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Case Notes

Ireland and Apple v European Commission: the competent exercise of competences

The European Commission knows how to grab the headlines: "State aid: Ireland gave illegal tax benefits to Apple worth up to €13 billion" it said,[1] following its decision of 30 August 2016 (the Decision).[2] Its activity has led to headlines again. This time the *Financial Times* website says: "Apple wins landmark court battle with EU over €14.3bn of tax payments."[3]

The battle was over two advance rulings of the Irish tax authorities given in relation to the chargeable profits in Ireland of two companies within the Apple group. By the Decision, the Commission found that the rulings gave rise to state aid which was to be recovered with interest. The EU's General Court annulled the Decision in a single judgment, delivered on 15 July 2020, in *Ireland (supported by Luxembourg intervening) v European Commission; Apple Sales International and Apple Operations Europe (supported by Ireland intervening) v European Commission* (*Ireland v European Commission*).[4]

Some basic facts

The two companies in the Apple group at the heart of the state aid investigation were Apple Operations Europe (AOE), formerly known as Apple Computer Ltd, and Apple Sales International (ASI).

Both AOE and ASI were incorporated in Ireland. Neither of them was resident there for Irish tax purposes.[5] Neither of them had a taxable presence in the US or anywhere other than in Ireland by virtue of their Irish branches. The head offices of AOE and ASI were said to lack any physical presence or employees and not to be located in any jurisdiction.[6] A significant number of directors

[1] European Commission, press release, *State aid: Ireland gave illegal tax benefits to Apple worth up to €13 billion* (30 August 2016), available at: *https://ec.europa.eu/commission/presscorner/detail/en/IP_16_2923* [Accessed 10 November 2020].
[2] Commission Decision (EU) 2017/1283 of 30 August 2016 on State aid SA.38373 (2014/C) (ex 2014/NN) (ex 2014/CP) implemented by Ireland to Apple [2017] OJ L187/1 (19.7.17).
[3] "Apple wins landmark court battle with EU over €14.3bn of tax payments", *FT.com*, 15 July 2020, available at: *https://www.ft.com/content/1c38fdc1-c4b3-4835-919d-df51698f18c4* [Accessed 10 November 2020].
[4] *Ireland (supported by Luxembourg intervening) v European Commission; Apple Sales International and Apple Operations Europe (supported by Ireland intervening) v European Commission* (Cases T-778/16 and T-892/16) EU:T:2020:338 (15 July 2020).
[5] The Finance Act 2014 (IR) (FA 2014 (IR)) s.43 inserted into the Taxes Consolidation Act 1997 (IR) (TCA 1997 (IR)) a new s.23A. This states that a company incorporated in Ireland is to be regarded for the purposes of the Tax Acts and the Capital Gains Tax Acts as resident in the state. FA 2014 (IR) s.43(2) provides that this rule has effect in relation to a company incorporated before 1 January 2015, like both AOE and ASI, after 31 December 2020 subject to other provisions dealing with changes of ownership.
[6] The Decision, above fn.2, recitals (51) and (52).

of AOE and ASI were employees of Apple Inc and were based in Cupertino, US from where Apple's global business was directed.[7]

Apple Inc was the company at the head of the Apple group with which AOE and ASI had a cost-sharing agreement. The agreement concerned, among other things, the research and development of technology in the products of the Apple group.[8] Both AOE and ASI held licences for the procurement, manufacture, sale and distribution of the Apple group's products outside North and South America[9] (the IP licences). The Irish branches had no rights to them and no interest in them.[10]

The Irish branch of ASI was concerned with procurement, sales and distribution activities associated with the sale of Apple-branded products to related parties and third-party customers in Europe, the Middle East, India and Africa (EMEIA) and the Asia-Pacific region. The Irish branch of AOE was responsible for the manufacture and assembly of a specialised range of computer products in Ireland such as iMac desktops, MacBook laptops and other computer accessories. It supplied these to related parties in the EMEIA region.

