POMOC PAŃSTWA – ZJEDNOCZONE KRÓLESTWO

Pomoc państwa SA.34914 (2013/C) (ex 2013/NN) – System poboru podatku dochodowego od osób prawnych w Gibraltarze

Zaproszenie do zgłaszania uwag zgodnie z art. 108 ust. 2 TFUE

(Tekst mający znaczenie dla EOG)

(2013/C 348/06)

Pismem z dnia 16 października 2013 r., zamieszczonym w autentycznej wersji językowej na stronach następujących po niniejszym streszczeniu, Komisja powiadomiła Zjednoczone Królestwo o swojej decyzji o wszczęciu postępowania określonego w art. 108 ust. 2 TFUE, dotyczącego wyżej wymienionego środka pomocy.

Zainteresowane strony mogą zgłaszać uwagi na temat środka, w odniesieniu do którego Komisja wszczyna postępowanie, w terminie jednego miesiąca od daty publikacji niniejszego streszczenia i następującego po nim pisma. Uwagi należy kierować do Kancelarii ds. Pomocy Państwa w Dyrekcji Generalnej ds. Konkurencji Komisji Europejskiej na następujący adres lub numer faksu:

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Otrzymane uwagi zostaną przekazane Zjednoczonemu Królestwu. Zainteresowane strony zgłaszające uwagi mogą wystąpić z odpowiednio uzasadnionym pisemnym wnioskiem o objęcie ich tożsamości klauzulą poufności.

STRESZCZENIE

W dniu 1 czerwca 2012 r. Komisja otrzymała skargę od władz hiszpańskich dotyczącą nowego systemu poboru podatku dochodowego w Gibraltarze, wprowadzonego ustawą o podatku dochodowym z 2010 r. (ITA 2010). Według Hiszpanii ten nowy system powoduje *de facto* selektywne korzyści dla przedsiębiorstw działających w sektorze *offshore*, za sprawą połączonego skutku stosowania zasady terytorialności oraz systemu zwolnień podatkowych w odniesieniu do dochodu biernego.

OPIS ŚRODKA

W dniu 1 stycznia 2011 r. weszła w życie ustawa o podatku dochodowym z 2010 r. („ITA 2010"), która zastąpiła poprzednią ustawę o podatku dochodowym z 1952 r. Ogólna stawka podatku dochodowego od osób prawnych wynosi 10 %; w stosunku do przedsiębiorstw użyteczności publicznej i przedsiębiorstw, które nadużywają pozycji dominującej na rynku, obowiązuje specjalna stawka wynosząca 20 %.

Zgodnie z ITA 2010 przy obliczaniu podstawy opodatkowania zastosowanie ma zasada terytorialności. Oznacza to, że podatnicy odprowadzają podatek jedynie od tych przychodów, które *powstały na terytorium* Gibraltaru *lub z tego terytorium pochodzą*.

Opodatkowaniu w Gibraltarze nie podlegają dywidendy, opłaty licencyjne i odsetki bierne (przychód z odsetek pochodzących z pożyczek udzielanych wewnątrz grupy). Odsetki podlegają jednak opodatkowaniu, jeśli zostaną uznane za zysk z działalności operacyjnej. Ma to miejsce w przypadku, gdy odsetki stanowią integralną część strumienia przychodów przedsiębiorstwa. Dotyczy to przedsiębiorstw działających w obszarze udzielania pożyczek pieniężnych na rzecz społeczeństwa (banki) lub przedsiębiorstw, które otrzymują odsetki od środków uzyskiwanych w wyniku działań polegających na przyjmowaniu depozytów, zgodnie z definicją zawartą w ustawie bankowej.

W dniu 7 czerwca 2013 r. władze gibraltarskie uchwaliły zmianę ITA 2010 dotyczącą opodatkowania odsetek. Zgodnie z uchwaloną zmianą wszystkie odsetki od pożyczek udzielanych między przedsiębiorstwami, zarówno krajowych jak i pochodzących z zagranicy, będą podlegać opodatkowaniu w zakresie, w jakim otrzymane odsetki przypadające na przedsiębiorstwo źródłowe przekroczą kwotę 100 000 GBP rocznie. Zmiana ta weszła w życie w dniu 1 lipca 2013 r.

OCENA ŚRODKA

Na obecnym etapie Komisja ma powody zakładać, że zwolnienie z podatku w odniesieniu do biernych odsetek i przychodów z opłat licencyjnych przewidziane w ITA 2010 r. stanowi pomoc państwa w rozumieniu art. 107 ust. 1 TFUE.

Istnienie powyższych korzyści oznacza zaangażowanie środków z zasobów państwowych w rozumieniu dochodów podakowych na rzecz gibraltarskiego skarbu, które zostały utracone. Zwolnienie dotyczące odsetek biernych oraz przychodów z opłat licencyjnych ma charakter selektywny, ponieważ stanowi odstępstwo od przedmiotowego systemu podatkowego (podatek dochodowy od osób prawnych) sprzyjające konkretnej grupie przedsiębiorstw, która otrzymuje takie przychody. Takiego odstępstwa nie uzasadnia charakter i ogólna struktura systemu podatkowego.

Występuje zakłócenie konkurencji i wpływ na wymianę handlową pomiędzy państwami członkowskimi, ponieważ wiele przedsiębiorstw posiadających siedzibę w Gibraltarze (oraz grup, do których należą) z dużym prawdopodobieństwem prowadzi działalność w sektorach, w których istnieje wymiana handlowa pomiędzy państwami członkowskimi.

Jeżeli chodzi o nową ustawę zmieniającą ITA 2010, nowe przepisy wydają się usuwać istnienie pomocy państwa w odniesieniu do zwolnienia dotyczącego odsetek biernych. Zmiany te nie wpływają jednak na ocenę pomocy państwa odnośnie do zwolnienia dotyczącego przychodów z opłat licencyjnych.

