return to the system of international tax cooperation that has long fostered cross border investment between the United States and EU Member States. The U.S. Treasury Department remains ready and willing to look for a path forward that achieves the shared objective of preventing the continued erosion of the corporate tax base while ensuring our international tax system is fair for all.

A similar statement was made by a spokesman for the U.S. Treasury Department:

> The Commission's actions could threaten to undermine foreign investment, the business climate in Europe, and the important spirit of economic partnership between the U.S. and the EU. We will continue to monitor these cases as they progress, and we will continue to work with the Commission toward our shared objective of preventing the erosion of our corporate tax bases.

In an article published in the *Wall Street Journal* on September 13, 2016, Treasury Secretary Jack Lew called for a U.S. tax reform in view of "Europe's Bite Out of Apple."

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16 Beate Erwin and Christine Long, "E.U. State Aid – The Saga Continues," *Insights* 6 (2016).

17 In addition, a credit may apply when a U.S. shareholder of a controlled foreign corporation includes in income an item of Subpart F income. Code §960.

18 Primarily, Code §904.

19 U.S. Department of the Treasury, "Treasury Releases White Paper on European Commission's State Aid Investigations into Transfer Pricing Rulings," accessed September 26, 2016..

CONCLUSION

The U.S. Treasury Department notes that the European Commission's interference in Member States' tax authority effectively undermines relations among those countries and with the U.S. More importantly, if domestic decisions can be overridden using a European Commission ruling, an E.U. Member State's power to enter into a bilateral income tax treaty is ultimately dismantled. On a practical level, U.S. multinational groups will have no interest in obtaining advance pricing agreements with an E.U. Member State which makes all pricing arrangements subject to audit in the U.S. and Europe.

The decision of the General Court in the State Aid cases will have far-reaching consequences. Should the court reject one of the Commission's main arguments, most notably its assertion that a deviation from the Commission's interpretation of the arm's length principle confers a "selective advantage" on the recipient, then it is likely that all of its final decisions will be annulled, since they are based on the same doctrinal "pillars." Moreover, if the E.C.J. does not support the Commission's approach on appeal, the Commission's use of the State Aid mechanism to crack down on tax avoidance will have failed dramatically. However, it will take years before certainty is reached on this level.

"Should the court reject one of the Commission's main arguments . . . it is likely that all of its final decisions will be annulled, since they are based on the same doctrinal 'pillars.'"

Until then, it remains to be seen whether pressure by the U.S. tax authorities will restrain the European Commission, or whether the European Commission will expand its investigations to include other U.S. multinationals. At this stage, with both the U.S. and the European Commission adamant in their respective positions, the stage is set for a prolonged battle. Meanwhile, U.S. multinationals are faced with difficult decisions on pricing and must carefully consider their European strategies.

EUROPEAN STATE AID AND W.T.O. SUBSIDIES

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Tags
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INTRODUCTION

Recent European Commission ("Commission") rulings involving Apple and Starbucks[1] and a World Trade Organization ("W.T.O.") ruling involving E.U. subsidies to Airbus[2] are viewed by some as evidence of a not-so *sub rosa* trade war between the U.S. and the European Union ("E.U."). The stated view in the E.U. is that these are two separate developments that should not be linked because one relates simply to fundamental harmony within the internal market of the E.U. and the other regards provisions in global trade agreements designed to settle disputes relating to export subsidies.

This article seeks to explain the basic internal procedures within the E.U. determining and outlawing State Aid. It also explains the global trade agreement embodied in the W.T.O. in connection with export subsidies and other actions designed to promote internal business in one country that harms competitors in other countries. This article concludes by evaluating the European position that State Aid within the E.U. and actionable or prohibited distortion of trade within the context of the W.T.O. are simply separate and distinct actions and that a discriminatory act under the latter cannot be compared with an illegal act under the former.

STATE AID TO STARBUCKS AND APPLE

In the past few years, the Commission has investigated many tax rulings between various companies and E.U. Member States to determine whether the agreements breached E.U. State Aid rules.

Starbucks in The Netherlands

The 2015 *Starbucks* decision addressed a Dutch advance pricing agreement obtained by the Netherlands-based entity Starbucks Manufacturing EMEA BV ("Starbucks Manufacturing"), the only wholly controlled Starbucks group entity (outside the U.S.) that roasts coffee. Starbucks Manufacturing supplied affiliates with roasted coffee. These were identified as controlled transactions for income tax purposes.

To obtain certainty regarding Dutch tax, a ruling was obtained allowing for a margin of between 9% and 12% over total production costs incurred to produce the roasted

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1 Beate Erwin, "Treasury Attacks European Commission on State Aid – What Next?" *Insights* 8 (2016).

