

General Court sets framework for the Commission to enforce arm's length transfer pricing under State aid rules (Fiat and Starbucks)



On 24 September 2019, the General Court upheld the Commission's decision that Fiat had received unlawful State aid from Luxembourg, and at the same time annulled the decision which had found the same with respect to Starbucks in the Netherlands.

Even though leading to different outcomes, these judgments support the Commission in its scrutiny of advance tax rulings on transfer pricing, explicitly confirming the possibility for the Commission to verify the arm's length nature of transactions between related parties. At the same time, it acknowledges taxpayers and Member States have a margin of appreciation.

Background

State aid is defined as a measure granted by the State or through State resources, which distorts or threatens to distort competition and affects intra-EU trade by favouring certain undertakings or the production of certain goods. Measures meeting those criteria may constitute an aid scheme, in particular, in the case they do not require further implementing measures and define beneficiaries in a general and abstract manner.

On 21 October 2015, the Commission concluded that the Netherlands and Luxembourg had granted unlawful aid to Starbucks and Fiat respectively (see our earlier [flash](#)). In both cases, the Commission challenged the transfer pricing (**TP**) analysis underpinning the price of certain intragroup transactions, e.g., with respect to the choice of the TP method, the choice of the profitability indicator, and the selection of comparable companies. The taxpayers and the Member States involved had appealed to the General Court, arguing in particular that the Commission (i) had exceeded its powers and sought to harmonise taxes through the backdoor, (ii) had made mistakes in its detailed TP assessment, and (iii) did not establish that the beneficiaries of the rulings were treated more favourably than other taxpayers.

Key findings

The General Court confirmed that the Commission can interpret State aid rules as imposing an obligation to comply with an arm's length principle, as integrated and standalone companies are in a similar situation. Hence, the Commission was right to compare the tax position of the relevant Fiat and Starbucks entities with the tax burden imposed by normal national taxation rules

on an undertaking operating in a comparable factual situation and under market conditions. The General Court appears to accept this would be the case even if there is no arm's length principle clearly laid down in domestic law. At the same time, the General Court acknowledges that TP inherently entails a degree of inaccuracy, so that an advantage only arises when the variation between two comparables exceeds the inaccuracy inherent to the chosen TP method. Moreover, in both the *Fiat* and *Starbucks* cases, the General Court found that the Commission did not exceed its powers when assessing compliance of the tax rulings with the arm's length principle.

The judgments also provide guidance on how to apply such principle concretely and came out with opposite conclusions as regards the actual evidence of an advantage provided by the Commission:

- In the *Fiat* case, the General Court found it was inappropriate to remunerate only a hypothetical amount of capital at risk, rather than the full amount of capital. Luxembourg had thus not complied with the arm's length principle, which resulted in an unlawfully reduced tax base for the taxpayer.
- In the *Starbucks* case, the General Court rejected the Commission's challenges to the Netherlands TP analysis. It found that choosing the TNMM rather than another, more direct TP method (the CUP) was not sufficient to prove the existence of an advantage. The General Court also reviewed the functional analysis of the parties to the transactions covered by the advance pricing agreement and the comparability analysis to determine an arm's length remuneration.

Finally, in the *Fiat* case, the General Court also confirmed the presumption of selectivity raised by the Commission (once an advantage resulting from the tax ruling is established). The General Court, however, also went through the standard 3-step selectivity analysis to set aside Luxembourg's and Fiat's arguments.

Next steps

Taxpayers engaged in intragroup transactions in the EU should review the General Court's positions on the different stages of a TP analysis, as the reasoning may affect how national tax authorities perform TP assessments going forward. It may be worthwhile to verify the strength of the taxpayer's TP position in view of these new developments.

The Commission (in the *Starbucks* case), Fiat and Luxembourg (in the *Fiat* case) respectively, may file an appeal with the Court of Justice, which is the court of final instance, to assess matters of law rather than fact.

An appeal of the Commission in the Belgian Excess profit ruling case is already pending with the

Court of Justice. The *Apple*, *Amazon* and *ENGIE* cases are still pending before the General Court; the hearing in the *Apple* case took place on 17 and 18 September 2019. The Commission still also has formal investigations pending into the tax treatment of Nike and IKEA in the Netherlands, Huhtamäki in Luxembourg and 39 Belgian companies which benefited from an Excess profit ruling.