Żadne z odstępstw przewidzianych w art. 107 ust. 2 i 3 nie ma zastosowania, gdyż środek stanowi pomoc operacyjną niezwiązaną z realizacją konkretnych projektów oraz jedynie obniża bieżące wydatki beneficjenta, nie przyczyniając się do osiągnięcia żadnego celu unijnego.

Pomoc stanowi nową pomoc w rozumieniu art. 1 lit. c) rozporządzenia Rady (WE) nr 659/1999.

Zgodnie z art. 14 rozporządzenia Rady (WE) nr 659/1999, wszelka niezgodna z prawem pomoc może podlegać odzyskaniu od beneficjenta.

PISMO

„The Commission wishes to inform the United Kingdom that, having examined the information supplied by your authorities on the aid scheme referred to above, it has decided to initiate the procedure laid down in Article 108(2) of the Treaty on the Functioning of the European Union ("TFEU").

1. **PROCEDURE**

(1) On 1 June 2012, the Commission received a complaint from the Spanish authorities concerning the new income tax system in Gibraltar, as introduced by the Income Tax Act 2010 (ITA 2010). According to Spain, this new system would grant a *de facto* selective advantage to the offshore sector, constituting state aid within the meaning of Article 107(1) TFEU.

(2) By letter of 2 July 2012, the Commission forwarded the complaint to the United Kingdom, asked for comments and requested additional information.

(3) By letter of 14 September 2012, the United Kingdom provided detailed information on the Gibraltar reformed income tax system and its effect. A second request for information was sent on 25 October 2012 to which the United Kingdom replied on 3 December 2012.

On 8 January 2013, the Commission forwarded the non-confidential versions of the submissions to Spain. By letter of 8 March 2013, the Spanish authorities provided their comments. On 8 April 2013, the Commission forwarded the reply of Spain to the United Kingdom on which the United Kingdom commented on 30 April 2013.

(4) The United Kingdom provided further clarifications on a number of remaining issues on 18 April 2013. Spain provided clarifications on the notion of 'offshore' companies by letter of 26 April 2013. On 21 June 2013, the UK submitted further information on passive interest income and informed the Commission that the Gibraltar Government had amended the ITA 2010 with effect as of 1 July 2013.

(5) Meetings were held with the United Kingdom (including representatives of the Gibraltar authorities) on 24 October 2012 and 12 March 2013. Several meetings were also held with the Spanish authorities.

2. **FACTS**

2.1. **Description of the grounds for complaint**

(6) The Spanish authorities allege that the ITA 2010 constitutes State aid. They consider that the Gibraltar corporate tax system amounts to a *de facto* selective advantage for the offshore sector [1], through the combined effect of the application of the territorial system and the tax exemption for passive income. According to the Spanish authorities, this would lead to double non-taxation. The current tax system would have the same effect as the envisaged tax system which the Commission considered to be incompatible aid in its decision of 30 March 2004 [2], as upheld by the European Court of Justice [3]. Moreover, the Spanish authorities consider the Gibraltar corporate tax system to be regionally selective, as it differs largely from the main features of the corporate tax system applied in the United Kingdom.

2.2. **Description of the Gibraltar corporate tax regime**

2.2.1. *Status of Gibraltar*

(7) Gibraltar is a British overseas territory. It has full internal self-government with respect to tax matters, while the United Kingdom government is responsible for its international relations, for example for the negotiation of tax treaties. Though being regarded for the purposes of EU law as part of the United Kingdom, Gibraltar has a "dependent territory" status in the European Union.

2.2.2. *Income Tax Act 2010*

(8) The Income Tax Act 2010 ("ITA 2010") entered into force on 1 January 2011 and replaced the former Income Tax Act 1952. It was amended by the Income Tax (Amendment) Regulation 2013 [4] with effect from 1 July 2013.

(9) The ITA 2010 is based on a territorial system of taxation. The general corporate income tax rate is 10 %, with a special rate of 20 % for utility companies and companies that abuse a dominant market position.

Taxable persons

(10) Under the ITA 2010, all companies ordinarily resident in Gibraltar or branches of companies not ordinarily resident in Gibraltar (when they carry on a trade in Gibraltar through these branches) are subject to tax for their taxable income [5]. A company is ordinarily resident in Gibraltar if the management and control of its business is exercised in Gibraltar or if the company carries on a business in Gibraltar and the management and control of the business is exercised outside Gibraltar by persons ordinarily resident in Gibraltar.

Territorial system of taxation as applied in Gibraltar

(11) For the computation of the taxable base, the ITA 2010 applies the territorial principle. In case of the ITA 2010, this means that profits or gains of a company or trust from any trade, business, profession or vocation are only taxed if the income is *accrued in, or derived from* Gibraltar [6]. There is no capital gain tax in Gibraltar.

[1] Offshore companies are defined by Spain as companies which are not engaged in any activity or trade in Gibraltar (no income generated in Gibraltar), are not resident in Gibraltar, have practically no economic substance (employees, material means) and all or most of their income is passive income (dividends, interests and royalties) originating outside Gibraltar.

[2] OJ L 85, 2.4.2005, p. 1.

[3] Joined Cases C-106/09 P and C-107/09 P, *Commission and Spain v Government of Gibraltar and United Kingdom* [2011].

[4] Second supplement to the Gibraltar Gazette, No.4006 of 6 June, 2013.

[5] Other taxable persons are unincorporated associations, trusts, individuals trading in partnership or individuals.

[6] See section 11, paragraph (1) of Part II and table A of Schedule 1, ITA 2010.

