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Global Tax Alert

The European General Court rules that the Netherlands did not grant illegal state aid to Starbucks

On 24 September 2019, the European General Court annulled the decision of the European Commission that the Netherlands granted illegal State aid to Starbucks. This implies that – according to the General Court – the Dutch Government did not give Starbucks an advantage compared to other Dutch taxpayers which operated under similar facts and circumstances, by concluding an Advance Pricing Agreement (APA).

Background

On 21 October 2015, the European Commission rendered its final decision in the State aid investigation regarding an APA concluded by Starbucks Manufacturing EMEA BV with the Dutch tax authorities in 2008.[1] The APA confirmed the arm's-length remuneration of Starbucks Manufacturing EMEA BV's intragroup production and distribution activities, as well as the determination of the royalty payment to its parent company Alki LP for the use of Starbucks' roasting Intellectual property (IP).

In its decision the European Commission concluded that the methodology proposed by the transfer pricing report and accepted by the Dutch Government in the APA (being the Transactional Net Margin Method), did not result in a reliable approximation of a market-based outcome in line with the arm's-length principle. The European Commission is of the view that the Comparable Uncontrolled Price (CUP) Method should have been used. The European

Commission concluded that, by accepting the Transactional Net Margin methodology (TNMM), this led to a reduction of the tax liability of Starbucks Manufacturing EMEA BV under the general Dutch corporate income tax system, as compared to non-integrated companies whose taxable profit under that system is determined by the market. As such, the Commission concluded that the APA confers a selective advantage on Starbucks for the purpose of article 107, paragraph 1 of the Treaty on the Functioning of the European Union (TFEU). Therefore, The Netherlands was obliged to recover the benefit received under the APA from Starbucks.

Both Starbucks and the Dutch Government appealed the European Commission's State aid decision with the European Court.

European General Court Decision

In its ruling of 24 September 2019, the General Court indicated that in the case of tax measures, an advantage can only be present if the position of the respective taxpayer is more beneficial compared to the regular application or absence of the underlying tax measure. Considering the fact that the pricing on intra-group transactions is not determined under market conditions, the arm's-length principle is applied to tax any profits resulting from these intra-group transactions similar to third-party transactions. The General Court indicated that the arm's-length principle and therefore the underlying APA concluded between the Dutch tax authorities and Starbucks can be analyzed against the rules included in article 107, paragraph 1 TFEU.

Although the General Court ruled that the arm's-length principle can be used to identify existing State aid, it rejected the European Commission's line of reasoning by which they argued that Starbucks received a selective advantage. First, the Court indicated that the mere non-compliance with methodological requirements does not necessarily lead to a reduction of the tax burden and the European Commission would have had to demonstrate that any methodological errors identified in the APA did not allow reliable approximation of an arm's-length outcome. Furthermore, the General Court found that the European Commission did not invoke any element as to why the taxpayer's use of the TNMM instead of the CUP method led to a result that was too low. The mere use of the TNMM to determine the arm's-length remuneration of Starbucks Manufacturing EMEA BV therefore did not confer an advantage on Starbucks Manufacturing EMEA BV.

Applying a similar line of reasoning, the General Court also indicated that the mere finding by the European Commission that the APA did not analyze the size of the royalty, is not sufficient to demonstrate that that royalty was not actually in line with the arm's-length principle. Furthermore, based on the functions performed by Starbucks Manufacturing EMEA BV, the European Commission failed to demonstrate that the royalty payment should have been equal to zero or that it resulted in an advantage pursuant to article 107, paragraph 1 TFEU.

Taking the above into account, the General Court ruled that the European Commission did not demonstrate the existence of a selective advantage giving rise to illegal State aid within the meaning of article 107 TFEU. Therefore, the General Court annulled the final State aid decision by the European Commission against Starbucks.

Next steps

The European Commission may now appeal the decision of the General Court with the European Court of Justice. Such appeal should be filed within two months and 10 days after the notification of the General Court's decision.

Endnote

1. On the same date, the European Commission also published its final decision on its State aid investigation regarding a tax ruling concluded by Fiat and the Luxembourg tax authorities.

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