2 *Id.*; Peggy Hollinger, Shawn Donnan, and Arthur Beesley, "W.T.O. Gives Boeing Lift with Airbus Ruling," *The Financial Times*, September 22, 2016; Jason Lange, "U.S. Accuses E.U. of Grabbing Tax Revenus with Apple Decision, *Reuters*, August 31, 2016.

coffee that was sold to affiliates. Because reported profits for financial statement purposes exceeded cost plus 12%, the Dutch tax authority agreed to allow a deduction in the form of a floating royalty payment to another group entity, Alki LP.

Alki LP then reduced its income through payments to the U.S. group under a cost sharing agreement. Alki LP made buy-in payments and annual payments reimbursing the U.S. group for the development of intangible property. Under U.S. practice, Alki LP could use the intangible property without payment of a royalty to the U.S. group. The cost sharing payments simply reduced net costs incurred by the group.

In the view of the Commission, this arrangement was not available to all and distorted the internal market because of the advantage received by Starbuck Manufacturing and Alki LP.

Apple in Ireland

In its most recent *Apple* decision, the Commission ordered Ireland to collect a record €13 billion ($14.6 billion) in unpaid taxes from Apple, holding that certain Irish tax rulings artificially lowered the tax paid in this country since 1991.[3] Apple Ireland recorded most of the profit for Apple's European operations. In turn, Apple Ireland allocated the bulk of its profits (and hence the European profits) to a fictitious "head office" that had no substance, thus essentially allowing Apple to be taxed "nowhere."

SUBSIDIES TO AIRBUS

In its recent *Airbus* ruling, the W.T.O.'s compliance panel report (the "Panel Report") confirms its 2011 Dispute Settlement Board Report (the "D.S.B. Report").[4] As a result, and in relevant part, several measures provided to Airbus by the European Communities, France, Germany, Spain, and the U.K. were characterized as specific subsidies[5] causing serious prejudice to the interests of the U.S.

The measures at issue constituted over 300 different allegations of illegal subsidies by the European Communities and the four W.T.O. member states participating in Airbus over a period of approximately 40 years. These measures enabled Airbus to develop and produce large civil aircraft that were sold globally. The principal subsidies can be summarized as follows:

- Launch aid/member state financing provided by France, Germany, Spain, and the U.K. for the development of certain large civil aircraft projects
- Certain equity infusions provided by France and Germany to companies that were part of the Airbus group
- Certain infrastructure measures provided to Airbus (*e.g.*, the lease of land in Germany, the right to exclusive use of an extended runway at a German airport, regional grants by German authorities and government, and regional grants in Spain)

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3 See Beate Erwin, "Apple in Europe – The Uphill Battle Continues." *Insights* 2 (2016), pp. 9-15.

4 See organizational chart of the W.T.O. below.

5 See below for a definition.

When compared to the aforementioned E.U. State Aid cases, the differences in the type of considered measures are substantial. The E.U. State Aid decisions fight fictitious tax arrangements allowed by certain Member States to specific taxpayers through the grant of a favorable ruling. The W.T.O. ruling condemns measures taken by a government that cause specific damage to another government.

E.U. STATE AID CONTROVERSY

One of the key concepts of the E.U. is its internal single market. The European Single Market seeks to treat the E.U. territories as one territory without any internal borders or other regulatory obstacles that may impede four fundamental principles:[6]

- The free movement of goods
- The free movement of services
- The free movement of capital
- The free movement of persons

The main objective of the European Single Market is to stimulate competition and trade, raise quality, and help cut prices.

In order to create and maintain this single market, the various E.U. Member States, relinquished national sovereignty, in part, to the E.U. This relinquishment was effected principally through the ratification of the Treaty on the Functioning of the European Union ("T.F.E.U."). While Member States relinquished the four freedoms, mentioned above, other aspects of national sovereignty were retained. Thus, the E.U., through its institutions, may only act within the limits of the grants of authority conferred to it by the Member States.

To further the achievement of the European Single Market, the E.U. State Aid rules were included in the T.F.E.U. These rules are designed to ensure fair and equal market conditions for commercial enterprises active within the various countries that comprise the European Single Market. Article 107 of the T.F.E.U. provides in relevant part that:

> Save as otherwise provided in the Treaties, 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 article further provides a list of deemed compatible aids and potential compatible aids.

In a 1998 Notice, the Commission further expanded the definition of State Aid.[7] It provides the following criteria upon which a measure by a Member State may be viewed to constitute State Aid:

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[6] Article 26 of the T.F.E.U.