(12) According to section 74 (a) of ITA 2010, income 'accrued in or derived from' is defined by reference to the location or the preponderance of the activities which give rise to the profits. In general, the location or the preponderance of the profit rising activities is determined on a case by case basis, depending on the specific facts and circumstance of the case. However, section 74 (b) provides for a legal presumption of territoriality for activities that require a licence in Gibraltar like activities performed by banks, insurance and gambling companies. Such activities are deemed to take place in Gibraltar. According to the UK, this provision has been introduced for the purpose of clarifying the territoriality principle for certain activities and to simplify the task of the Income Tax Office. However, even in the absence of section 74 (b), these activities would have been captured under the territoriality principle as a logic consequence of the legislative and administrative requirements [1] that a company needs to comply with in order to be granted a license in Gibraltar.

(13) With respect to cross-border activities which do not require a licence, the UK authorities explained that the Commissioner in Gibraltar is bound by the criteria established by the case law of British Commonwealth countries in the application of the territorial system. The general guiding principles followed by Gibraltar would be included in two leading judgments confirmed by the House of Lords (strictly, the Judicial Committee of the Privy Council), *Commissioner of Inland Revenue v Hang Seng (Hang Seng)* [2] and *Commissioner of Inland Revenue v HK-TVB International Ltd (HK-TVB)* [3]. According to these judgements, in assessing where a profit is accrued in or derived from, it needs to be considered (i) what the profit producing operations are, (ii) where they take place and (iii) what the tax payer has done to earn the profit. For example, in the last case, if the taxpayer has rendered a service, the place where the service was rendered will most probably be the place where the profits derive from. But in the case that the profits are earned by the exploitation of property, the profits will derive from the place where the property is situated.

(14) Apart from the guiding principles established by the case law, there are no instructions, administrative circulars or guidance notes in Gibraltar on how to apply the notion of territoriality. On request, the Gibraltar tax authorities may grant tax rulings confirming the tax treatment of a particular business activity or transaction.

The tax base and tax exemption for passive income under ITA 2010

(15) Irrespective of the source of the income, according to Article 11(1) in conjunction with Article 15 of Schedule 3 and Schedule 1, Table C of ITA 2010, dividends, royalties and passive interest) are not subject to tax in Gibraltar. However, interest is subject to tax if it is considered trading income ('trading interest income'). This is the case when the interest forms an integral part of the company's revenue stream. This applies to companies engaged in money lending activities to the general public (banks) or to companies that are in receipt of interest on funds derived from deposit taking activities as defined in the Banking Act [4].

(16) The notion of passive interest income therefore covers all interest income other than trading interest income. This includes mainly inter-company loan interest (of which the exemption is a new feature of the ITA 2010) but also the other categories of interest income which were already exempt before the adoption of the ITA 2010:

a. Interest paid or payable by a bank;

b. Interest paid or payable by the Gibraltar Government Savings Bank;

c. Income from debentures issued by a quoted company, including debenture stock, loan stock, bonds, certificates of deposit and any other instruments creating or acknowledging indebtedness including bills of exchange accepted by a banker other than instruments included in the below category;

d. Income from loan stock, bond and other instruments creating or acknowledging indebtedness issued by or on behalf of a public authority;

e. Income from units in a collective investment scheme which is marketed and available to the general public, including shares in or securities of an open-ended investment company.

(17) In theory, the notion of inter-company loan is broader than intra-group loan as it could also (at least in theory) include loans between unrelated companies (where the lender is not a bank or financial institution). However, in practice, loans between a (non-banking) Gibraltar company and an unrelated company would not occur.

2.2.3. *Objective of the tax system*

(18) In principle, the objective of the tax system is to introduce a general system of taxation for all companies established in Gibraltar. According to the UK, the overall objective of the corporate tax system in Gibraltar is to obtain tax revenues in an efficient way and, as a small tax administration, to ensure that tax is imposed in a manner which is administratively simple and where the expected revenue can be relied on to exceed the cost of collection.

[1] For example, the standard agreement for the granting of gambling licence requires that the operation, management and control of the entire licensed business shall be exercised from Gibraltar and that the core telecommunications services/equipment for the provision of the gambling activities must be situated in Gibraltar. The failure to maintain a physical presence in Gibraltar is a ground for not renewing a licence.

[2] CIR v Hang Seng Bank Limited [1991] 1 AC 306.

[3] CIR v HK-TVB International Limited [1992] 3 WLR 439.

[4] See section 15 of part III of schedule 3, ITA 2010.

2.2.4. *Repeal of the tax exemption for passive interest income*

(19) In response to the discussions on the ITA 2010 in the Code of Conduct Council Working Group on Harmful Business Taxation, which concluded that the non-taxation of foreign-source inter-company loan interest is a harmful aspect of the ITA 2010, the Gibraltar authorities have enacted an amendment of their legislation on 7 June 2013 with effect on 1 July 2013. With the amendment, all inter-company loan interest income, both domestic and foreign-sourced, will be subject to tax in as far as the interest received per source company [1] exceeds an amount of £ 100,000 per annum. According to the UK authorities this amendment will apply to approximately 99 % of all inter-company loan interest paid whilst remaining consistent with the stated objective of ensuring that the system is administratively simple. Also the reference to the 'preponderance of activities' was deleted from the law as (i) the preponderance criterion seemed to cause confusion with regard to the notion of territoriality and (ii) the outcome of the territoriality assessment would not be different without the criterion.

3. POSITION OF UNITED KINGDOM

(20) According to the UK, the current corporate tax system in Gibraltar does not amount to a selective advantage of certain companies or sectors. It argues that the corporate tax system is based on the principle of territoriality, which is an internationally accepted tax system and the logical choice in a small jurisdiction like Gibraltar, which has no double taxation agreements with other countries. The principle would avoid double taxation and lead to simplification. The system applies to all companies and all sectors and would therefore be general in nature. The UK points out that the territorial tax system was introduced in Gibraltar already in 1952 and that the Commission, when it examined the Gibraltar corporate tax system in the past, never questioned the territoriality system as such under the state aid rules. The UK further argues that the foreign source passive interest income exception would in any event arise from the normal application of the territorial system and should therefore not be regarded as selective. Should the tax exemption for passive interest income be selective, the UK is of the opinion that it should be considered existing aid.

