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COMPETITION AND REGULATORY NEWSLETTER

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General Court issues judgment in Amazon and Engie tax rulings cases

On 12 May 2021 the EU General Court (GC) delivered two judgments; both in the context of State aid and tax rulings. The GC ruled that Luxembourg did not provide a selective advantage, and therefore unlawful State aid to Amazon. In a separate judgment, the GC ruled that Luxembourg gave unlawful State aid to the French energy company Engie as a result of two tax rulings which allowed the company not to pay taxes on 99 per cent of profits in Luxembourg.

AMAZON

THE 2017 DECISION

In its decision of 4 October 2017 the European Commission concluded that Luxembourg had granted illegal State aid to Amazon in the form of anti-competitive tax benefits. The Commission found that a tax ruling given to two companies in the Amazon group by Luxembourg in 2003, and extended in 2011, amounted to an illegal tax advantage of around €250 million. The Commission's investigation examined the structure by which Amazon set up its European sales operations using these two companies for the period May 2006 to June 2014. During this time Amazon's sales operations in Europe were structured in such a way that all European Amazon website sales were technically made through Amazon EU, the Luxembourg operating company, recording in Luxembourg all its European sales and profits. The holding company, Amazon Europe Holding Technologies (whilst not itself actively making use of intellectual property rights (IPR)) granted Amazon EU an exclusive IPR licence which enabled Amazon EU to run Amazon's European retail business. Amazon EU then paid the holding company royalties in return for the use of those rights.

This structure was endorsed by the Luxembourg tax ruling issued in 2003 and extended in 2011. The ruling authorised a way to calculate the taxable base of the operating company, Amazon EU. The tax ruling also approved a method for calculating royalty payments from the operating company to the holding company for the Amazon IPR from which only the operating company benefited. According to the Commission, the royalty payments were not in line with economic reality and were based on an unjustified methodology as their level was inflated.[1]

The Commission concluded that the tax ruling enabled the company not to pay tax on three quarters of its profits in the EU between 2006 and 2014. The Commission also concluded that the tax ruling, issued by Luxembourg endorsing the level of royalty payments, granted an unfair economic advantage to Amazon and therefore ordered

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[1] These royalty payments, which remained untaxed, amounted to over 90 per cent of Amazon EU's operating profits on average.

Luxembourg to recover the allegedly unpaid tax of €250 million from the company. Both Amazon and Luxembourg challenged the decision with the GC.

THE GC JUDGMENT

The GC upheld the appeals and annulled the Commission's decision. The GC found that the Commission has failed to prove "*to the requisite legal standard that there was an undue reduction of the tax burden of a European subsidiary of the Amazon group*". The GC held, in particular, that the Commission has failed to demonstrate that the tax ruling gave Amazon a selective advantage which would have led to unlawful State aid. The GC disagreed with the Commission's reasoning on several points. In particular, it concluded that the cost-sharing agreement between the Amazon companies constituted a lawful method to calculate taxable profits in Luxembourg and the royalty fee from the operating company to the holding company was not inflated. Amazon will not have to pay back €250 million in taxes.

The GC, in its press release, stated that the judgment provides clarity in relation to the Commission's required burden of proof to establish the presence of a selective advantage where the level of taxable income of a group company is calculated by choice of transfer pricing method. The Commission has announced that it will "*carefully study the judgment and reflect on possible next steps*". It may decide to appeal the decision with the European Court of Justice.

ENGIE

On 20 June 2018 the Commission concluded that Luxembourg gave Engie a selective advantage through two tax rulings which allowed certain Engie group subsidiaries to not pay tax on 99 per cent of profits in Luxembourg between 2008 and 2014.

The Commission decided that the tax rulings issued by Luxembourg endorsed Engie's financial structures through which the company channeled profits from one subsidiary to another by treating the same transaction both as equity and as debt, resulting in untaxed profits. The Commission found that the tax rulings issued by Luxembourg gave a selective advantage to the Engie group which could not be justified. Therefore, the Commission decided that Luxembourg's tax treatment of Engie endorsed by the tax rulings is illegal under EU State aid rules. In its decision, the Commission ordered Luxembourg to recover all illegal State aid (amounting to circa €120 million).

Engie argued that it had followed the law and had merely taken advantage of a provision in national laws. Luxembourg and Engie challenged the Commission decision before the GC.

In its judgment of 12 May 2021 the GC dismissed the appeals and according to its press release, it rejected the appellants' arguments alleging, firstly, that the Commission had not established an infringement of the national tax provisions and, secondly, that no companies had been identified which would be refused identical tax treatment for an identical financing structure. The GC emphasised that the Commission was right to look "*at the economic and fiscal reality rather than a formalistic approach that takes in isolation each of the transactions under the structure*" and confirmed that Engie's preferential tax treatment constituted a selective advantage and therefore unlawful State aid. Luxembourg must now recover the unpaid tax from Engie.

