

# State Aid, Subsidy and Tax Incentives under EU and WTO Law

Claire Micheau



**Wolters Kluwer**  
Law & Business

# Summary of Contents

<b>About the Author</b>	<b>vii</b>
<b>Table of Contents</b>	<b>xi</b>
<b>List of Abbreviations</b>	<b>xxi</b>
<b>Acknowledgements</b>	<b>xxv</b>
<b>Introduction</b>	<b>1</b>
<b>PART I</b>	
<b>Regulatory Framework of Tax Incentives</b>	<b>21</b>
CHAPTER 1	
Rationales for Tax Incentive Rules	23
CHAPTER 2	
EU and WTO Legal Regimes of Tax Incentive	89
<b>PART II</b>	
<b>Definition of Tax Incentive under EU and WTO Law</b>	<b>157</b>
CHAPTER 3	
Basic Criteria for Defining a Tax Incentive	159
CHAPTER 4	
The Distinctive Importance of Tax Selectivity	219

Summary of Contents

---

<b>PART III</b>	
<b>Procedural Rules on Tax Incentives under EU and WTO Law</b>	<b>301</b>
CHAPTER 5	
Administrative and Judicial Review of Tax Incentives	303
CHAPTER 6	
Remedy Rules	375
<b>PART IV</b>	
<b>Relationships between EU State Aid Law and WTO Subsidy Law</b>	<b>421</b>
CHAPTER 7	
Interactions between EU and WTO Rules on Tax Incentives	423
CHAPTER 8	
Perspectives and Proposals for a Multi-level Regulation of Tax Incentives	457
<b>Conclusion</b>	<b>509</b>
<b>Bibliography</b>	<b>515</b>

# Table of Contents

About the Author	vii
List of Abbreviations	xxi
Acknowledgements	xxv
Introduction	1
PART I	
Regulatory Framework of Tax Incentives	21
CHAPTER 1	
Rationales for Tax Incentive Rules	23
§1.01 General Objectives of Tax Incentive Rules	23
[A] Economic Justifications for Incentives	24
[1] Effects of Incentives	24
[a] The Positive Effects of Correcting Market Failure	24
[b] Overview of Some Negative Effects of Incentives	27
[2] Incentives in the Regulatory Context of Competition	29
[B] Different Objectives of the EU and the WTO	31
[1] Objectives of the WTO Rules on Tax Subsidy	31
[a] General Objectives of Trade	32
[b] WTO Principles Applied to Subsidy Law	33
[c] The SCM Agreement: An Objective of Competition Policy?	35
[d] WTO Tax Principles	36
[2] Objectives of EU Rules on Tax State Aid	36
[a] General Objective of Market Integration	37
[b] State Aid Law as Part of Competition Law?	38
[c] Addressing Harmful Tax Competition	40

## Table of Contents

---

	Conclusion: Two Regulatory Systems of Incentives with Distinct Objectives	42
§1.02	Historical Review of Tax Incentive Rules	43
	[A] Different Evolutions of Tax Incentive Rules	44
	[1] Evolution of WTO Rules on Tax Subsidies	44
	[a] The Havana Charter: Origins of Tax Subsidy Regulations	44
	[b] Development of Tax Subsidy Regulations: The GATT 1947	46
	[c] Significant Evolution of Rules on Tax Subsidies: The Subsidies Code 1979	49
	[d] The Uruguay Round (1986-1994) and the Adoption of the SCM Agreement	52
	[2] Evolution of EU Rules on Tax State Aid	54
	[a] Developments of State Aid Rules	55
	[i] The Early Developments	55
	[ii] Evolution under EU Primary, Secondary and Supplementary Law	56
	[b] Application of State Aid Rules to Taxation	62
	[i] Pioneering Role of the Court of Justice	62
	[ii] The Monti Memorandum: Adoption of a Global Tax Strategy	64
	[iii] Harmful Tax Competition in the Context of Tax State Aid	65
	[iv] The 1998 Notice: Clarification of State Aid Rules Applied to Direct Taxation	69
	[v] Review on the Application of the Notice: The Implementation Report	70
	[vi] The Recent Developments	72
	[B] Mutual Influence on Tax Incentive Regulations	73
	[1] Limited Influence between WTO and EU Law on Incentive Regulations	74
	[a] The Difficult Compromise on the Notion of Incentive	74
	[b] Absence of Mutual Influence on Tax Incentive Regulations	76
	[2] Significant Influence of the OECD	78
	[a] OECD Criteria to Identify Harmful Preferential Tax Regimes	79
	[b] Influence of the OECD on EU Review of Tax Aids	83
	Conclusion: Evolution of Two Different Conceptions of Tax Incentive Regulations	86