(21) In more detail, the UK explain that before the ITA 2010 came into effect, the application of the territoriality principle to interest income was determined by reference to the "situs of the loan". The UK submitted that the Gibraltar Tax Commissioner had to consider the following factors (these factors are meant to implement the territorial principle for such income):

— The place of residence of the debtor;

— The source from which the interest was paid;

— The place where the interest was paid; and

— The nature and location of the security for the debt.

(22) If all four factors were in Gibraltar, then the 'situs' of the loan was in Gibraltar (and under the 1952 Act passive interest was taxable in Gibraltar). If one or more factors were outside Gibraltar the 'situs' was decided in the light of the facts. In practice the fourth factor, the location of the security of the debt, was usually the most important. According to the UK, the effect of these rules was that only intra-group financing between Gibraltar companies were taxable under the 1952 Act.

(23) According to the UK, even in combination with the exemption for passive income, the tax system could not favor offshore companies now that these companies do no longer exist since the qualifying and exempt companies were abolished as from 24 February 2005 [2] and 1 January 2011 [3] respectively.

4. ASSESSMENT OF THE ITA 2010

4.1. Existence of aid

(24) The ITA 2010 has been in place since 1 January 2011. The Commission at this stage has reasons to assume that some of the derogations granted under the ITA 2010 do constitute State aid pursuant to Article 107 (1) TFEU.

(25) Article 107 (1) TFEU states that "any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods shall, insofar as it affects trade between Member States, be incompatible with the internal market".

(26) It follows that in order to be qualified as State aid, the following cumulative conditions have to be met: 1) the measure has to be granted out of State resources, 2) it has to confer an economic advantage to undertakings, 3) the advantage has to be selective and distort or threaten to distort competition, 4) the measure has to affect intra-Community trade. With respect to tax measures, selectivity is generally considered as the main criterion in applying Article 107(1) TFEU [4]. The selectivity criterion has been assessed at both a material and geographical (or regional) level.

4.1.1. *Material selectivity*

Scope of assessment

(27) According to settled case-law, the material selectivity of tax measures should normally be assessed by following a three step analysis [5]. Firstly, the system of reference has to be

[1] Interest received from different companies will be considered to be from the same source company if the different companies are connected persons.

[2] State Aid C52/2001 – United Kingdom, Gibraltar Qualifying Companies, Decision of 30 March 2004, C(2004) 928), OJ L 29, 2.2.2004, p. 24. See also Income Tax (Amendment) Ordinance 2005, No. 3457 of 24 February 2005.

[3] State Aid E 7/2002 (ex C53/2001 & NN52/2000) – United Kingdom, Proposal for appropriate measures under Article 88(1) of the EC Treaty concerning Gibraltar exempt companies, C(2004)2687.

[4] See Commission Notice on the Application of the State Aid Rules to Measures relating to Direct Business Taxation, OJ C 384, 10.12.1998, p.3.

[5] See e.g. Joined Cases C-78/08 to C-80/08, *Paint Graphos and others* [2011], paragraph 49 et seq.

identified. Secondly, it should be determined whether a given measure constitutes a derogation from this system insofar as it differentiates between economic operators who, in light of the objective intrinsic to that system, are in a comparable factual and legal situation. If the measure in question does (and therefore is *prima facie* selective), it still needs to be verified in the last step of the test whether the derogatory measure is justified by the nature or the general scheme of the (reference) system [1]. If a *prima facie* selective measure is justified by the nature or the general scheme of the system, it will not be considered selective and thus fall outside the scope of Article 107(1) TFEU.

(28) Nevertheless, it must be emphasised that Article 107(1) TFEU does not distinguish between measures of State intervention by reference to their causes or their aims, but defines them in relation to their effects and thus independently of the techniques used [2]. This means that, in certain exceptional circumstances, it is not sufficient to examine whether a given measure derogates from the rules of the system of reference as defined by the Member State concerned, but it is also necessary to evaluate whether the boundaries of the system of reference have been designed in a consistent manner or, to the contrary, in a clearly and arbitrary or biased way, so as to favour certain undertakings which are in a comparable situation with regard to the underlying logic of the system in question.

(29) In the present case, it appears that the passive income exemption measure introduced by the ITA 2010 constitutes a derogation from the system of reference. This derogation is not justified by the nature or the general scheme of the reference system.

The system of reference

(30) The system of reference normally constitutes the framework against which the selectivity of a measure is assessed. It is composed of a consistent set of rules generally applicable – on the basis of objective criteria - to all undertakings falling within its scope as defined by its guiding principle.

(31) In the case at hand, the reference tax system must be defined as the Gibraltar corporate income tax as introduced by the ITA 2010, which applies to all resident companies in Gibraltar (as well as to non-resident companies carrying on a trade in Gibraltar through a branch or agency). The guiding principle of this system would consist in levying taxes on all these undertakings generating income accruing in or derived from Gibraltar, avoiding double taxation and leading to simplification. The UK authorities point out that this system is adapted to a small jurisdiction like Gibraltar, which has no double taxation agreements with other countries.

The passive income exemption

(32) In accordance with the above mentioned territoriality principle, only income accruing in or derived from Gibraltar is subject to taxation. However, passive income (interest, dividends or royalty) is not taxable in Gibraltar, with the exception of interest income forming an integral part of the company's revenue stream.

(33) The above tax exemption measure applies regardless of both the source of the income and the location where the company's relevant activities take place (inside or outside Gibraltar). Given that companies are exempted from taxation on the basis of the type of income, i.e active (i.e. profits) vs. passive (interest, dividends or royalty), the exemption differentiates between certain kinds of income and must at this stage be considered prima facie selective.