CONCLUSION

The two cases are the latest rulings in a series of State aid cases relating to tax rulings, which according to EU Competition Commissioner Margrethe Vestager "*confirm once more a key principle: while member states have exclusive competence to determine their taxation laws, they must do so in respect of EU law, including state aid rules*".

The General Court held in *Apple*, *Starbucks* and most recently *Amazon*, that the Commission has failed to provide sufficient evidence that tax rulings issued to those companies constituted a selective advantage and therefore unlawful State aid. It will remain to be seen whether future caselaw (such as the awaited GC judgment in *Nike* (Case T-

648/19) will be able to provide further clarity on the complexity of the application of the EU State aid rules to tax rulings.

OTHER DEVELOPMENTS

MERGER CONTROL

COURT OF APPEAL DISMISSES FACEBOOK APPEAL IN RELATION TO CMA REFUSING TO GRANT INITIAL ENFORCEMENT ORDER DEROGATIONS IN FACEBOOK/GIPHY

On 13 May 2021 the UK Court of Appeal rejected Facebook's appeal of the Competition Appeal Tribunal's (CAT) judgment which upheld an initial enforcement order (IEO) imposed by the Competition and Markets Authority (CMA) in its takeover of Giphy. The IEO was imposed last June and Facebook appealed the CMA's refusal to allow specific derogations to the CAT. However, the CAT upheld the CMA's decision.

Facebook relied on four grounds of appeal before the Court of Appeal, all of which were rejected. On the first two grounds, the judgment confirmed that the CMA's powers go beyond ordering the divestiture of the target corporation and allow it to freeze a company's business until clearance is granted by the CMA. This upheld the CAT's finding that preserving competition in a market includes the prevention of irreversible harm that could impact others in the market.

The third and fourth grounds of appeal related to the specific obligations of the IEO being too broad and the disproportionate nature of the requests for information issued by the CMA RFIs in relation to Facebook's request for derogations. On the third ground, the Court of Appeal held that Facebook did not cooperate appropriately in relation to requests for information issued by the CMA and so the CMA was right not to release Facebook from its obligations under the IEO. On the fourth ground, the Court of Appeal held that it was not for the CAT to decide what information was adequate for the CMA, and so the CAT's finding that the information sought was proportionate was upheld.

ANTITRUST

EUROPEAN COMMISSION PUBLISHES FINDINGS OF THE EVALUATION OF RULES ON HORIZONTAL AGREEMENTS BETWEEN COMPANIES

On 6 May 2021 the European Commission published a staff working document following its evaluation of the Research & Development Block Exemption Regulation, the Specialisation Block Exemption Regulation and the Horizontal Guidelines. The review was launched in July 2019 in order to allow the Commission to decide whether to let the two Regulations lapse, revise or extend them.

The evidence gathered during the process highlighted the relevance of the rules and suggested that their application has clear added value. However, a number of issues were identified in relation to the clarity of the rules and their limitations in keeping up with market developments, such as digitisation and the growing importance of sustainability. Additionally, multiple elements were considered to be too rigid or limited in scope – for example, the types of agreement the Regulations cover and the applicable market thresholds. These issues were found to impact the effectiveness and efficiency of the rules, indicating the need for revision.

The Commission has launched the impact assessment phase of the review with the aim of publishing a draft of the revised rules at the beginning of 2022. The Commission is aiming to implement revised rules by the end of 2022.

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REGULATORY

FCA SETS OUT PLANS FOR A NEW CONSUMER DUTY AIMED AT STRONGER PROTECTION FOR CONSUMERS IN FINANCIAL MARKETS

On 14 May 2021 the Financial Conduct Authority (FCA) announced that it is consulting on a 'consumer duty' which aims to set clearer and higher expectations for firms' standards of care towards consumers in retail financial markets. The proposals apply to the regulated activities of firms in relation to products sold to all clients other than professional clients, and apply to firms even where firms do not have a direct relationship with the end user.

The proposals for a consumer duty aim to address the need for a clear statement of expectations that goes beyond the FCA's current Principles and Rules. Under the consumer duty, firms would have to (i) ask themselves what outcomes consumers should be able to expect from their products and services; (ii) act to enable rather than hinder these outcomes; and (iii) assess the effectiveness of their actions.

The FCA is proposing to set out the consumer duty as rules and guidance in the FCA Handbook in order to provide clarity to those to whom it applies. There will be an overarching 'consumer principle' which sets the tone and establishes the overall standards of behaviour expected from firms. This will be expanded upon by the rules requiring firms to take all reasonable steps to avoid causing foreseeable harm and enable customers to pursue their financial objectives, while acting in good faith towards customers. Finally, there will be four outcomes which set out more detailed expectations for the conduct of firms. The outcomes proposed relate to communications with consumers, effective design of products and services, enhanced customer service, and fair price and value.

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