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EU orders Luxembourg to recover €250 million in unpaid taxes from Amazon and takes action against Ireland to recover up to €13 billion from Apple in tax advantages

On 4 October 2017 the European Commission **announced** its decision that Luxembourg had granted Amazon illegal State aid in the form of anti-competitive tax benefits. Luxembourg must now recover approximately €250 million from Amazon. Also on 4 October the Commission **announced** its decision to refer Ireland to the European Court of Justice for failing to recover illegal tax benefits of up to €13 billion from Apple.

The Amazon decision

In October 2014 the Commission launched an in-depth investigation into Luxembourg's tax treatment of Amazon. As a result of the investigation the Commission concluded that a tax ruling given to two companies in the Amazon group by Luxembourg in 2003, and extended in 2011, amounted to an illegal tax advantage of around €250 million.

The structure

The Commission's investigation focused on Luxembourg's tax treatment of two Luxembourg-incorporated subsidiaries in the Amazon group - Amazon EU and Amazon Europe Holding Technologies. Both are wholly owned and controlled by the US parent company, Amazon.com, Inc. Amazon EU is the operating company responsible for Amazon's European retail business. Amazon Europe Holding Technologies is a holding company, structured as a limited partnership, which the Commission described as "*an intermediary between the operating company and Amazon in the US*".

The Commission's investigation examined the structure by which Amazon set up its European sales operations using these two companies for the period May 2006 to June 2014. During this time Amazon's sales operations in Europe were structured in such a way that all European Amazon website sales were technically made through Amazon EU, the Luxembourg operating company, recording in Luxembourg all its European sales and profits stemming from these

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sales. The holding company, Amazon Europe Holding Technologies (whilst not itself actively making use of intellectual property rights (IPR)) granted Amazon EU an exclusive IPR licence which enabled Amazon EU to run Amazon's European retail business. Amazon EU then paid the holding company royalties in return for the use of those rights.[1]

The tax ruling

This structure was endorsed by the Luxembourg tax ruling issued in 2003 and extended in 2011. The ruling authorised a way to calculate the taxable base of the operating company, Amazon EU. The ruling also approved a method for calculating royalty payments from the operating company to the holding company for the Amazon IPR from which only the operating company benefited. These royalty payments, which remained untaxed (as the holding company is structured as a limited partnership which means it is not subject to corporate taxation under Luxembourg law), amounted to over 90 per cent of Amazon EU's operating profits on average. The Commission has described these royalties as "inflated" and not reflecting economic reality, stating that:

> "*Under the method endorsed by the tax ruling, the operating company's taxable profits were reduced to a quarter of what they were in reality. Almost three quarters of Amazon's profits were unduly attributed to the holding company, where they remained untaxed. In fact, the ruling enabled Amazon to avoid taxation on three quarters of the profits it made from all Amazon sales in the EU.*"

Commission conclusions

The Commission found that the Luxembourg tax ruling endorsed an unjustified method to calculate Amazon's taxable profits in Luxembourg, enabling Amazon to shift almost three quarters of its profits from a company that is subject to tax to a company which is not. The selective tax treatment of Amazon which gave Amazon a significant competitive advantage compared to other businesses therefore was illegal under EU State aid rules.

Aid which is found to be incompatible with the Treaty on the Functioning of the European Union (TFEU) must by recovered by the relevant Member State. The Commission has determined that the methodology for calculating the amount Luxembourg must now recover covers the eight-year period Amazon had its structure in place. The Commission further characterised the amount as reflecting the value of the competitive advantage Amazon received, equalling the difference between what the company paid in taxes and what it would have paid without the benefit of Luxembourg's favourable tax ruling. The Commission has estimated this to be around €250 million, plus interest. The Luxembourg tax authorities are now to determine the exact amount.

[1] The holding company passed on part of the royalty to Amazon in the US. A US tax court has recently determined the appropriate level of these payments. The US tax authority will challenge this ruling.