## CHAPTER 2

EU and WTO Legal Regimes of Tax Incentive	89
§2.01 Overview of the EU Legal Regime of State Aid	89
[A] Principle of Effect-Based Assessment	90
[B] Rules on Compatibility with the Internal Market	91
[1] Aids Compatible De Jure under Article 107 §2 TFEU	92
[2] Aid Subject to a Discretionary Assessment under Article 107 §3 TFEU	95
[a] Scope of the Discretionary Powers	95
[b] Exemptions under Article 107 §3 TFEU	96
[i] Article 107 §3 (a) and (c) TFEU	96
[ii] Article 107 §3 (b) TFEU	98
[iii] Article 107 §3 (d) TFEU	99
[iv] Article 107 §3 (e) TFEU	100
[3] Other Legal Basis to Assess the Compatibility	100
[4] Operating Aids	101
§2.02 Overview of the WTO Legal Regime of Subsidy	102
[A] Classification of Subsidies	103
[1] Introduction to WTO Subsidy Regulations	103
[a] The GATT 1947 and the SCM Agreement	103
[b] Subsidies on Trade in Services	105
[c] Subsidies on Agricultural Products	107
[d] Treatment of Developing Countries	108
[2] The Traffic-Light Approach	111
[a] The Red Light: Prohibited Subsidies	111
[b] The Yellow Light: Actionable Subsidies	113
[i] Injury to a Domestic Industry	114
[ii] Nullification or Impairment of Benefits Accruing under GATT 1994	116
[iii] Serious Prejudice	117
[c] The Former Green Light: Non-actionable Subsidies	120
[B] Prohibited Subsidies in Taxation	121
[1] Tax Import Subsidies	121
[a] Prohibition of Tax Import Subsidies and Article III §4 of GATT 1947	121
[b] Prohibition of Tax Import Subsidies and Article III §8(b) of GATT 1947	124
[2] Tax Export Subsidies: The FSC Cases	125
[a] Introduction to FSC Proceedings	126
[b] The First Dispute: The FSC Legislation	127
[i] Historical Framework: The DISC Legislation	127
[ii] The FSC Legislation: Tax Exemption of Foreign Trade Income	129
[iii] Report of the Panel Body on the FSC Dispute	131

## Table of Contents

---

	[iv] Report of the AB on the FSC Dispute	135
	[v] Outcomes of the Reports on the FCS Legislation	136
[c]	The Second Dispute: The ETI Act	138
	[i] The ETI Act: Prevailing System or Exception to the System?	138
	[ii] Report of the Panel Body on the ETI Dispute	140
	[iii] Report of the AB on the ETI Dispute	143
	[iv] Outcomes of the Reports on the ETI Act	146
[d]	The Third Dispute: The Jobs Act	147
	[i] The Repeal of the ETI Act	148
	[ii] Transitional Rules: The Grandfathering Clause	149
[e]	Conclusive Remarks: Main Findings of the FSC Cases	150
	Conclusion of Part I	155
	PART II	
	Definition of Tax Incentive under EU and WTO Law	157
	CHAPTER 3	
	Basic Criteria for Defining a Tax Incentive	159
§3.01	Origin of the Tax Measure	159
	[A] Assessing the Origin of the Tax Measure under Two Legal Systems	159
	[1] Origin of the Tax Measure under EU Law	159
	[a] Introduction to the Criterion of 'State-Originated Resources'	160
	[i] Imputability	161
	[ii] State Resources	162
	[b] The Positive Fiscal Effect on Budget	164
	[c] Link between State-Origin and Advantage	168
	[2] The 'Financial Contribution by a Government' under WTO Law	169
	[a] Introduction to the Notion of 'Financial Contribution by a Government'	170
	[b] The Foregoing of Fiscal Revenue Otherwise Due	172
	[c] The Issue of Double Taxation	174
	[B] Comparative Analysis of the Criterion	175
	[1] EU State versus WTO Government	176
	[2] Double Taxation: Restrictive Approaches under EU Law and WTO Law	177
	[3] The Issue of Charge on the Public Account	180
	[a] Two Different Historical Views	180
	[b] 'Charge on the Public Account' versus 'Transfer of State Resources'	182
	[c] Critical Analysis	186