[7] "Commission Notice on the Application of the State Aid Rules to Measures Relating to Direct Business Taxation," *Official Journal* C 384 (1998), pp. 3-9.

- The recipient of the measure is granted an advantage relieving it of certain charges it may otherwise incur. This advantage may reduce the taxpayer's tax burden in several ways, including
    - a tax base reduction (such as a special deduction, a special or accelerated depreciation arrangement, or the entering of reserves on the balance sheet),
    - a total or partial reduction in the amount of tax (such as an exemption or a tax credit), and
    - a deferment, cancellation, or even special rescheduling of tax debt
- The advantage must be granted either by the Member State (including its regional or local bodies) or through its resources. Whether that measure is provided for in a given Member State's tax laws or through the practice of its tax authorities is irrelevant. A loss of tax revenue is equivalent to consumption of Member State resources in the form of fiscal expenditure.
- The measure must affect competition and trade between Member States.
- The measure must be specific or selective in that it favours "certain undertakings or the production of certain goods."

Article 108(1) of the T.F.E.U. states that "the Commission shall, in cooperation with Member States, keep under constant review all systems of aid existing in those States." Such review extends to tax measures because Article 107 applies to measures in any form whatsoever.[8] Thus, although the Member States retain sovereignty in terms of direct taxes, their direct tax systems must be compliant with the E.U. State Aid rules.[9] As the Commission is responsible for enforcing the E.U. State Aid rules, it may, on its own initiative, examine information regarding alleged unlawful aid from any source.[10]

"As the Commission is responsible for enforcing the E.U. State Aid rules, it may, on its own initiative, examine information regarding alleged unlawful aid from any source."

In this area, the Commission operates in several steps. It begins by opening a preliminary investigation. If questions regarding the compatibility of the measure persist, the Commission then carries out an in-depth investigation.[11] The decision to initiate the formal investigation procedure is sent to the relevant Member State.

Pursuant to the formal investigation, a final decision is taken. There is no legal deadline to complete an in-depth investigation, and its actual length depends on many factors, including the complexity of the case, the quality of the information provided, and the level of cooperation by the Member State concerned.[12]

Three possible outcomes exist:

- The Commission reaches a favorable decision regarding the measure at issue. The measure is considered not to be aid or the aid is considered to be compatible with the internal market.

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8 *Id.*

9 *Italy v. Commission*, Case 173/73, EU:C:1974:71.

10 Council Regulation 2015/1589, Article 12.

11 "Competition: State Aid Procedures," European Commission.

12 *Id.*

- The Commission reaches a conditional decision. The measure at issue is found compatible, but its implementation is subject to conditions stated in the decision.
- The Commission reaches a negative decision. The measure is incompatible with Article 107 of the T.F.E.U. and must be withdrawn retroactively. The Commission, in principle, orders the Member State to recover the State Aid that has already been paid out to the beneficiaries.

The Commission can order the retroactive recovery of unlawful State Aid for a period of up to ten years preceding the Commission's first action taken with regard to the unlawful aid.[13] The aim of recovery is to remove the undue advantage granted to a company and to restore the market to its state before illegal State Aid was granted. A Member State is deemed to comply with the recovery decision when the aid (plus compound interest) has been fully recovered.[14] If the relevant Member State does not comply with the decision in due time, the Commission may refer it to the C.J.E.U.[15]

"The main purpose of the W.T.O. is to allow 'open, fair and undistorted competition' with regard to goods, services, and intellectual property, to the extent possible."

W.T.O. PROHIBITION REGARDING SUBSIDIES

The W.T.O. was established on January 1, 1995, as a result of the Uruguay Round of the General Agreement on Tariffs and Trades ("G.A.T.T."). It is composed of 164 member states as of July 29, 2016.[16] The main purpose of the W.T.O. is to allow "open, fair and undistorted competition" with regard to goods, services, and intellectual property, to the extent possible.[17]

The W.T.O. also provides a forum for the settlement of disputes. The W.T.O. settlement procedures are directed at government actions that distort trade. The decisions of the W.T.O. are binding on the governments that are parties to the dispute.

Typical areas of dispute include

- dumping practices, occurring when a company exports a product at a price that is lower than the price it normally charges on its own home market;
- export subsidies; and
- emergency measures that temporarily limit imports to protect domestic industries.

The following organizational chart facilitates the understanding of the W.T.O.'s work:[18]

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13 Regulation 2015/1589, Article 17.