By virtue of section 25 of the Taxes Consolidation Act 1997 (IR) (TCA 1997 (IR)), companies like AOE and ASI, not resident in Ireland, were subject to corporation tax only to the extent that they carried on a trade in Ireland through a branch or agency. The chargeable profits of such companies included any trading income arising directly or indirectly through or from the branch or agency, and any income from property or rights used by, or held by or for, the branch or agency.[11]

The arm's length principle as contained in Article 9 of the *OECD Model Tax Convention on Income and on Capital* was first introduced into Irish tax law in 2010 in relation to arrangements between persons. An arrangement between a head office and its branch did not fall within the relevant legislation.[12]

The two advance rulings of the Irish tax authorities which the Commission alleged gave rise to state aid were given, initially, by letter of 29 January 1991 and then revised in a letter of 23 May 2007. The letters, which agreed with the proposals made by the Apple group's representatives, concerned the basis for the calculation of the chargeable profits of the Irish branches of AOE and ASI.[13]

So far as AOE was concerned, both the original and the revised tax rulings were concerned with the amount of operating costs which could be taken into account in calculating chargeable profit and the level of capital allowances which were available. The revised ruling identified an amount which was to be taken as corresponding to the "IP return" for the manufacturing process technology developed by the branch.

[7] The Decision, above fn.2, recital (44).
[8] The Decision, above fn.2, see "2.5.4. Cost Sharing Agreement between Apple Inc., ASI and AOE".
[9] The Decision, above fn.2, recital (15).
[10] The Decision, above fn.2, recital (159).
[11] See TCA 1997 (IR) s.25(2)(a).
[12] The legislation is in TCA 1997 (IR) Pt 35A, inserted by the Finance Act 2010 (IR) (FA 2010 (IR)) s.42. See further the Decision, above fn.2, recital (78). In relation to the OECD generally see the Decision, above fn.2, "2.4. Guidance on Transfer Pricing and Profit Allocation to Permanent Establishments".
[13] *Ireland v European Commission* (Cases T-778/16 and T-892/16), above fn.4, EU:T:2020:338 at [11].

So far as ASI was concerned, the original ruling provided that the calculation of the chargeable profit of its Irish branch had to be based on a margin of 12.5 per cent of operating costs, excluding materials for resale. The revised ruling of 2007 provided that the chargeable profit of the branch should correspond to a proportion of its operating costs, subject to certain exclusions.

The revised rulings of 2007 came into effect from 1 October 2007 for both branches and applied for five years if circumstances remained unchanged. They could be renewed annually and were effective until the 2014 tax year.[14] By a letter dated 12 June 2013, the Commission had asked for details of tax rulings, including those concerning AOE and ASI, and had decided to investigate them by a decision dated 11 June 2014.[15] The Commission may note that, irrespective of the validity of the Decision, the practical results of opening an investigation appear to have been significant.

The Decision

In concluding that the tax rulings gave rise to unlawful state aid which was to be recovered by Ireland, the Decision addressed the four elements of state aid contained in Article 107 of the Treaty on the Functioning of the European Union (TFEU)[16] and identified by the Court of Justice.[17]

First, it stated that Ireland had renounced tax revenue and lost state resources.[18] Secondly, it said that ASI and AOE were part of Apple which was a globally active multinational group operating in all Member States so any aid was liable to affect intra-Union trade.[19] Thirdly, ASI and AOE obtained an advantage through a reduction in their taxable bases.[20] That advantage was selective[21] and constituted operating aid.[22] Fourthly, it distorted or threatened to distort competition.[23]

The most significant part of the Commission's state aid analysis is in section 8.2 of the Decision entitled "Existence of a selective advantage" contained in recitals (225) to (413).

The Commission's reasoning in relation to the existence of a selective advantage followed a three step analysis. The first step was to identify the reference framework against which an advantage was to be judged and to show it contained the arm's length principle.[24] The second step was to consider whether or not any derogation from the reference framework resulted in a selective advantage. The third step was to address the possible justification of the selective advantage. Ireland did not advance a justification, no doubt because in its view there was no selective advantage to justify.[25] It followed that the first two steps were the significant ones before the General Court.

[14] *Ireland v European Commission* (Cases T-778/16 and T-892/16), above fn.4, EU:T:2020:338 at [21].
[15] *Ireland v European Commission* (Cases T-778/16 and T-892/16), above fn.2, EU:T:2020:338 at [22]–[23].
[16] Consolidated Version of the Treaty on the Functioning of the European Union [2016] OJ C202/47.
[17] The Decision, above fn.2, recital (220).
[18] The Decision, above fn.2, recital (221).
[19] The Decision, above fn.2, recital (222).
[20] The Decision, above fn.2, recital (223).
[21] The Decision, above fn.2, recitals (412) and (413).
[22] The Decision, above fn.2, recital (415).
[23] The Decision, above fn.2, recital (414).
[24] The Decision, above fn.2, recitals (227)–(243).
[25] The Decision, above fn.2, recital (405).