(34) In addition, the derogation in question differentiates between companies which, in light of the objective intrinsic to that system, are in a comparable factual and legal situation. Considering the objective of the Gibraltar tax system which is to tax all companies generating income accruing in or derived from Gibraltar, companies in receipt of passive interest, royalty or dividend income are in a similar legal and factual situation as other companies falling into the scope of the Gibraltar tax system. The passive income exemption therefore seems to be *prima facie* selective.

(35) Moreover, the Commission at this stage considers that in particular the passive interest income exemption does not as such follow from the territorial system. In fact the passive income exemption in the ITA 2010 differs from the territorial system in place before the adoption of the ITA 2010 insofar as there was no outright exemption for passive interest, but a case-by-case assessment of the "situs" of the loan, with an inevitable margin of discretion in applying the criteria referred to in paragraph 22. Similarly, concerning the exemption of passive income derived from royalties, the Commission notes that it favours a specific group of undertakings, namely companies that obtain revenue from intellectual property rights. Such an exemption is not in line with the territoriality principle and indeed it appears that revenues derived from royalties were normally taxed under the general territoriality principle prior to the entry into force of the ITA 2010.

(36) The UK authorities themselves state that, under the former exempt companies scheme, by obtaining an exempt status, a company would obtain absolute legal certainty that it was not subject to tax in Gibraltar, which implies that such certainty would not be available through the application of the normal rules. ITA 2010 therefore introduced a de jure derogation from the territoriality principle, by exempting from taxation all passive interests (both from domestic and foreign sources) and all revenues derived from royalties.

[1] See e.g. Case C-279/08 P, *Commission v Netherlands (NOx)* [2011], paragraph 62, Case T-210/02 RENV, *British Aggregates Association v Commission* [2012], paragraph 83, Joined Cases C-78/08 to C-80/08, *Paint Graphos and others* [2011], paragraph 69 et seq. Sometimes the Court refers also to justification by "the logic of the system", see e.g. Case C-53/00, *Ferring*, [2001] ECR I-9067, paragraph 17.

[2] See case C-487/06 P, *British Aggregates* v *Commission*, [2008] ECR I-10515, paragraphs 85 and 89 and the case-law cited; Case C-279/08 P *Commission* v *Netherlands* [2011], paragraphs 51; Joined Cases C-106/09 P and C-107/09 P, *Commission and Spain v Government of Gibraltar and United Kingdom* [2011], paragraph 87.

(37) Selectivity can also be established in cases where the structure of the measure is such that its effects significantly favour a particular group of undertakings (*de facto* selectivity). In the case at hand, the passive income exemption might be found *de facto* selective as the measure seems to significantly favour a group of 529 companies in receipt of passive income, in particular interests from other companies of the same group or royalties for intellectual property rights. The measure therefore seems to favour a specific group of companies, namely companies providing loans to related companies or receiving royalty income for intellectual property rights. Such *de facto* selectivity is confirmed by the quantitative effects of the measure concerning the exemption of interest. The figures provided by the UK authorities for 2011 show that, of the total amount of inter-company loan interests received by Gibraltar companies (£ 1 400 million), the largest part (99.8 %) derives from loans granted to foreign (group) companies, in particular from non-EU countries (76 %). This seems to demonstrate that the measure would mainly benefit intra-group financing companies providing loans to foreign related companies, ([1]) which can be considered as a privileged group of companies. Given that Gibraltar previously exempted those companies under the former exempt companies scheme ([2]) (definitely repealed by the end of 2010 after being found as not state aid compliant), and further envisaged to introduce a new taxation system favouring offshore companies ([3]), the new passive income exemption, seen against the background of the territorial system, seems to re-establish the effect that companies providing loans to other companies of the same group, and in particular offshore companies exercising such activities, continue to benefit from zero taxation.

The absence of justification by the nature or the general scheme of the reference system

(38) A measure which derogates from the system of reference (prima facie selectivity) may be still found to be non-selective if it is justified by the nature or general scheme of that system. Such is the case where a measure results directly from the intrinsic basic or guiding principles of the reference system or where it is the result of inherent mechanisms necessary for the functioning and effectiveness of that system. On the contrary, external policy objectives which are not inherent to the system cannot be relied upon for that purpose.

(39) The exemption of domestic and foreign-source dividends would seem to be justified by the logic of preventing double taxation of such income as dividends are in principle paid out of taxable profits (either in Gibraltar or in the foreign source country). By contrast, the tax exemption for interest and royalty income does not follow any such logic. Despite the possible application of anti-abuse rules in the source country, the corresponding interest or royalty payment usually constitutes a deductible expense at the level of the paying company.

(40) The UK authorities submit that as regards foreign source passive interest income, the non-chargeability to tax would arise from the logic of a normal application of the territorial system and should therefore not be regarded as selective. At this stage, the Commission does not find this argument convincing. Under the territoriality principle, only income of intra-group financing companies the activity of which is not preponderantly taking place in Gibraltar would fall outside the charge of taxation in Gibraltar, not the income of financing companies performing such activity in Gibraltar. Thus, the measure as enacted by the Gibraltar authorities does not correspond to the alleged logic of the system.

(41) With respect to foreign source interest, the UK authorities have also explained that the application of the territoriality principle to interest income would be determined by reference to the "situs of the loan" ([4]).

(42) The Commission notes that, while the territoriality principle as such relies on the location and preponderance of the activities performed by a Gibraltar company, the criteria allegedly applied in order to determine the "situs of the loan" do not seem to conform to the same principles. In particular, the place of residence of the debtor, the source from which the interest is paid and the nature and location of the security for the debt do not appear, in principle, to be relevant for such purposes. In any event, as indicated above, the application of the territoriality principle would need to be assessed on a case-by-case basis, without automaticity, while the passive interest exemption is automatic.