§3.02	Tax Advantage	189
	[A] Notion of Tax Advantage under EU Law	190
	[1] Introduction to the Notion of Advantage	190
	[2] Tax Advantage	193
	[a] Main Forms of Tax Advantages	193
	[b] Advantage as a Derogation Tax Scheme	195
	[c] Tax Advantage and Transfer Prices	197
	[B] Notion of Tax Benefit under WTO Law	199
	[1] Assessing the Criterion of Benefit	199
	[a] Introduction to the Notion of Benefit	199
	[i] Benefit and Financial Contribution	199
	[ii] Recipient of the Benefit	200
	[b] Calculation of the Benefit	201
	[2] Tax Benefit: Similarities with the EU Interpretation of Tax Advantage	204
	[a] Tax Benefit	204
	[b] Tax Benefit versus Tax Advantage	204
§3.03	Affection of Trade, Distortion of Competition and Adverse Effects	206
	[A] Effect on Trade and Competition under EU Law	206
	[1] Broad Interpretation of the Conditions of Affection of Trade and Competition	206
	[2] <i>De Minimis</i> Rules	210
	[B] Adverse Effects under WTO Law	211
	[C] Parallel between EU Trade and Competition Effects and WTO Adverse Effects	212
	Conclusion: Parallelism and Difference	214
CHAPTER 4		
	The Distinctive Importance of Tax Selectivity	219
§4.01	Different Approaches to Tax Selectivity	220
	[A] The Criterion of Tax Selectivity under EU Law	220
	[1] Tax Selectivity	220
	[a] Different Forms of Tax Selectivity	221
	[b] Dichotomy between General and Selective Tax Measures	224
	[c] The Derogation Test	228
	[d] Margin of Discretion	233
	[e] Regional Tax Selectivity	235
	[i] Assessment of Regional Selectivity	236
	[ii] Critical Thoughts on Regional Selectivity	242
	[2] Justification by the Nature and General Scheme of the System	248
	[a] Jurisprudential Origin of the Justification	248



## Table of Contents

---

	[b] Application of the Justification by the Logic of the Tax System	249
	[c] Restrictive Approach of EU Case Practice	252
[B]	The Criterion of Tax Specificity under WTO Law	255
	[1] The Specificity Test	255
	[a] Introduction to the Notion of Specificity	255
	[b] The Specificity Test under Article 2 of the SCM Agreement	256
	[2] Tax Specificity	258
§4.02	Limits to the Notion of Tax Selectivity	260
	[A] Comparative Review of Tax Selectivity	261
	[1] Selectivity versus Specificity	261
	[a] Conceptual Differences	261
	[b] Presumption of Specificity	262
	[c] Certain Undertakings versus Certain Enterprises	262
	[d] Jurisprudential Selectivity Test versus Textual Specificity Test	264
	[2] Analysis of Tax Selectivity	266
	[a] Subtle Distinction between Tax Advantage and Tax Selectivity	266
	[b] Regional Selectivity versus Regional Specificity in Tax Matters	269
	[B] Tax Selectivity and Tax Reference Framework	271
	[1] Difficulty in Assessing the Tax Reference Framework	272
	[a] Derogation Test and Comparability Test	272
	[b] Extensive Application of the Selectivity Test	275
	[2] Proposal for Alternative Approaches	284
	[a] The 'But For' Test	284
	[b] Considering the Objective of the Tax Measure	286
	[c] A More Economic-Based Approach	291
	Conclusion: Refining the Approach for Tax Selectivity	296
	Conclusion of Part II	299
	PART III	
	Procedural Rules on Tax Incentives under EU and WTO Law	301
	CHAPTER 5	
	Administrative and Judicial Review of Tax Incentives	303
§5.01	Overview of the Enforcement Systems	303
	[A] Procedural Aspects of Tax State Aid under EU Law	304
	[1] Administrative Phase	304
	[a] Notified Aids	306
	[b] Unlawful Aids	308

	[c] Existing Aid Schemes	310
	[d] Decision Adopted by the Council	312
[2]	Judicial Phase	314
	[a] Overview of the Allocation of Powers between European and National Courts	314
	[b] Actions Taken before the European Jurisdiction	317
	[i] Action for Failure to Fulfil an Obligation	317
	[ii] Action for Annulment	319
	[iii] Action for Failure to Act	322
	[iv] Action for Damages	323
[B]	Procedural Aspects of Tax Subsidies under WTO Law	325
	[1] Notification of Subsidies	325
	[2] Dispute Settlement Mechanism	328
	[a] Dispute Resolution of Prohibited Subsidies	329
	[b] Dispute Resolution of Actionable Subsidies	332
	Conclusion: Disparities between the Enforcement Systems	334
§5.02	Limited Rights of Taxpayers as Third Parties	338
	[A] Right of Taxpayers as Third Parties under EU Law	338
	[1] Rights of Taxpayers as Third Parties during the Administrative Proceeding	340
	[a] Notion of Third Party	340
	[b] Absence of Rights under the Preliminary Examination	341
	[c] Limited Rights under the Formal Investigation Procedure	346
	[2] Rights of Taxpayers as Third Parties during the Judicial Proceeding (Article 263 TFEU)	348
	[a] Tax Autonomous Region	348
	[b] Recipient of the Tax Aid	350
	[c] Competing Undertakings	352
	[d] Associations	357
	[B] Limited Rights of Taxpayers as Private Parties under WTO Law	358
	[1] WTO Members as Third Parties	359
	[2] Indirect Access for Taxpayers	360
	[3] Private Complaints at a National Level	361
	[4] Limited Effects of Amicus Curiae Briefs for Taxpayers	367
	Conclusion: Strengthening the Rights of Taxpayers as Private Parties under EU Law and WTO Law	370
CHAPTER 6		
	Remedy Rules	375
§6.01	Recovery of Tax Aids	376
	[A] The Principle of Recovery under EU Law	377
	[1] Legal Framework of Aid Recovery	377