As to the first step, the Commission considered that the reference framework consisted of the ordinary rules of taxation of corporate profit in Ireland which sought to tax the profits of all companies subject to tax in Ireland. Section 25 TCA 1997 (IR), which concerned the taxation of branches was to be treated as a part of that reference framework and not as a distinct reference framework. Integrated companies were to be considered comparable to independent companies.

The Commission also considered that profit was to be allocated to the Irish branches on the basis of an arm's length principle justified by reference to domestic law and EU law in the form of Article 107 TFEU, and *Belgium and Forum 187 ASBL v Commission* (*Belgium and Forum 187*).[26] It took the view that profit allocations to AOE and ASI were based on a one-sided profit allocation method which resembled the transactional net margin method (TNMM) as described in the OECD's *Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations*.[27] The Commission referred to the edition of 2010. The TNMM had also been used by the Netherlands in relation to Starbucks and by Luxembourg in relation to Fiat Chrysler.[28]

The Commission provided alternative reasoning to justify its position if it was wrong about the reference framework and the arm's length principle in relation to section 25 TCA 1997 (IR), more conveniently outlined below.

As to the second step, concerning selective advantage, the Commission had primary and subsidiary lines of reasoning.[29]

The primary line of reasoning rested on, what proved to be, a flawed factual analysis.[30] The Commission considered that the IP licences contributed significantly to the income of AOE and ASI. It criticised the Irish tax authorities for allocating assets, functions and risks, to the head offices of AOE and ASI as they had no physical presence or employees. In the Commission's view it must have been the case that the head offices could not have controlled or managed the IP licences. Consequently, the profits should have been allocated to the Irish branches of AOE and ASI. The branches were the only element of the companies with a physical presence and employees.[31] There was no positive evidence, however, as to what the branches actually did.

In the Commission's view, the failure to allocate the relevant profit to the Irish branches resulted in an advantage being given to those companies. The advantage was selective because the tax liabilities of AOE and ASI were reduced as compared with non-integrated companies whose profits reflected prices negotiated at arm's length.

[26] *Belgium and Forum 187 ASBL v Commission* (Joined Cases C-182/03 and C-217/03) EU:C:2006:416 (22 June 2006).

[27] OECD, *Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations* (OECD, 2010), available at: *https://www.codfiscal.net/media/OECD-transfer-pricing-guidelines.pdf* [Accessed 20 November 2020]; The Decision, above fn.2, recital (93).

[28] *Netherlands (supported by Ireland intervening) v European Commission; Starbucks Corp v European Commission* (*Starbucks*) (Cases T-760/15 and T-636/16) EU:T:2019:669; [2019] STC 2323; *Luxembourg (supported by Ireland intervening) v European Commission; Fiat Chrysler Finance Europe (supported by Ireland intervening) v European Commission* (*Fiat Chrysler*) (Cases T-755/15 and T-759/15) EU:T:2019:670; [2019] STC 2416. See also T. Lyons, "Starbucks and Fiat Chrysler: is the European Commission defending national tax regimes?" [2020] BTR 37, 41–42.

[29] *Ireland v European Commission* (Cases T-778/16 and T-892/16), above fn.4, EU:T:2020:338 at [32]; and the Decision, above fn.2, recitals (260), (261) and sections 8.2.2.2 and 8.2.3.

[30] The Decision, above fn.2, recitals (264)–(321).

[31] *Ireland v European Commission* (Cases T-778/16 and T-892/16), above fn.4, EU:T:2020:338 at [37]–[40], [125], [126], [186], [228], [243] and [296].

The Commission's subsidiary line of reasoning applied if the Irish authorities were correct to allocate the IP licences outside Ireland and the Commission was wrong to say that management and control of the IP licences had to be allocated to the Irish branches.[32] In such circumstances, AOE and ASI still obtained a selective advantage. It was said to arise due to the choice of the Irish branches of ASI and AOE as the focus of the one-sided profit allocation methods, the choice of operating expense as a profit level indicator and the levels of accepted returns.[33]

The alternative line of reasoning, referred to above, which was relied upon in the event that the Commission was wrong about the reference framework, came in two parts.

First, if the reference framework consisted only of the provisions of section 25 TCA 1997 (IR), a selective advantage was, nevertheless, given to AOE and ASI. Section 25 was based on the arm's length principle and the rulings were inconsistent with that principle for the reasons given in support of the subsidiary reasoning.[34]

Secondly, if section 25 TCA 1997 (IR) was not based on the arm's length principle a selective advantage arose because the contested tax rulings "would then be the result of discretion exercised by Irish Revenue in the absence of objective criteria related to the tax system".[35] The Commission looked at a number of rulings by the Irish tax authorities,[36] but adduced no evidence of the actual exercise of a discretion in relation to the branches.

