Progressive Turnover Taxes and EU State Aid Law (C-562/19 P, *Commission v. Poland*, and C-596/10 P, *Commission v. Hungary*)

WIRTSCHAFTS UNIVERSITÄT WIEN VIENNA UNIVERSITY OF ECONOMICS AND BUSINESS

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DST | *Freedoms and State Aid*

- Criticism that the **revenue thresholds and covered services** in the EU and unilateral DSTs, though facially neutral, in fact and by intention …
  - … target largely foreign (US) taxpayers or groups, lead to **indirect nationality discrimination**, and
  - … grant **aid** to smaller (EU) taxpayers below the thresholds (→ violation of Art 107, 108 TFEU).
- *E.g., Mason/Parada, Digital Battlefront in the Tax Wars, 92 TNI 1183 (2018); Mason/Parada, Company Size Matters, BTR 2019, 610; Mason, What the CJEU's Hungarian Cases Mean for Digital Taxes, 98 TNI 161 (2020); Mason/Parada, The Legality of Digital Taxes in Europe, 40 Virginia Tax Rev. 175 (2020).*
- Note: Potential **State aid** would be no issue if the DST were in an **EU Directive**, as any aid would then not be imputable to a Member State and hence not fall under the prohibition of Art 107, 108 TFEU (T-351/02, ***Deutsche Bahn***, paras. 101-103). – Similar considerations for the fundamental freedoms? *(E.g., Mason, A Political-Process Defense of Deference to EU Directives, Virginia Law and Economics Research Paper No. 2018-17)*

Turnover Taxes | *Freedoms and Aid*

Case	COM	GC	AG	ECJ
Commission v Poland	Decision C(2016) 5596	GC, 16 May 2019, T-836/16 and T-624/17	AG Kokott, 15 October 2020, C-562/19 P	***ECJ, 16 Mar. 2021, C-562/19 P (Appeal of 2 July 2019)***
Commission v Hungary	Decision (EU) 2017/329	GC, 27 June 2019, T-20/17	AG Kokott, 15 October 2020, C-596/19 P	***ECJ, 16 Mar. 2021, C-596/19 P (Appeal of 6 Aug. 2019)***
Vodafone (HU)	–	–	AG Kokott, 13 June 2019, C-75/18	ECJ, 3 Mar. 2020, C-75/18
Tesco-Global (HU)	–	–	AG Kokott, 4 July 2019, C-323/18	ECJ, 3 Mar. 2020, C-323/18
Google Ireland (HU)	–	–	AG Kokott, 12 Sept. 2019, C-482/18	ECJ, 3 Mar. 2020, C-482/18

- ***Vodafone*** and ***Tesco*** and ***Commission v Poland*** and ***Commission v Hungary*** – ***State Aid***
  - The Court in ***Vodafone*** and ***Tesco*** found the State aid questions inadmissible (for lack of connection with a general aid scheme).
  - In ***Commission v Poland*** (C-562/19 P) concerning a tax on the retail sector and ***Commission v Hungary*** (C-596/19 P) concerning a tax on advertisements, the Court found that those progressive, turnover-based taxes do no amount to illegal State *– Confirming the General Court in Commission v. Poland (T-836/16 und T-624/17) and Commission v. Hungary (T-20/17) and likewise AG Kokott in her Opinions in Vodafone and Tesco (AG Kokott, 15 October 2020, C-562/19 P and C-596/19 P).*

Turnover Taxes | *State Aid*

- Core arguments in ***Commission v Poland*** and ***Commission v Hungary***
  - ***Progressive, turnover-based tax on the retain sector***, with bands: 0% (for monthy turnover up to € 3,750,000), 0.8% (for the portion turnover between € 3,750,000 and € 37,500,000) and 1.4% (for the portion of turnover turnover above € 37,500,000)
  - ***Non-selectivity of such measure?***
    - Classification a national tax measure as **"selective"** requires the identification of the ***reference system*** (= "normal" tax system applicable in the Member State concerned), and thereafter demonstration that the tax measure at issue is a derogation from that reference system, in so far as it differentiates between operators who, in the light of the objective pursued by that system, are in a ***comparable factual and legal situation*** (*Commission v Poland*, para. 31).
    - The application of ***progressive taxation*** "falls within the discretion of each Member State" (*Vodafone*, *Tesco*) and "[t]he same is true in the field of State aid" (*Commission v Poland*, para. 37, referring to *ANGED*)
    - According to the ECJ (and the GC) the progressive tax rates are an ***integral part*** of the reference system (*Commission v Poland*, para 33-42) *– The Commission argued that the resulting average rate resulting from the progressive rates favors certain undertakings and that the reference framework should be a flat-rate turnover tax).*

Turnover Taxes | *State Aid*

- Core arguments in ***Commission v Poland*** and ***Commission v Hungary***
  - Turnover as an ***indicator of ability to pay***:
    - EU law on State aid does not preclude Member States from deciding to opt for ***progressive tax rates*** intended to take account of the ***ability to pay of taxable persons***, not only for natural persons but also for ***legal persons***, in particular undertakings (*Commission v Poland*, para. 40).
    - EU law thus does not preclude progressive taxation from being ***based on turnover***, including where such taxation is not intended to offset the negative effects likely to be caused by the activity being taxed (*Commission v Poland*, para. 41).
    - Turnover is a criterion of differentiation that is ***neutral and a relevant indicator*** of the taxable person's ability to pay (*Vodafone*, *Tesco*). *– Note: Turnover as indicator of ability to pay for the "earner", not the "consumer" (VAT)*
    - "It does not follow from any rule or principle of EU law, including in the field of State aid, that progressive rates may apply only to taxes on profits" (*Commission v Poland*, para. 41), and it is irrelevant for the State aid analysis that profits may be a "more precise indicator than turnover"(*Commission v Poland*, para. 41).