Table of Contents

---

	[a]	Restoring the Previously Existing Situation	377
	[b]	Aid Recovery at the EU Level	379
	[c]	Aid Recovery at the Member State Level	381
	[d]	Parallel Litigation at European and National Levels	383
	[2]	Enforcement of Aid Recovery	384
	[a]	Justifications for Failure to Recover	384
	[b]	Timetable for the Implementation of the Recovery Decision	386
	[c]	<i>The Degendorf Principle: Set-Off of Illegal Aid for Approved Aid</i>	387
	[B]	Issues of Tax Recovery	388
	[1]	Terms of Tax Recovery	389
	[a]	Amount of Tax Recovery	389
	[b]	Incidence of the Tax System in the Determination of the Amount Recovered	390
	[2]	Recovery of a Tax Financing the Aid	392
	[a]	Recovery of a Tax Forming a Part of the Aid	392
	[b]	Liability to the Tax Financing an Aid	394
	[c]	Reimbursement of the Tax Financing an Aid	396
§6.02		Withdrawal and Countervailing Duties for Tax Subsidies	398
	[A]	Multilateral Measures	399
	[1]	Withdrawal	399
	[2]	Retrospective Payment of Tax Subsidies	401
	[3]	Appropriate Countermeasures	404
	[B]	Unilateral Measures	405
	[1]	Countervailing Duties Proceedings	406
	[2]	Calculation of Tax Subsidies to Levy Countervailing Duties	408
	[3]	Accelerated Tax Depreciation	410
		Conclusion: Unsatisfactory Remedies for Tax Incentives	412
		Conclusion of Part III	417
		PART IV	
		Relationships between EU State Aid Law and WTO Subsidy Law	421
		CHAPTER 7	
		Interactions between EU and WTO Rules on Tax Incentives	423
§7.01		Overlaps between EU and WTO Rules on Tax Incentives	424
	[A]	Differences in Scopes and Definitions	424
	[1]	Different Scopes of Application	424
	[2]	Different Substantive Conditions	426
	[a]	Origin of the Tax Measure	426
	[b]	Notion of Tax Advantage/Benefit	428
	[c]	Notion of Tax Specificity/Selectivity	429

	[B] Differences in Exemptions	433
	[1] De Jure and Discretionary Exemptions	433
	[2] General Block Exemption Regulation	434
§7.02	Liabilities in Situations of Conflict	435
	[A] Issue of Liability Raised by a State	437
	[1] Representation of the EU in the WTO	437
	[2] Joint Liability for Violation of Subsidy Law	441
	[3] Liability of the Subsidizing Member State	444
	[B] Issue of Liability Raised by an Individual	446
	[1] Absence of Direct Effect	446
	[2] Non-contractual Liability of the EU	450
	Conclusion: Is There a Need for Conformity?	452
CHAPTER 8		
	Perspectives and Proposals for a Multi-level Regulation of Tax Incentives	457
§8.01	What Is Next?	458
	[A] EU Development	458
	[1] Limited Outcome of the State Aid Action Plan (2005-2009)	458
	[2] The Distinctive Work of the Code of Conduct Group	460
	[3] The State Aid Modernisation Reform	462
	[B] The Difficult Negotiations of the Doha Round	465
§8.02	Designing New Approaches	474
	[A] Balancing the Regulation of Tax Incentives with State Tax Sovereignty	474
	[1] General Considerations on the Notion of Tax Sovereignty	474
	[2] Respecting Tax Sovereignty under EU Law and WTO Law	479
	[B] Establishing a Forum on Tax Incentive Regulation	486
	[1] A Need for a Forum	486
	[2] Determining an Appropriate Structure for a Forum on Tax Incentive Regulation	490
	[a] The WTO	490
	[b] The UN	492
	[c] The OECD	493
	[d] Creating a New Organization	498
	Conclusion: Towards a Suitable Institutional Vehicle for a Forum on Tax Incentive Regulation?	500
	Conclusion of Part IV	505
	Conclusion	509
	Bibliography	515