(43) In the case of domestic source passive interest, the UK authorities have claimed that the non-chargeability to tax should be regarded either as the result of the application of the reference system or a derogation from that system which is justified by the nature and logic of all general taxation that, in accordance with normal economic rationale, the cost for collecting tax to finance public expense must not be likely to exceed the potential tax yield (estimated £ 2.5 million of domestic source interest income that would yield, at most, £ 250,000 in tax). In the Commission's view, this cost efficiency reasoning is not convincing either. If, in the absence of the measure, foreign source passive interest income was subject to the territorial principle and therefore taxable where it was derived from or accruing in Gibraltar, extending tax liability to domestic ones would not seem to involve disproportionate costs in terms of assessment and control. In addition, the UK authorities' reasoning is not based on a single consistent logic applying to both domestic and foreign source income but on two different logics.

([1]) With respect to the number of benefitting companies, the UK authorities have explained that of the total amount of passive interest income (£ 1 400 million), £ 1 381 million arose from 137 companies with the balance of £ 18.34 million spread over a further 400 companies. Within the grouping of 137 companies, there was a single company that accounted for £ 1 000 million in interest.

([2]) Exempt companies were essentially companies that did not carry out any trade or business in Gibraltar and were not owned by Gibraltar residents. These companies were exempt from corporate tax. In 2001 the Commission initiated proceedings under the state aid rules in respect of a specific tax regime put in place for such companies, which regime was considered to favour the offshore sector. As a result, Gibraltar definitively abolished this scheme by the end of 2010 and today there are no exempt companies in Gibraltar anymore.

([3]) See Joined Cases C-106/09 P and C-107/09 P, *Commission and Spain v Government of Gibraltar and United Kingdom* [2011].

([4]) See above, paragraphs 22 and 23.

(44) As to the exemption for royalty income, the UK authorities have indicated that the territorial system of taxation would determine that all royalty income received by a Gibraltar company accrues and derives in Gibraltar. For the taxation of royalties to be effective, the Income Tax Office in Gibraltar would have to put in place a verification and anti-avoidance system allowing it to properly assess the amount of royalty income to be taxed. In addition, the whole area of royalties and intellectual property would be very sophisticated and issues of licensing, sublicensing, amortisation, and fair value and these would require an expertise well beyond those presently available in Gibraltar. Furthermore, and in any event, the UK authorities argue that when royalties were still taxed under the 1952 Act, it did not give rise to a significant tax yield. For this reason royalties were excluded from the heads of charge when the 2010 Act was enacted.

(45) The Commission considers however that the requirement to make the Gibraltar tax system simple and effective cannot be seen a valid justification (based on the guiding principles of the Gibraltar tax system) for not taxing royalties. In particular, the taxation of royalties would not require a verification and anti-avoidance system more sophisticated than for other categories of income which may equally require verification and anti-avoidance rules to prevent shifting of taxable profits. On the contrary, the exemption of such royalty income would seem to require verification and anti-abuse rules, in particular to avoid the shifting of profits between Gibraltar companies. Finally, when looking at the amount of royalty income received by Gibraltar companies in 2011 (£ 90 million), the Commission doubts the UK's reasoning that the taxation of royalties would not give rise to a significant tax yield.

(46) In conclusion, although a justification may be found for certain aspects of the tax measures concerned (e.g. the prevention of double taxation may justify the exemption of dividends), no overall logic justifying the exemption for passive interest and royalty income has been found.

Conclusion on material selectivity

(47) It follows from the analysis of the passive income exemption that both the exemption for passive interest income and royalties appear to be *de jure* and *de facto* selective. No overall logic justifying such exemptions could so far be identified.

4.1.2. *Regional selectivity*

(48) In the light of the relevant case-law, the Commission does not see any reason to assume that the system is also regionally selective.

(49) In principle, only measures whose scope extends to the entire territory of the State escape the selectivity criterion laid down in Article 107(1) TFEU. However, as outlined below, the system of reference does not necessarily need to be defined within the limits of the Member State concerned ([1]). A measure favouring undertakings active in a part of the national territory should therefore not be automatically considered selective.

(50) As established by the Court of Justice in the *Azores* ([2]) judgment and further developed in the *Unión General de Trabajadores de La Rioja* ([3]) judgment, measures with a regional or local scope of application may escape the geographical selectivity criterion if certain requirements are fulfilled.

(51) Where a regional authority can adopt tax measures applicable within its territory, the assessment of the selective nature of the measure in question depends on whether the authority at stake is sufficiently autonomous from the central government of the Member State ([4]). The regional or local authority shall be considered sufficiently autonomous from the central government of the Member State if it plays a fundamental role in the definition of the political and economic environment in which the undertakings operate ([5]). This is the case when three cumulative criteria of autonomy are fulfilled: institutional, procedural and economic autonomy ([6]). If all of these criteria of autonomy are present when a regional or local authority decides to adopt a tax measure applicable only within its territory, then the geographical framework of reference is constituted by the territory of the region in question and not by that of the Member State.

(52) In its judgment of 18 December 2008 in Joined Cases T-211/04 and T-215/04, the General Court found that Gibraltar met the three cumulative autonomy criteria established by the Azores case-law ([7]) (institutional, procedural and financial autonomy). Accordingly, it concluded that the reference framework corresponds exclusively to the geographical limits of the territory of Gibraltar. That finding of the General Court, although challenged by Spain in its appeal, was not reviewed by the Court of Justice.

(53) With respect to the institutional autonomy, the General Court merely stated that the competent Gibraltar authorities which have devised the tax reform have, from a constitutional point of view, a political and administrative status separate from that of the central government of the United Kingdom and that, accordingly, the first condition is met ([8]).

([1]) Case C-88/03 *Portugal v Commission* [2006] ECR I-7115, paragraph 57, Joined Cases C-428/06 to C-434/06 *Unión General de Trabajadores de La Rioja*, [2008] ECR I-6747, paragraph 47.

([2]) Case C-88/03 *Portugal v Commission* [2006] ECR I-7115 [2006] ECR I-7115, paragraphs 57 et seq.

([3]) Cases C-428/06 to C-434/06 *Unión General de Trabajadores de La Rioja* [2008] ECR I-6747, paragraphs 47 et seq.