The recitals to the Decision went on to consider other necessary matters. These were not considered by the General Court and so are not reviewed here.

Before turning to the Court's judgment it may be noted that two matters of political significance appeared in the recitals. The first was a reference to ASI and AOE being "stateless".[37] The second consisted of comments by Apple's tax adviser to the Irish authorities that Apple was the largest employer in the Cork area where the branches of AOE and ASI were established.[38] To the Court's credit it did not take account of prejudicial statements which lacked, as it pointed out, legal relevance.[39]

The Court's judgment

Like the Netherlands and Luxembourg before it, Ireland was concerned to raise broader issues surrounding the actions of the Commission. The General Court had rejected Luxembourg's claim, supported by Ireland, that the Commission had exceeded its competence and infringed that of the Member States in relation to the Fiat Chrysler matter.[40] It rejected a similar claim by the Netherlands.[41] It is no surprise that it rejected a claim by Ireland that the Commission had

[32] The Decision, above fn.2, recitals (325)–(360).
[33] The Decision, above fn.2, recital (327).
[34] The Decision, above fn.2, recitals (369)–(378).
[35] The Decision, above fn.2, recital (379).
[36] The Decision, above fn.2, recitals (385)–(395).
[37] The Decision, above fn.2, at [52], [276], [277] and [281].
[38] The Decision, above fn.2, recital (64).
[39] *Ireland v European Commission* (Cases T-778/16 and T-892/16), above fn.4, EU:T:2020:338 at [120]–[121] and [440].
[40] *Fiat Chrysler* (Cases T-755/15 and T-759/15), above fn.28, EU:T:2019:670; [2019] STC 2416 at [100], [101], [107] and [135].
[41] *Starbucks* (Cases T-760/15 and T-636/16), above fn.28, EU:T:2019:669; [2019] STC 2323 at [143] and [160].

exceeded its competence and encroached on the competence of Member States derived from Articles 4 and 5 of the Treaty on European Union.[42]

Furthermore, the Court made clear that it "cannot be argued" that the Commission was carrying out de facto tax harmonisation when analysing whether the chargeable profits of AOE and ASI corresponded to that of the Irish branches.[43] It may be no more than a statement of elementary principle, but the Commission must take such help as it can find from the judgment.[44]

The Court also dismissed Ireland's contention that the Commission erred in considering the existence of an advantage and the issue of selectivity together, notwithstanding that they are distinct conditions. The two matters could be examined together.[45] Nevertheless, the Commission had to show the two conditions were satisfied.[46]

Next, the Court dismissed the contention that the reference framework against which the existence of a selective advantage should be assessed was section 25 TCA 1997 (IR), and not the ordinary rules of the Irish corporate tax system taxing all companies subject to taxation. The Court found that section 25 did not constitute a specific regime separate from the ordinary rules of taxation.[47] Then it moved on to what would become more significant matters.

The primary line of reasoning: the "exclusion approach"

The primary line of reasoning adopted what the Court called "an 'exclusion' approach".[48] This required the allocation to the Irish branches of the profits of ASI and AOE to the extent that they could not be allocated elsewhere. Ireland referred to this as "allocation by default". It was an approach which the Court found to be inconsistent with the requirements of Irish tax law and the approach of the OECD and to lack an evidential base. Each of these is considered next.

The primary line of reasoning and Irish tax law

The Court accepted Ireland's contention that the exclusion approach was incorrect as a matter of Irish tax law having regard in particular to an expert opinion on Irish law which highlighted the judgment of the Irish High Court in *S. Murphy (Inspector of Taxes) v Dataproducts (Dub.) Ltd* (*Dataproducts*).[49]

Dataproducts was incorporated and carried on manufacturing in Ireland but was resident in the Netherlands. The Irish branch transferred some funds to Switzerland. Carroll J held, on the basis of pre-consolidation legislation, that, save for certain re-transferred sums, the fund was held for and used by the company and not the Irish branch. Consequently, Irish corporation tax was not chargeable on the income arising from it.

