EU Direct Tax Newsalert

General Court annuls European Commission's decision declaring the aid incompatible with internal market on Amazon

On 12 May 2021, the General Court of the European Union ("GC") rendered its judgments (T-816/17 and T-318/18) regarding the action brought by Amazon group companies and Luxembourg against the final State aid decision of the European Commission (EC) 4 October 2017 (SA.38944).

Background and facts

In 2014, the EC launched an investigation into a ruling issued by the Luxembourg tax authorities to a Luxembourg tax resident company of the Amazon group in 2003, and prolonged in 2011. According to the facts as described in the decision, during the period under scrutiny (until 2014), Amazon EU Sarl (AEU) functioned as the European headquarter of the group and principal operator of Amazon's European online retail and service business, in charge of strategic decisions related to the retail and services business carried on through the EU websites. In order to carry out its operations, AEU used under a license agreement for intellectual property (IP) rights from Amazon Europe Holding Technologies (AEHT), a Luxembourg partnership. Its functions were to hold the IP and participate in the development of that IP under a cost-sharing arrangement with Amazon US.

Under the transfer pricing analysis carried out at the time when the ruling was obtained, the royalty that AEU paid to AEHT was determined based on the residual profit split method. The transfer pricing report explained why this method was preferable over the comparable uncontrolled price method (CUP) which was also analyzed.

In its decision, the EC concluded that Amazon received an individual selective advantage in the form of the tax ruling because it set a transfer pricing result and methodology that was found by the EC to be not in line with the arm's length principle.

GC decision

The GC stated first that, when examining a fiscal measure granted to an integrated company, the EC may compare the tax burden of that undertaking with the tax burden resulting from the application of the normal rules of taxation under national law of an undertaking, placed in a comparable factual situation, carrying on its activities under market conditions.

Then, the GC pointed out that the EC can demonstrate the existence of an advantage in examining the TP methodology used by an integrated company's taxable income only if the remuneration applied leads to a reduction in the taxable profit of the company compared with the tax burden of a standalone undertaking transacting on the open market subject to the application of the normal taxation rules.

In the case at hand, the GC concluded that the EC did not sufficiently demonstrate the existence of an advantage on the following grounds:

- The EC relied only on its own functional analysis of AEHT and did not demonstrate that the Luxembourg tax authorities had incorrectly chosen AEU as the tested party in order to determine the amount of the royalty.
- The EC did not establish the existence of an advantage because the "arm's length" remuneration proposed by the EC could not be solely calculated on the basis of the mere passing on of development costs of the intangible assets to AEHT without taking into account the increase in value of its intangible assets.
  - The EC was wrong to ascertain the remuneration of AEHT on the basis of the supply of "low value adding" services.
  - The EC failed to prove the undervaluation of the remuneration of AEU and did not justify to the requisite legal standard the methodological choice in light of the functions of AEU.

Takeaway

The GC provided in this decision important clarifications regarding the scope of the EC's burden of proof in establishing the existence of an advantage where the level of taxable income of an integrated company belonging to a group is determined by the choice of the transfer pricing method. It remains to be seen whether the judgment will be appealed.

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