([4]) Case C-88/03 *Portugal v Commission* [2006] ECR I-7115, paragraph 58: "*it is possible that an infra-state enjoys legal and factual status which makes it sufficiently autonomous in relation to the central government of a Member State, with the result that, by the measures it adopts, it is that body and not the central government which plays a fundamental role in the definition of the political and economic environment in which undertakings operate.*"

([5]) Joined cases C-428/06 to C-434/06 *Unión General de Trabajadores de La Rioja* [2008] ECR I-6747, paragraph 55.

([6]) Case C-88/03 *Portugal v Commission* [2006] ECR I-7115, paragraph 67.

([7]) C-88/03 Portugal v Commission.

([8]) See Joined cases T-211/04 and T-215/04, paragraph 89.

(54) Regarding the procedural autonomy criteria, the General Court concluded that the United Kingdom's residual power to legislate for Gibraltar and the various powers granted to the Governor must be interpreted as means enabling the United Kingdom to assume its responsibilities towards the population of Gibraltar and to perform its obligations under international law, and not as granting an ability to intervene directly as regards the content of a tax measure adopted by the Gibraltar authorities, in particular since those residual powers have never been exercised in matters of taxation ([1]).

(55) Finally, the General Court held that the financial autonomy criterion was met as Gibraltar does not receive any financial support from the United Kingdom that offsets the financial consequences of the tax reform ([2]). In particular, it found that the mere existence of financial transfers from the UK central government to Gibraltar is not sufficient to violate the third criterion.

(56) As far as the Commission is aware of, Gibraltar's situation as regards the three autonomy criteria has not changed since the above referred judgment of the General Court. In the absence of any changes in its political, administrative and financial status ([3]), Gibraltar must be seen as a sufficiently autonomous region for the above-mentioned reasons.

(57) In this context, the reference framework corresponds exclusively to the geographical limits of the territory of Gibraltar and so no regional selectivity can be identified on the ground that the tax regime applies to Gibraltar only.

4.1.3. *State resources*

(58) The use of State resources can also follow from the loss of tax revenue. Since the non-liability to tax for companies in receipt of passive interest and royalty income results in a loss of tax revenue that otherwise would have been available to Gibraltar, it can be concluded that the scheme is financed through State resources. ([4])

4.1.4. *Advantage*

(59) According to the case-law, the concept of aid embraces not only positive benefits, but also measures which in various forms mitigate the charges which are normally included in the budget of an undertaking ([5]).

(60) Therefore, since the tax exemption for passive interest and royalty income reduces the charges that are normally included in the operating costs of these companies incorporated in Gibraltar, it seems to provide an economic advantage to the benefitting companies in comparison to other companies which cannot benefit of such tax advantages.

([1]) See paragraphs 90-99.
([2]) See paragraphs 101-113.
([3]) The UK has confirmed that Gibraltar receives no subsidy or financing of any kind from the UK. Gibraltar raises all its revenue from its own taxation.
([4]) Joined Cases C-106/09 P and C-107/09 P, *Commission and Spain v Government of Gibraltar and United Kingdom* [2011], paragraph 72.
([5]) Case C-143/99, Adria-Wien Pipeline, ECR 2001, I-8365, point 38.

4.1.5. *Effect on trade and competition*

(61) Many of the companies established in Gibraltar (and the groups to which they belong) are likely to be active in sectors where there is trade between Member States. The Court of Justice has repeatedly ruled that when aid granted by the State strengthens the position of an undertaking vis-à-vis other undertakings competing in intra-Community trade, the latter must be regarded as affected by that aid. For that purpose, it is not necessary for the recipient undertaking itself to export its products. Where a Member State grants aid to an undertaking, domestic production may for that reason be maintained or increased with the result that undertakings established in other Member States have less chance of exporting their products to the market in that Member State. Similarly, where a Member State grants aid to undertakings operating in the service and distribution industries, it is not necessary for the recipient undertakings themselves to carry on their business outside the Member State for the aid to have an effect on Community trade, especially in the case of undertakings established close to the frontier between two Member States. The relatively small amount of aid, or the relatively small size of the undertaking which receives it, does not as such exclude the possibility that intra-Community trade might be affected ([6]). Therefore to the extent that Gibraltar companies, benefiting from the advantages described in paragraphs 16-18, operate in sectors where intra-Community trade takes place, it would appear that the aid affects trade between Member States and thereby threatens to distort competition.

4.1.6. *Conclusion on the existence of aid*

(62) The Commission concludes, at this stage, that the tax exemptions for passive interest and royalty income constitute State aid within the meaning of Article 107(1) TFEU.

4.1.7. *New aid*

(63) Although under the former system (1952 Act), foreign source passive interest income might not have been taxed as a result of the territoriality principle or might have benefitted from certain specific exemptions, it remains that the exemption for inter-company loan interest income from a foreign source was not granted automatically (as is the case under the 2010 Act) and required the assessment of territoriality.

(64) The non-chargeability to tax of domestic passive interest income also constitutes a new feature of the ITA 2010 (new Article 15 of Schedule 3 of ITA 2010). Although some exemptions for such income may have been granted initially (in 1952) as a result of a policy decision, legislative amendments were introduced in 2005 with the result that inter-company loan interest was not part of the consolidated list of exempted items of interest income. In other words, the domestic inter-company loan interest income was taxed under the 2005 legislative amendment. Such interest was finally excluded from taxation by the 2010 Act (Article 15 of Schedule 3).

([6]) See cases 730/79 *Philip Morris v Commission* [1980] ECR 2671, 142/87, *Belgium v Commission* [1990] ECR I-959, joined cases C-278/92, C-279/92 and C-280/92 *Spain v Commission* [1994] ECR I-4103, paragraphs 40-42 and case C-310/99 *Italy v Commission* [2002] ECR I-2289, paragraphs 84-86.