[42] *Ireland v European Commission* (Cases T-778/16 and T-892/16), above fn.4, EU:T:2020:338 at [103]–[123]. Consolidated version of the Treaty on European Union [2016] OJ C202/13.
[43] *Ireland v European Commission* (Cases T-778/16 and T-892/16), above fn.4, EU:T:2020:338 at [116].
[44] *Ireland v European Commission* (Cases T-778/16 and T-892/16), above fn.4, EU:T:2020:338 at [106f] and [122].
[45] *Ireland v European Commission* (Cases T-778/16 and T-892/16), above fn.4, EU:T:2020:338 at [133] and [139].
[46] *Ireland v European Commission* (Cases T-778/16 and T-892/16), above fn.4, EU:T:2020:338 at [134], [136] and [137].
[47] *Ireland v European Commission* (Cases T-778/16 and T-892/16), above fn.4, EU:T:2020:338 at [163]–[164].
[48] *Ireland v European Commission* (Cases T-778/16 and T-892/16), above fn.4, EU:T:2020:338 at [178].
[49] *S. Murphy (Inspector of Taxes) v Dataproducts (Dub.) Ltd* [1988] IR 10.

The judgment did not use the exclusion approach. Instead it required a factual analysis of the activities of the branch. It asked whether the funds were "used by, or held by or for the branch"[50] as the legislation required for income to fall within the Irish corporation tax net.

The judgment in *Dataproducts* had been relied on by Ireland in the administrative procedure. The Commission did refer to Irish case law in the Decision,[51] but not to *Dataproducts*. One may wonder why not. The Commission would have been much better advised to have anticipated that Ireland would continue to rely on the case and address it.

The primary line of reasoning and OECD principles

The Court recognised that at the time of the rulings, the arm's length approach had not been incorporated into Irish law by the incorporation of the OECD Transfer Pricing Guidelines or of the Authorised OECD Approach for the purpose of allocating profits to branches of non-resident companies.[52]

Ireland confirmed, nevertheless, that for the purposes of applying section 25 TCA 1997 (IR), the value of the activities actually carried out by branches "is to be determined according to the value of that type of activity on the market".[53] The Court concluded therefore that the Commission could compare the tax burden of a non-resident company carrying on a trade in Ireland through a branch with a resident company in a comparable situation trading under market conditions.[54] The Court also placed reliance on the Irish case of *Belville Holdings v Cronin*[55] to justify the adjustment by reference to market value of a transaction between associated undertakings.[56]

In addition, the Court's conclusion was supported by the well-known case of *Belgium and Forum 187*[57] which provided for integrated companies and standalone companies to be treated on equal terms.[58]

So, the Commission does have the arm's length principle in its tool box, but subject to some basic but important qualifications.

The first is that an advantage may be identified only if "the variation between the two comparables goes beyond the inaccuracies inherent in the methodology used to obtain that approximation".[59] That was made clear also in the judgment concerning the Netherlands' tax rulings on Starbucks.[60]

[50] *Dataproducts*, above fn.49, [1988] IR 10 at 13.
[51] The Decision, above fn.2, recital (257) fn.176 where there is a reference to *Texaco (Ireland) Ltd v Murphy (Inspector of Taxes)* [1991] 2 IR 449 at 454 (Supreme Court).
[52] *Ireland v European Commission* (Cases T-778/16 and T-892/16), above fn.4, EU:T:2020:338 at [217] and FA 2010 (IR).
[53] *Ireland v European Commission* (Cases T-778/16 and T-892/16), above fn.4, EU:T:2020:338 at [210].
[54] *Ireland v European Commission* (Cases T-778/16 and T-892/16), above fn.4, EU:T:2020:338 at [212].
[55] *Belville Holdings v Cronin* [1985] IR 465.
[56] *Ireland v European Commission* (Cases T-778/16 and T-892/16), above fn.4, EU:T:2020:338 at [219].
[57] *Belgium and Forum 187* (Joined Cases C-182/03 and C-217/03), above fn.26, EU:C:2006:416.
[58] *Ireland v European Commission* (Cases T-778/16 and T-892/16), above fn.4, EU:T:2020:338 at [213].
[59] *Ireland v European Commission* (Cases T-778/16 and T-892/16), above fn.4, EU:T:2020:338 at [216].
[60] *Starbucks* (Cases T-760/15 and T-636/16), above fn.28, EU:T:2019:669; [2019] STC 2323 at [498] and [512].

Secondly, there is no freestanding arm's length principle derived from Article 107.1 TFEU which Member States are obliged to apply in all areas of their tax law.[61] That too had been stated before this judgment[62] but Member States will be pleased to see it repeated.

Thirdly, it is for Member States to designate bases of assessment and to spread the tax burden across the different factors of production and economic sectors.[63] Member States will, no doubt, welcome that uncontroversial statement.

