Reports of Cases

Cases T-760/15 and T-636/16

Kingdom of the Netherlands and Others
v
European Commission

Judgment of the General Court (Seventh Chamber, Extended Composition), 24 September 2019

(State aid — Aid implemented by the Netherlands — Decision declaring the aid to be incompatible with the internal market and unlawful and ordering its recovery — Tax ruling — Transfer pricing — Calculation of the tax base — Arm's length principle — Advantage — Reference system — Fiscal and procedural autonomy of the Member States)

1. *Judicial proceedings — Application initiating the proceedings — Procedural requirements — Identification of the subject matter of the proceedings — Summary of the pleas in law relied on — Documents annexed to the application — Whether admissible — Conditions*
(Statute of the Court of Justice, Art. 21; Rules of Procedure of the General Court, Art. 76(d))

(see paragraphs 114-117)

2. *Aid granted by the States — Concept — Grant of an advantage to the recipients — Advance tax decision relating to the transfer prices of an integrated undertaking — Examination of the tax treatment of intra-group transactions in the light of the arm's length principle — Whether admissible — Judicial review — Scope*
(Art. 107(1) TFEU)

(see paragraphs 136-156, 197-199)

3. *Aid granted by the States — Concept — State intervention in areas which have not been harmonised in the European Union — Direct taxation — Whether included — Designation of the tax base and allocation of the tax burden — Powers of the Member States — Limits*
(Art. 107 TFEU)

(see paragraphs 158-160)

4. *Aid granted by the States — Concept — Grant of an advantage to the recipients — Tax ruling relating to the transfer price of an integrated undertaking — Examination of the method of determining transfer prices validated in the decision in the light of the arm's length*

principle — Methodological errors identified by the Commission — Errors not necessarily giving rise to advantageous tax treatment
(Art. 107(1) TFEU)

(see paragraphs 186-193, 200-203, 206-216)

5. *Aid granted by the States — Concept — Grant of an advantage to the recipients — Tax ruling relating to the transfer price of an integrated undertaking — Advantageous tax treatment — Burden of proof borne by the Commission — Absence of proof of a tax advantage*
(Art. 107(1) TFEU)

(see paragraphs 194-196, 359, 371-373, 403, 501, 548, 549)

6. *Aid granted by the States — Concept — Grant of an advantage to the recipients — Tax ruling relating to the transfer price of an integrated undertaking — Advantageous tax treatment — Assessment in the light of the information available or reasonably foreseeable at the time of adoption of that decision*
(Art. 107(1) TFEU)

(see paragraphs 241-251, 271, 288, 396)

7. *Acts of the institutions — Statement of reasons — Obligation — Scope — Commission decision on State aid — Examination of the existence of an advantage*
(Arts 107(1) and 296(2) TFEU)

(see paragraphs 420-432)

Résumé

In the judgment of 24 September 2019, *Netherlands and Others* v *Commission* (T-760/15 and T-636/16), the Seventh Chamber, Extended Composition, of the General Court annulled the decision of European Commission classifying as State aid an advance pricing arrangement concluded by the Netherlands tax authorities with the company Starbucks Manufacturing Emea BV[1] ('SMBV').

SMBV is a subsidiary of the Starbucks group and is responsible for certain production and distribution activities within that group. On 28 April 2008, the Netherlands tax authorities concluded an advance pricing arrangement with SMBV ('the advance arrangement'), the objective of which was to determine SMBV's remuneration for its activities within the Starbucks group. Thereafter, SMBV's remuneration served to determine annually its taxable profit for the purposes of Netherlands corporate income tax. On 21 October 2015, the Commission adopted its decision (i) classifying the advance arrangement as State aid incompatible with the internal market and (ii) ordering recovery of that aid. The Kingdom of the Netherlands, on the one hand, and Starbucks Corp. and SMBV, on the other hand, each brought an action for annulment against that decision.

[1] 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 (OJ 2017 L 83, p. 38).