(65) Furthermore, as indicated by the UK authorities, the application of the territoriality principle determines that all royalty income received by a Gibraltar company accrues in and derives from Gibraltar. Such income was only excluded from taxation by the 2010 Act.

(66) It follows that the exemption rule for passive (inter-company loan) interest and royalty income cannot be seen as a mere continuation of the previous system but involves a substantial alteration of the tax regime for such income. In this context, the State aid which results from the exemption of inter-company loan interest and royalty income must be seen as new aid [1].

(67) In any event, the passive interest income exemption should be considered as new aid at least insofar as it concerns those incomes that were taxable before the entry into force of the ITA 2010.

4.1.8. *Compatibility of aid*

(68) As the measure appears to constitute State aid, it is therefore necessary to determine if such aid is compatible with the internal market. State aid measures can be considered compatible on the basis of the exceptions laid down in Article 107(2) and 107(3) TFEU.

(69) So far, the Commission has doubts as to whether the measures in question can be considered compatible with the internal market. The UK authorities did not present any argument to indicate that any of the exceptions provided for in Article 107 (2) and 107 (3) TFEU, under which State aid may be considered compatible with the internal market, applies in the present case.

(70) The exceptions provided for in Article 107 (2) TFEU, which concern aid of a social character granted to individual consumers, aid to make good the damage caused by natural disasters or exceptional occurrences and aid granted to certain areas of the Federal Republic of Germany, do not seem to apply in this case.

(71) Nor does the exception provided for in Article 107 (3) (a) TFEU apply, which provided for the authorisation of aid to promote the economic development of areas where the standard of living is abnormally low or where there is a serious unemployment, and of the regions referred to in Article 349 TFEU, in view of their structural, economic and social situation. Such areas are defined by the UK's regional aid map [2]. Since Gibraltar is not such an area, this provision does not apply.

(72) As regards the exceptions laid in Article 107 (3) (b) and (d) TFEU, the aid in question is not intended to promote the execution of an important project of common European interest nor to remedy to a serious disturbance in the economy of the UK, nor is it intended to promote culture or heritage conservation.

(73) Aid granted in order to facilitate the development of certain economic activities or of certain economic areas could be considered compatible where it does not adversely affect trading conditions to an extent contrary to the common interest, according to Article 107 (3) (c) TFEU. At this stage however, the Commission has no elements in order to assess whether the tax advantages granted by the measure under examination are related to specific investments eligible to receive aid under the Community rules and guidelines, to job creation or to specific projects. The Commission considers on the contrary, that the measures in issue seem to constitute a reduction of charges that should normally be borne by the entities concerned in the course of their business, and should therefore be considered as operating aid. According to the Commission practice, such aid cannot be considered compatible with the internal market in that it does not facilitate the development of certain activities or of certain economic areas, nor are the incentives in question limited in time, digressive or proportionate to what is necessary to remedy to a specific economic handicap of the areas concerned. In addition Gibraltar is not included in the regional aid map for the United Kingdom for the period 2007 to 2013, as approved by the Commission under State aid N673/2006.

5. **ASSESSMENT OF THE ITA 2013**

(74) As described in paragraph (19), an amendment of the ITA 2010, which entered into force on 1 July 2013, introduces that all inter-company loan interest income received after 1 July 2013, both domestic and foreign-sourced, will be subject to tax in as far as the interest received per source company exceeds an amount of £ 100,000 per annum.

(75) The amendment seems to remove the existence of State aid with respect to the passive (inter-company loan) interest exemption. In particular, the Commission considers that the exemption of interests received per source company not exceeding an amount of £ 100,000 per annum can be regarded as a legitimate simplification measure, as confirmed by the figures provided by the United Kingdom, according to which approximately 99 % of all inter-company loan interest paid would now be subject to taxation. On the contrary, the amendment does not affect the assessment of material selectivity regarding the exemption of royalty income.

(76) The other criteria for the assessment of the existence of aid are not affected by the July 2013 amendment either. Against this background, the Commission concludes, at this stage, that the exemption rule for passive (inter-company loan) interest constitutes State aid only with respect to the application of the rule before the entry into force of the amendment enacted by the Income Tax (Amendment) Act of 7 June 2013. By contrast, the royalty exemption still constitutes State aid within the meaning of Article 107(1) TFEU.

(77) The findings on compatibility laid down in paragraph (69) to (74) apply equally to the 2013 amended tax system.

[1] Joined Cases T-195/01 and T-207/11, *Governement of Gibraltar* v *Commission*, para. 111

[2] OJ C 55, 10.03.2007, p. 2.

6. **CONCLUSION**

In the light of the foregoing considerations, the Commission's preliminary view is that the exemption rule for passive (inter-company loan) interest and royalty income resulting from ITA 2010 constitutes a State aid measure according to Article 107(1) TFEU and has doubts about it compatibility with the internal market. The Commission has therefore decided to initiate the procedure laid down in Article 108(2) TFEU with respect to the measures in question. As far as the exemption relates to royalty income, the Commission takes the same view and the same Decision concerning the Income Tax Act 2010 as amended by the Income Tax Regulation 2013.

The Commission wishes to remind the United Kingdom that Article 108 (3) TFEU has suspensory effect, and would draw your attention to Article 14 of Council Regulation (EC) No. 659/1999, which provides that all unlawful aid may be recovered from the recipient.

The Commission invites the UK authorities to transmit immediately copy of the present decision to all (potential) beneficiaries of the aid, or at least to proceed to inform them with appropriate means.

The Commission informs the United Kingdom that it will inform interested parties by publishing this letter and a meaningful summary of it in the Official Journal of the European Union. It will also inform interested parties in the EFTA countries which are signatories to the EEA Agreement, by publication of a notice in the EEA Supplement to the Official Journal of the European Union and will inform the EFTA Surveillance Authority by sending a copy of this letter. All such interested parties will be invited to submit their comments within one month of the date of such publication."