Fourthly, again as the Court has previously stated, "normal" taxation, for the purposes of state aid law, is to be determined according to national tax rules. Given the content of the Irish tax rules, considered above, the Commission did not make an error in choosing to use the arm's length standard.[64]

It is, however, one thing to have the arm's length standard available and it is another to apply it correctly. The view that certain events "must have happened", the so-called "exclusion approach" and the lack of factual analysis of the Irish branches were fundamentally inconsistent with the proper application of the standard.[65]

Turning to the OECD's *2010 Report on the Attribution of Profits to Permanent Establishments* of 22 July 2010[66] the Court found an overlap between the approach it authorised (the Authorised Approach) and section 25 TCA 1997 (IR). The Commission was, therefore, entitled to use that approach.[67]

Just as with the arm's length principle, however, it is one thing to have a tool and another to use it correctly. The Authorised Approach required the functions carried on at the permanent establishment to be analysed.[68] As was noted above, the Commission did not analyse the functions carried out by the branches. It had, therefore, acted inconsistently with the requirements of the Authorised Approach.[69]

The primary line of reasoning and evidence generally

The Commission's failure to engage with what the Irish branches actually did resulted in its horse being flogged beyond all hope of resurrection. The Court continued, nevertheless, to wield the whip "[f]or the sake of completeness".[70] In particular it addressed Ireland's contention that, independently of the requirements of Irish tax law and the OECD, there was no justification as a matter of fact, for allocating the IP licences to the Irish branches. All strategic decisions, it was said, were taken outside the branches following a strategy set in Cupertino.

[61] *Ireland v European Commission* (Cases T-778/16 and T-892/16), above fn.4, EU:T:2020:338 at [221].
[62] *Starbucks* (Cases T-760/15 and T-636/16), above fn.28, EU:T:2019:669; [2019] STC 2323 at [498] and [512].
[63] *Ireland v European Commission* (Cases T-778/16 and T-892/16), above fn.4, EU:T:2020:338 at [222].
[64] *Ireland v European Commission* (Cases T-778/16 and T-892/16), above fn.4, EU:T:2020:338 at [223]–[225]. See also *Fiat Chrysler* (Cases T-755/15 and T-759/15), above fn.28, EU:T:2019:670; [2019] STC 2416 at [112]. See also Lyons, above fn.28, 44–46.
[65] *Ireland v European Commission* (Cases T-778/16 and T-892/16), above fn.4, EU:T:2020:338 at [228].
[66] OECD, *2010 Report on the Attribution of Profits to Permanent Establishments* (22 July 2010), available at: *http://www.oecd.org/tax/transfer-pricing/45689524.pdf* [Accessed 10 November 2020].
[67] *Ireland v European Commission* (Cases T-778/16 and T-892/16), above fn.4, EU:T:2020:338 at [239].
[68] *Ireland v European Commission* (Cases T-778/16 and T-892/16), above fn.4, EU:T:2020:338 at [242]–[243].
[69] *Ireland v European Commission* (Cases T-778/16 and T-892/16), above fn.4, EU:T:2020:338 at [244].
[70] *Ireland v European Commission* (Cases T-778/16 and T-892/16), above fn.4, EU:T:2020:338 at [250].

The Court looked in detail at the evidence concerning the branches of both AOE and ASI.[71] In many respects the Commission had no evidence at all to support its position. In relation to ASI, for example, it assumed that because a branch was permitted to carry out certain functions under the cost-sharing agreement the functions were in fact carried out[72] and that because certain activities were crucial for the branch they were actually performed by it.[73] To the extent that the Commission had evidence it was insufficient. In some respects the evidence countered its assertion. For example, it was accepted in the Commission's Decision itself that ASI had no staff until 2012 to carry out the functions alleged.[74] The rulings took effect, it will be recalled, from 1 October 2007.

The Court concluded that the Commission erred when it concluded that Apple's IP was "necessarily" managed by the Irish branches of ASI and AOE[75] and that ASI and AOE lacked the ability to manage the IP by delegating to staff outside the Irish branch where necessary.[76]

It was unnecessary to consider submissions in relation to selectivity of the advantage alleged and the justifications for it. Instead, having flogged the primary line of reasoning beyond death, it turned to the subsidiary line of reasoning.

The subsidiary line of reasoning

The Court started its analysis by noting that it was not enough for the Commission to identify methodological errors in the work of the Irish tax authorities when judged against the OECD's Transfer Pricing Guidelines. It had to show a reduction in the taxpayer's tax burden compared with that under the normal rules of taxation.[77] In other words, the Commission is carrying out a state aid investigation, not marking the tax authorities' homework. Perhaps that needed saying, but it is hardly surprising.