Ireland taken to Court over the Apple decision

On 4 October 2017 the Commission **announced** its decision to refer Ireland to the Court of Justice for failing to implement a Commission decision of 30 August 2016 in which it ordered Ireland to recover up to €13 billion of illegal State aid from Apple.[2]

The deadline for recovery was 3 January 2017, four months from the official notification of the Commission decision. Ireland has yet to recover any of the sum and is only planning to complete its work on the calculation of the exact amount of the illegal aid granted to Apple by March 2018 at the earliest.

Ireland appealed the Commission's 2016 decision to the Court of Justice. However, this does not suspend its obligation to recover the illegal aid (under Article 278 of the TFEU).

The wider framework

The above decisions form part of a series of Commission investigations into corporate tax deals. In October 2015 the Commission decided that Luxembourg and the Netherlands had granted illegal tax advantages to Fiat and Starbucks respectively. In January 2016 the Commission found that Belgium had given numerous companies illegal tax advantages. Speaking on 4 October 2017 Competition Commissioner Margrethe Vestager **described** the Commission's work in relation to corporate tax deals as "by no means done", which, together with the recent decisions, sends a clear signal that the Commission expects companies to pay their fair share of tax.

Other developments

Antitrust

CAT dismisses Balmoral's information exchange appeal

On 6 October 2017 the Competition Appeal Tribunal (CAT) issued a **judgment** dismissing an appeal made by Balmoral Tanks Limited and Balmoral Group Holdings Limited against a fine of £130,000 imposed on Balmoral by the Competition and Markets Authority (CMA). In December 2016 the CMA **found** that Balmoral, a supplier of galvanised steel water tanks, had exchanged information relating to current and future pricing plans with three of its competitors at a one-off meeting in July 2012. The three competitors were part of a cartel in the market, which Balmoral had refused to join, and were fined separately. The CMA found that by sharing commercially sensitive pricing information with its competitors, Balmoral had engaged in a concerted practice prohibited by Article 101 of the TFEU and by Chapter I of the Competition Act 1998.

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[2] For further information on the Apple decision, see Slaughter and May's **EU Competition Newsletter** (26 August – 1 September 2016).

Before the CAT, Balmoral argued that the purpose of the meeting was not to restrict competition; rather, Balmoral intended to put an end to unwanted contact from the cartel members. The CAT found that the purpose of the meeting should be judged based on the arrangements arrived at by the end of the meeting, rather than on the intentions of the parties at the beginning. While the CAT accepted that Balmoral had attended the meeting to bring the illegitimate contact to an end, their representative remained at the meeting after he had made clear that Balmoral would not be joining the cartel. He then provided information about Balmoral's pricing, asked a competitor a specific question about their own pricing and suggested that he was keen for prices to stabilise.

In addition, Balmoral contended that the one-off nature of the meeting and type of information exchanged meant that the CMA was wrong to have concluded that the discussion was capable of reducing uncertainty within the market. The CAT found that in the context of this market where a cartel was operating, a one-off exchange of pricing information (some of which was not generic or historic) had the potential to affect prices well into the future.

TFTC imposes USD773 million fine and corrective order on Qualcomm for abuse of dominance

On 11 October 2017, following an investigation launched in February 2015, the Taiwan Fair Trade Commission (TFTC) **announced** its decision to impose a fine of TWD23.4 billion (approximately USD773 million) and a corrective order on US chipmaker Qualcomm for abuse of market dominance in the market for baseband chips for mobile communications standards including CDMA, WCDMA and LTE.