As direct taxation falls within the competence of the Member States, the Court, in the first place, pointed out that the Member States were nevertheless required to exercise that competence consistently with EU law. Thus, intervention by the Member States in matters of direct taxation, even if it related to issues that had not been harmonised in the European Union, was not excluded from the scope of the rules on the monitoring of State aid. It follows that the Commission could classify a tax measure such as the advance arrangement as State aid provided that the conditions for such classification had been met.

In the second place, the Court observed that, where national tax law was intended to tax the profit arising from the economic activity of an integrated company as though it had arisen from transactions carried out under market conditions, the Commission could use the arm's length principle to ascertain that the intra-group transactions were remunerated as though they had been negotiated between independent companies and, accordingly, whether a tax ruling had conferred an advantage on its beneficiary for the purposes of Article 107(1) TFEU. In that regard, the Court observed that the arm's length principle, as identified by the Commission in its decision, constituted a tool enabling it to check that intra-group transactions were remunerated as though they had been negotiated between independent companies. It thus found that, having regard to Netherlands tax law, that tool came within the framework of the exercise of the Commission's powers under Article 107 TFEU. The Commission was therefore in a position to verify whether the price level for intra-group transactions accepted by the advance arrangement in question corresponded to the level that would have been negotiated under market conditions.

In the third place, as regards the demonstration as such of the existence of an advantage, the Court considered, however, that the Commission had not managed to demonstrate that the advance arrangement at issue had conferred an advantage for the purposes of Article 107(1) TFEU by reducing SMBV's tax burden. More particularly, the Court rejected the various lines of reasoning whereby the Commission had sought to demonstrate that, by endorsing a transfer pricing method that did not enable an arm's length outcome to be reached, the advance arrangement had conferred an advantage on SMBV.

Thus, the Court first of all rejected the line of reasoning according to which the advance agreement conferred an advantage on SMBV on the ground that the very choice of the transfer pricing method for intra-group transactions did not result in a reliable approximation of a market-based outcome, in line with the arm's length principle. As mere non-compliance with methodological requirements does not necessarily lead to a reduction of the tax burden, it was further necessary for the Commission to demonstrate that the methodological errors that it had identified in the advance arrangement at issue did not allow a reliable approximation of an arm's length outcome to be reached and that those errors had led to a reduction in the taxable profit compared with the tax burden resulting from the application of normal taxation rules under national law on an undertaking placed in a comparable factual situation to SMBV and carrying out its activities under market conditions. However, such proof had not been adduced by the Commission.

In that regard, the Court inter alia observed that the Commission had invoked no element grounding the conclusion that the method applied in the advance arrangement for determining transfer pricing, namely the transactional net margin method ('the TNMM'), necessarily led to a result that was too low, conferring an advantage on SMBV. Likewise, the Court observed that the mere finding by the Commission that the advance arrangement had not analysed the royalty paid back by SMBV to an undertaking in the Starbucks group for the use of its intellectual property rights, including in particular the roasting methods and other roasting know-how, did not suffice to demonstrate that that royalty was not in fact consistent with the arm's length principle. As regards the amount of that royalty paid by SMBV, according to an analysis of the functions of SMBV relating to the royalty and an analysis of comparable roasting agreements examined by the Commission, the Court further considered that the Commission had not shown that it gave rise to an advantage within the meaning of Article 107(1) TFEU.

The Court then examined the Commission's subsidiary reasoning, according to which, even on the assumption that the TNMM could be used in the present case to determine transfer pricing, the advance arrangement conferred an advantage on SMBV because the detailed rules for the application of that method accepted by the advance arrangement were erroneous. In that regard, the Court observed that the Commission had not shown that the various errors it had identified in the detailed rules for the application of the TNMM — whether the advance arrangement's validation of the identification of SMBV as tested entity for the purposes of the application of the TNMM, of the choice of profit level indicator for the application of the TNMM or of certain adjustments made to that indicator — had conferred an advantage on SMBV.