Just as the Commission could use the arm's length standard in the primary line of reasoning it was found to be justified in using the TNMM in the subsidiary line of reasoning.[78] Again, similarly to its approach to the arm's length standard, the Court then had to determine whether the Commission had used its tools correctly. There were three matters to be considered.

First, there was the Commission's contention that it was inappropriate for the Irish authorities to have chosen the branches as the "tested parties" for the purposes of the TNMM analysis in allocating profit to the Irish branches. Secondly, the Commission said it was inappropriate to calculate the profits of the Irish branches as a margin of their operating costs. Sales, it said, was a better indicator. Finally, the Commission said that the levels of return accepted in the tax rulings were inappropriate.

[71] *Ireland v European Commission* (Cases T-778/16 and T-892/16), above fn.4, EU:T:2020:338 at [255]–[295].
[72] *Ireland v European Commission* (Cases T-778/16 and T-892/16), above fn.4, EU:T:2020:338 at [264].
[73] *Ireland v European Commission* (Cases T-778/16 and T-892/16), above fn.4, EU:T:2020:338 at [259].
[74] *Ireland v European Commission* (Cases T-778/16 and T-892/16), above fn.4, EU:T:2020:338 at [265] and the Decision, above fn.2, recital (109).
[75] *Ireland v European Commission* (Cases T-778/16 and T-892/16), above fn.4, EU:T:2020:338 at [302].
[76] *Ireland v European Commission* (Cases T-778/16 and T-892/16), above fn.4, EU:T:2020:338 at [309].
[77] *Ireland v European Commission* (Cases T-778/16 and T-892/16), above fn.4, EU:T:2020:338 at [319] and also [347], [416], [478] and [480].
[78] *Ireland v European Commission* (Cases T-778/16 and T-892/16), above fn.4, EU:T:2020:338 at [325].

There is insufficient space here to consider each of these elements in full. In summary, the Commission's failure to justify its conclusions by reference to evidence, which had destroyed the primary line of reasoning, led to the destruction of the subsidiary line of reasoning too.

The OECD's Transfer Pricing Guidelines (2010), at paragraph 3.18, recommended the party with the least complex functional analysis be a tested party.[79] If, contrary to the primary line of reasoning, Apple's IP licences were correctly allocated to the head offices of ASI and AOE, they were unable to perform complex and crucial functions in relation to IP. The branches were inappropriate as tested parties, said the Commission, because such functions must have been performed by the branches. There was, however, no evidence that was so.[80]

There was also a lack of evidence in relation to operating costs[81] including as to why they did not reflect the value which ASI's branch had contributed to the company's operations.[82] The flawed "exclusion approach" taken to determine the functions carried out by ASI was again present.[83]

Then, in considering the Commission's view that "it must be assumed" that the Irish branch of ASI took on certain risks,[84] the Court noted that "the Commission's argument is based, according to the very wording of the contested decision, on an assumption".[85] The exclusion approach featured again.[86] Ultimately, the Court decided that the Commission did not succeed in demonstrating that the branch of ASI was responsible for risk connected with turnover.[87] When the Court came to consider other risks further evidential deficiencies were found.[88] The Commission fared no better when it came to the analysis of levels of return. The Court also found inadequacies in the subsidiary line of reasoning in relation to AOE.

The alternative line of reasoning

The Court was able to dispatch quickly the alternative line of reasoning. The first part of the reasoning was founded on the basis that the reference framework for the determination of an advantage was section 25 TCA 1997 (IR) only. An advantage was alleged to arise by virtue of the alleged use of profit allocation methods which departed from the arm's length principle as set out in the subsidiary line of reasoning. The flaws in the subsidiary line of reasoning therefore caused the failure of the alternative line of reasoning.[89]

The second part of the alternative reasoning said there was an advantage given even if section 25 TCA 1997 (IR) did not incorporate the arm's length principle. In such circumstances, said the Commission, the Irish authorities must have issued the tax rulings on a discretionary basis.