Turnover Taxes | ***State Aid***

- Core arguments in ***Commission v Poland*** and ***Commission v Hungary***
  - Are there limits to the use of ***turnover-based (progressive) taxes***? What does it mean for ***DSTs***?
    - The Court (broadly) concluded "that the characteristics constituting the tax, which ***include progressive tax rates***, form, in principle, the reference system or the 'normal' tax regime for the purposes of analysing the condition of selectivity" (*Commission v Poland*, para. 42).
    - That said, "it cannot be ruled out that those characteristics may, in certain cases, reveal a ***manifestly discriminatory element***, which it is, however, for the Commission to demonstrate" (*Commission v Poland*, para. 42), and which it did not do regarding the progressivity of the rates (*Commission v Poland*, para. 44).
    - Where to draw the line?
      - What would such ***"a manifestly discriminatory element"*** be? → *Thresholds? Scope? Financing of aid schemes?*
      - What is the borderline to a *Gibraltar*-situation, where the Court dealt with a tax system "that had been configured according to manifestly discriminatory parameters intended to circumvent EU law on State aid" (*Commission v Poland*, para. 43)?
      - What does it mean for ***unilateral DSTs***?

DST | *Outlook*

- **OECD Pillar 1 as an end to unilateral measures (such as DSTs)?** (Note the recent positive sentiment to reach a "consensus-based solution by the July meeting of G20 Finance ministers" in the OECD's Februar 2020 report to the G20).

6. Pillar One seeks to adapt the international income tax system to new business models through changes to the profit allocation and nexus rules applicable to business profits. Within this context, it expands the taxing rights of market jurisdictions (which, for some business models, are the jurisdictions where the users are located)[6] where there is an active and sustained participation of a business in the economy of that jurisdiction through activities in, or remotely directed at, that jurisdiction.[7] It also aims to significantly improve tax certainty by introducing innovative dispute prevention and resolution mechanisms. Pillar One seeks to balance the different objectives of Inclusive Framework members and result in the removal of relevant unilateral measures.

10.3. Removal of unilateral measures

847. As stated in the Outline, it is expected that any consensus-based agreement must include a commitment by members of the Inclusive Framework to implement this agreement and at the same time to withdraw relevant unilateral actions, and not adopt such unilateral actions in the future.[3]

DST | *Outlook*

- Commissions Communication on ***"Europe's moment: Repair and Prepare for the Next Generation"***, COM(2020)456

> The funds raised will need to be repaid through future EU budgets - not before 2028 and not after 2058. To help do this in a fair and shared way, **the Commission will propose a number of new own resources**. These could include a new own resource based on the Emissions Trading Scheme, a Carbon Border Adjustment Mechanism and an own resource based on the operation of large companies. It could also include a new digital tax, building on the work done by the Organisation for Economic Co-operation and Development (OECD). The Commission actively supports the discussions led by the OECD and the G20 and stands ready to act if no global agreement is reached. These will be in addition to the Commission's proposals for own resources based on a simplified Value Added Tax and non-recycled plastics.

DST | *Outlook*

- **EU Commission`s Work Programme 2021**, COM(2020)690 and Annex:

  > To uphold fairness in the digital world, the EU will continue to work for an international agreement for a fair tax system that provides long-term sustainable revenues. Failing this, the Commission will propose a **digital levy** in the first half of next year. In the same spirit of a fair business environment, the Commission will propose a legal instrument to **level the playing field as regards foreign subsidies**.

- Proposal for a **"digital levy"** announced for Q2/2021. – *See the Inception impact assessment Ares(2021)312667 and Pt A.29 of the Council Conclusions EUCO 10/20 (21 July 2020)*

  > The work undertaken in the OECD Inclusive Framework to find a global consensus-based solution that addresses the tax challenges of the digitalisation of the economy is considered and should be factored into the final design and scope of the initiative, as it is important not to undermine the ongoing discussions at the OECD nor to fuel international trade tensions. The initiative should be designed in a way that is compatible with the international agreement to be reached in the OECD as well as broader international obligations.
  >
  > The baseline scenario will take account of developments at international level. The Commission will identify additional policy options, such as:
  >
  > - A corporate income tax top-up to be applied to all companies conducting certain digital activities in the EU
  > - A tax on revenues created by certain digital activities conducted in the EU
  > - A tax on digital transactions conducted business-to-business in the EU

Thank you!

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