The TFTC found Qualcomm to own considerable standard essential patents (SEPs) and to have a dominant position in the baseband chip market. It also found that Qualcomm: (i) refused to license SEPs to rival chipmakers; (ii) coerced mobile phone manufacturers to sign unfair licensing agreements by linking chipset supply with patent licence contracts; and (iii) imposed exclusive terms on licensing agreements. This conduct increased the trading costs between phone manufacturers and Qualcomm's competitors, thereby forcing phone manufacturers to accept disadvantageous terms, deprived or lowered competitors' opportunities to do business, and/or reduced their ability to withstand price competition. Since Qualcomm's competitors could not circumvent the SEPs, they had to raise prices to offset the increased costs, which led to a decrease in demand for their products, thus excluding them from competing with Qualcomm. The TFTC therefore concluded that Qualcomm's licensing practices in Taiwan restricted and harmed competition in the baseband chip market, breaching the Taiwan Fair Trade Act.

This is the largest fine levied on a single company by the TFTC and marks the third recent major Asian antitrust enforcement ruling against Qualcomm. In early 2015 the Chinese National Development and Reform Commission imposed a fine of RMB6.08 billion (approximately USD975 million) on Qualcomm for its unfair patent-licensing practices; and in December 2016 the Korean Fair Trade Commission fined Qualcomm KRW1.03 trillion (approximately USD865 million), again for similar patent-licensing practices.

It is worth noting that the TFTC's fine of TWD23.4 billion is indeed very significant, especially when compared proportionally with Taiwan's much bigger neighbours, China and South Korea. Unlike in Europe, but not uncommonly in Asia, there is no further detail in its public decision of how the TFTC arrived at this level of fine. If Qualcomm's recent encounter is the beginning of a growing trend of high antitrust

fines in multiple jurisdictions across Asia, this will rapidly become a very significant risk area for companies facing antitrust investigations by Asian competition authorities.

In addition to the fine, the TFTC also imposed a corrective order requiring Qualcomm to stop its abusive behaviour and re-negotiate concluded agreements in good faith with competing chipmakers and mobile phone manufacturers.

Qualcomm released a **statement** the next day outlining its intention to seek a stay of the corrective order and appeal against the TFTC's decision to the Taiwanese courts after receiving the formal decision. Qualcomm also intends to appeal the amount of the fine and the methodology adopted in calculating it.

Regulatory

Ofgem publishes new Enforcement Guidelines and guidance on revised Standards of Conduct

On 10 October 2017 the Office of Gas and Electricity Markets (Ofgem) **published** guidance relating to its revised Standards of Conduct, which form conditions of gas and electricity licences. Additionally, Ofgem **published** updated Enforcement Guidelines, which set out how Ofgem may use its enforcement powers where businesses breach their obligations, including the Standards of Conduct.

The Standards of Conduct are enforceable, overarching rules aimed at ensuring that licensees treat domestic and microbusiness customers fairly. In addition to the three existing broad principles that suppliers must follow (behaviour towards customers, providing customers with information and customer service processes), Ofgem has added a fourth broad principle that suppliers must consider vulnerable domestic customers. Ofgem will take into account four main components when applying the Standards of Conduct: (i) the customer objective of delivering fair outcomes for customers; (ii) compliance with the broad principles discussed above; (iii) adhering to the 'fairness test' and (iv) ensuring ongoing compliance. Ofgem has now amended the 'fairness test' so that it focusses on the outcome for consumers, rather than the impact on suppliers. In addition, instead of licensees being required to take "all reasonable steps" to achieve the Standards of Conduct, they now "must" achieve these, i.e. whether a customer has been treated fairly is now based on the consumer outcomes a supplier has delivered, rather than their attempts to secure compliance.

The Enforcement Guidelines set out Ofgem's approach to using its enforcement powers under sectoral, consumer and competition legislation. The main changes made to the Guidelines include streamlining the criteria that Ofgem applies to decide when to open an investigation and use its enforcement powers and clarifying Ofgem's expectations regarding companies self-reporting possible non-compliance with licences. In addition, there are general revisions to reflect the fact that enforcement of the Standards of Conduct is now well-established and to account for Ofgem's updated practices in relation to competition law investigations.

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