Material selectivity after Gibraltar

ACTL Conference

Prof. Dr. Raymond Luja

13 April 2012
Notion of State Aid

Article 107 (1) TFEU:

- Presence of a benefit

- Aid granted by a Member State or through state resources, to the extent attributable to the Member State

- Aid that distorts or threatens to distort competition and affects trade between Member States

- Aid that favours certain undertakings or the production of certain goods (selectivity)

→ *No* special definition for tax purposes
→ *All* elements have to be fulfilled
Gibraltar

Case:

- Proposal to abandon corporation tax
- To be replaced by a payroll tax and a business property occupation tax
- The sum of both taxes will be capped of at 15% of profits
- Obvious benefit for off-shore companies (harmful tax competition?)
Gibraltar

“[I]t is apparent that the regime at issue, by combining those bases, even though they are founded on criteria that are in themselves of a general nature, in practice discriminates between companies which are in a comparable situation with regard to the objective of the proposed tax reform, namely to introduce a general system of taxation for all companies established in Gibraltar [...] Combining those bases of assessment not only results in taxation according to the number of employees and the size of the business premises occupied, but also, due to the absence of other bases of assessment, excludes from the outset any taxation of offshore companies, since they have no employees and also do not occupy business property.
Gibraltar

- Limited impact of this decision:

  No obligation to tax at all, despite the fact that the preceding regime did include a corporation tax.

  Decision not to tax offshore profits may be harmful tax competition, but not necessarily state aid.

- But: Gibraltar explicitly stated its new tax system intended to “tax all companies in Gibraltar”
Selectivity redefined?

- No: benchmark test still exist (favourable treatment vis-a-vis others subject to the same tax, not explained by the nature and general scheme of that tax)

- But: first determine whether the tax base is broad enough as not to exclude undertakings in a comparable situation from the outset

- However: ECJ did not address the penalty tax issue (no tax normally due, as 99% of all Gibraltar companies were to be exempt)
<table>
<thead>
<tr>
<th>Question</th>
<th>Yes</th>
<th>No</th>
<th>Yes</th>
<th>No</th>
<th>Yes</th>
<th>No</th>
<th>Selective benefit</th>
</tr>
</thead>
<tbody>
<tr>
<td>Q1. Is the scope (base) of the tax or levy broad enough? I.e. does it not (de jure or de facto) exclude undertakings (or activities or products) objectively comparable* to those included?</td>
<td>Yes: → Q2. Are undertakings subsequently entitled to a (de jure or de facto) exemption from the tax base?</td>
<td>No: →</td>
<td>Yes: → Q3. Does the exemption apply to most if not all undertakings subject to tax otherwise?</td>
<td>No: →</td>
<td>Yes: → Q4. Does the exemption extend to all undertakings that are in an objectively comparable* situation as those exempted?</td>
<td>Yes: →</td>
<td>Yes: → Selective benefit (may be declared compatible aid depending on the objectives pursued by the selectivity criterion used, unrelated to the tax at hand)</td>
</tr>
</tbody>
</table>
| No ↓                                                                     | No ↓         | Yes ↓       | No ↓         | No ↓        | No ↓         | No↓         | [* Comparable in a legal and factual situation in the light of the nature and objective of the tax; i.e. an exclusion/exemption warranted in respect of a tax’s rationale should apply to all those in a comparable situation and be proportional as to the extent of incomparability.]
| As for those undertakings initially included, a benefit may still arise; continue at Q2 as indicated. | No benefit at issue (only a general tax) [result 0] | No benefit (the exclusion or exemption is part of the benchmark used to determine whether taxes are normally due by comparable undertakings, quod non) [result I] | Selective benefit (does not meet the nature-and-structure test by means of failing the comparability test; it will most likely be declared to be incompatible aid, except for the presence of compatible objectives unrelated to the tax at hand) [result III A] | General benefit [result II] | ** Like the usual suspects: exemptions based on region, sector of industry size of investment, size or geographical spread of undertakings and alike. |
Analytical taxation: what if offshore companies were patent holding companies or financing companies?

What if the corporation tax on interest or royalties received would effectively be reduced for all companies?

“the fact that offshore companies, which constitute a group of companies with regard to the bases of assessment adopted in the proposed tax reform, avoid taxation precisely on account of the specific features characteristic of that group gives reason to conclude that those companies enjoy selective advantages.”