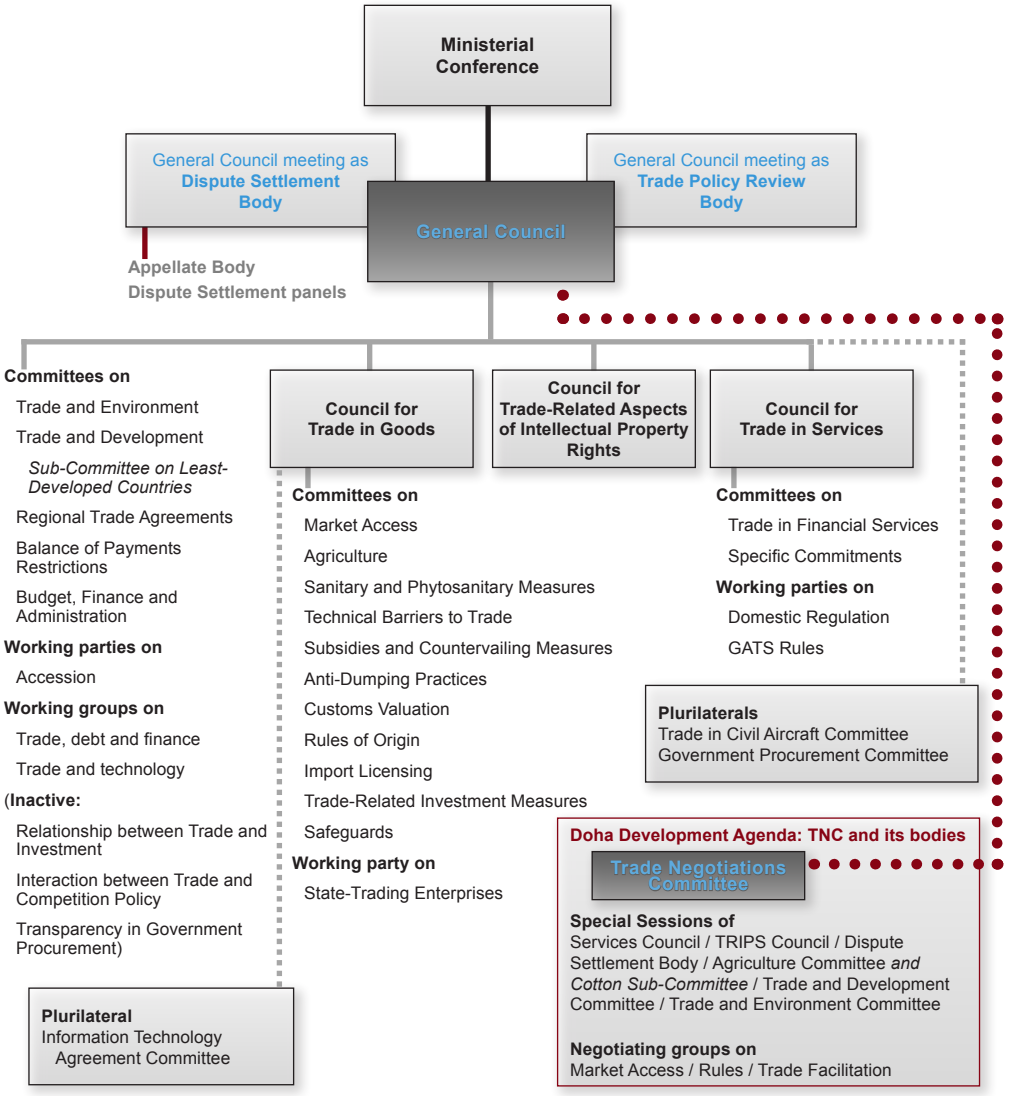
14 European Commission, "State Aid: Recovery of Illegal State Aid Gets Faster as Commission Tightens Procedures," press release, February 18, 2011.

15 Article 258 of the T.F.E.U.

16 "Understanding the WTO – Members," W.T.O.

17 *Understanding the WTO*, Fifth Edition, (Geneva: World Trade Organization Information and External Relations Division, 2015), pp. 10, 12, and 23.

18 "Understanding the WTO – Organization Chart," W.T.O.



Of the three main areas of dispute, the balance of this article focuses on the regulation of subsidies and the dispute settlement procedure.

Among the various agreements between the members of the W.T.O. is the Agreement on Subsidies and Countervailing Measures (the "S.C.M. Agreement"), which contains a definition of the term "subsidy." This definition is composed of three basic elements: (i) a financial contribution (ii) by a government or any public body within the territory of a W.T.O. member state (iii) that confers a benefit. All three of these elements must be satisfied in order for a subsidy to exist.