[79] They are quoted in the Decision, above fn.2, recital (94) and fn.68.
[80] *Ireland v European Commission* (Cases T-778/16 and T-892/16), above fn.4, EU:T:2020:338 at [328] and [340]–[341].
[81] *Ireland v European Commission* (Cases T-778/16 and T-892/16), above fn.4, EU:T:2020:338 at [369].
[82] *Ireland v European Commission* (Cases T-778/16 and T-892/16), above fn.4, EU:T:2020:338 at [365].
[83] *Ireland v European Commission* (Cases T-778/16 and T-892/16), above fn.4, EU:T:2020:338 at [361].
[84] The Decision, above fn.2, recital (337).
[85] *Ireland v European Commission* (Cases T-778/16 and T-892/16), above fn.4, EU:T:2020:338 at [376].
[86] *Ireland v European Commission* (Cases T-778/16 and T-892/16), above fn.4, EU:T:2020:338 at [379].
[87] *Ireland v European Commission* (Cases T-778/16 and T-892/16), above fn.4, EU:T:2020:338 at [390].
[88] By way of example, *Ireland v European Commission* (Cases T-778/16 and T-892/16), above fn.4, EU:T:2020:338 at [394].
[89] *Ireland v European Commission* (Cases T-778/16 and T-892/16), above fn.4, EU:T:2020:338 at [486] and [488].

There were two reasons why this failed. First, even if there were a discretion that did not mean there was an advantage.[90] Secondly, the Commission had not shown that there was a discretion.[91]

Conclusion

Ireland is bound to be as pleased with this judgment as Apple, notwithstanding the loss of tax that it entails. The US will no doubt also be pleased with the result, particularly as it lost its application to intervene in the case brought by ASI and AOE.[92]

So far as the European Commission is concerned, there are a number of possible responses to the decision of the General Court.

One would be to say, perhaps, that it should be appealed and, the Court has now, indeed, entered an appeal.[93] An appeal by an investigator who lacks evidence to support its conclusions would, doubtless, be fiercely and properly resisted. For the Commission to lose an appeal and see the Court's judgment affirmed would only increase the damage it has suffered. Nevertheless, the Commission clearly thinks an appeal is justified.

An alternative response would have been to say that the judgment is only one judgment in a developing area of activity and that the Court has made some statements which are helpful to the Commission. For example, it has affirmed that the Commission can scrutinise the tax rulings of national tax authorities to discover if state aid has been granted. It has confirmed too that the Commission can use the arm's length principle so long as there is a basis for such an assessment in national tax law. The Commission can continue, therefore to pursue its investigations into tax rulings. There may be some truth in this, but the Commission had already established these propositions.

Perhaps the most important consideration to be borne in mind in analysing the Court's judgment, is that the Commission lost the case not because of isolated errors but because of a flawed approach to factual analysis and the evidence in issue. A reliance on "what must have happened" and on the "exclusion approach" removed the Commission's Decision from reality. It is telling how many times the Court makes statements to the effect that: "the Commission provided no evidence".[94]

All courts are familiar with the conflict between abstract reasoning on the one hand and evidence and experience on the other. As Oliver Wendell Holmes Jr said: "The life of the law has not been logic: it has been experience."[95] The litigant who says that something "must have happened" is frequently met by the response "prove it". In future, surely, the Commission will make sure it can.

[90] *Ireland v European Commission* (Cases T-778/16 and T-892/16), above fn.4, EU:T:2020:338 at [493].
[91] *Ireland v European Commission* (Cases T-778/16 and T-892/16), above fn.4, EU:T:2020:338 at [395].
[92] *Ireland v European Commission* (Cases T-778/16 and T-892/16), above fn.4, EU:T:2020:338 at [72].
[93] See *Commission v Ireland* (C-465/20 P) (20 September 2020). The appeal was lodged after this case note was submitted to the publisher and is not commented on here.
[94] *Ireland v European Commission* (Cases T-778/16 and T-892/16), above fn.4, EU:T:2020:338 at [263] and [293] and see to similar effect [271], [292], [333], [350], [380], [416], [440] and [479]. Note also [331] where the Court notes: "[T]he Commission merely asserted."
[95] O.W. Holmes Jr, *The Common Law*, available at: *http://www.gutenberg.org/files/2449/2449-h/2449-h.htm* [Accessed 11 November 2020], 1.

Like the Netherlands, Ireland has shown that the Commission's decisions in relation to tax rulings are vulnerable to detailed scrutiny. The Commission will not want another Member State to do the same. One consequence of this judgment, therefore, is to increase significantly the importance of Luxembourg's forthcoming appeal.[96] The Commission will be hoping the result of that appeal does not make more adverse headlines. Were it to do so, the stakes in the appeal which has now been commenced in relation to Ireland would be increased considerably.

Timothy Lyons*

[96] See *Ireland v Commission* (C-898/19 P) and *Fiat Chrysler Finance Europe v Commission* (C-885/19 P).

Advance rulings; Competence; Corporation tax; EU law; Ireland; Non-resident companies; OECD; State aid; Transfer pricing

* QC, Barrister, 39 Essex Chambers.