A financial contribution requires a charge on government funds. It can take the form of any of the following measures made directly or through payments to an intermediary:[19]

- A government practice involving a direct transfer of funds (*e.g.*, grants, loans, and equity infusion) or a potential direct transfer of funds or liabilities (*e.g.*, loan guarantees)

[19] Article 1 of the S.C.M. Agreement and Article 16 of G.A.T.T. 1994.

- The relinquishment of government revenue or the failure to collect revenue (as would be the case with a credit or an exemption from tax generally due on domestic sales)
- The provision of goods or services other than general infrastructure by a government or the purchase of goods by a government
- Any form of income or price support that operates, directly or indirectly, to increase exports of any product from or reduce imports of any product to its territory

A subsidy is subject to the terms of the S.C.M. Agreement only if it has been specifically provided to an enterprise or industry or group of enterprises or industries so that it is not broadly available within a given economy. The basic principle is that a subsidy that distorts the allocation of resources within an economy violates the S.C.M. Agreement. In comparison, a subsidy that is widely available within an economy does not distort resources and for that reason is not subject to the S.C.M. Agreement.

Article 2 provides that the following fact patterns involve subsidies that violate the S.C.M. Agreement because benefits are directed to certain enterprises:

- Access to the subsidy is explicitly limited to certain enterprises either by law or by administrative practice.
- The law or the administrative practice for granting the subsidiary does not provide objective criteria for eligibility, or if such criteria exists, the subsidy is not automatic or the administrative practice is not strictly followed.
- There is reason to believe that the subsidy may be specific, based on other factors, such as
    - the subsidy program is used by a limited number of enterprises;
    - the subsidy program is predominantly used by a limited number of enterprises; or
    - the way in which discretion has been exercised by the granting authority.

A subsidy also is subject to the S.C.M. Agreement if it is limited to certain enterprises located within a designated geographical region, or if it targets export goods or goods using domestic inputs.

Once a subsidy subject to the S.C.M. Agreement exists, a determination must be made whether the subsidy is prohibited or actionable. Prohibited subsidies are those that promote exports and those that have local content requirements. Actionable subsidies are subsidies that cause adverse effects to the interests of another member of the W.T.O. Most subsidies fall in this category.

There are three types of adverse effects. First, there is injury to a domestic industry caused by subsidized goods that are imported into the territory of the complaining member state. Second, there is serious prejudice, which usually arises because of adverse effects of the subsidy on the market of the complaining member state or a third country. Third, there is nullification or impairment of benefits accruing under

G.A.T.T., meaning an impairment of market access is presumed to flow from a tariff reduction as a result of the subsidy.[20]

CONCLUSION

As to procedure, Commission decisions regarding illegal State Aid of an E.U. Member State differs from W.T.O. rulings as to trade disputes that impair global trade.

- The Commission's rulings on State Aid are binding on the relevant Member State, which then must recover up to ten years in back taxes and interest.
- The W.T.O.'s rulings are based on good faith participation by the W.T.O. member states. Every member will then carefully consider whether a countermeasure, such as the implementation of an import duty, would be the appropriate remedy. No retroactive effect is given to a W.T.O. ruling.

However the goals of Article 107 of the T.F.E.U. to stop actions that distort free trade and those of Article 2 of the S.C.M. Agreement appear to be identical.

PROVISONS THAT MAY CONSTITUTE STATE AID	PURPOSE OF W.T.O. AGREEMENT; ACTIONABLE & PROHIBITED ACTS
The recipient of the measure is granted an advantage relieving it of certain charges it may otherwise incur.	A benefit conferred by a government or any public body within the territory of a member in the form of a financial contribution.
This advantage may reduce the taxpayer's tax, which amounts to a loss of tax revenue.	The foregoing of or absence of collection of revenue, for instance tax incentives such as tax credits.
The measure must affect competition and trade between Member States.	Government actions contrary to open, fair and undistorted competition.
The measure must be specific or selective in that it favors certain undertaking.	Access to a subsidy that is explicitly limited to a certain enterprise.

There may be many ways to look at the foregoing similarities between the Commission actions against Apple and Starbucks, and the W.T.O. decision in the *Airbus* case. However, the quantum of similarities in the goals of E.U. principles and W.T.O. principles leads one to question the judgment of the Commission to attack Member States and U.S. companies on the basis of illegal distortion to internal trade, while at the same time turning a blind eye on subsidies granted to European enterprises in a way that distorts a global market.

[20] Article 5 of the S.C.M. Agreement.

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