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Article

Analysis of the (In)compatibility of Digital Services Taxes With State Aid Rules

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After the recent agreements at a global level, some Member States of the European Union have paused their plans for Digital Services Taxes. However, others have decided to move forward with them as the global political agreement reached, while encouraging, has not been implemented yet. Therefore, it is still relevant to understand the nature of such taxes and, more importantly in the context of the EU, their possible (in)compatibility with state aid rules.

The purpose of this article is to shed light into these measures in a manner that encompasses all possible taxes. To establish the possible incompatibility of the taxes, an analysis is made passing through all the conditions for a measure to be considered as state aid and giving particular importance to the notion of selective advantage, which will be the determining factor if the Court of Justice of the European Union (CJEU) ever must pronounce itself on this matter.

Keywords: Digital Services Taxes, State aid, Fiscal State aid, Selective Advantage, European Union, European Commission, Court of Justice of the European Union, Unilateral measures, OECD

1 Introduction

In the last decade, the revolution of the digital economy has affected all sectors and has exposed the need to reform the 'outdated'[1] international taxation system to respond to the new business models. Given the magnitude of the changes needed and the effects of globalization which require a common solution, the consensus regarding the way forward was searched, in the first moment, at an international level, namely in the Organisation for Economic Cooperation and Development (OECD). In that regard, it is noteworthy the 'overwhelming consensus that the international tax regime needs to be reshaped',[2] but also the lack of agreement on how to do so. As a direct consequence of this absence of consensus at an international level, several 'unilateral and uncoordinated actions'[3] have been adopted both at a regional and national level in the form of Digital Service Taxes (DST).

Member States have autonomy in the design of their own taxation systems as they retain sovereignty over taxation. However, EU law and, particularly for the purpose of this article, its state aid rules, can and must be considered to ensure that Member States do not fragment the Internal Market and distort competition intra-EU. It is worth mentioning that, while state aid rules may be applicable to control taxation, they '[are] not a panacea which can be used to cure all defects of tax legislation',[4] as a way to circumvent the lack of competence of the EU in these matters.

In this context, this article tries to answer whether it can be claimed that these DST are incompatible with state aid rules. To do so, I recall the proposals of the OECD and the EU (section 2), as the national DST are greatly inspired by the latter one and share the main characteristics that will be analysed later. Afterwards, I perform a step-by-step examination of all the conditions required for a tax to be considered as state aid (section 3), with a special focus on the criterion of 'selective advantage' (section 4), relying primarily on the latest jurisprudence of the Court of Justice of the European Union (CJEU). Finally, I summarize the main points that lead to answering the main issue of the article (section 5).

2 From the OECD's and EU's (failed) proposals to the national DST: A 'patchwork' of unilateral responses?

The expansive and swift nature of digital transformation has resulted in significant changes in the economy and in society worldwide. The advances in this field have derived in a new way to do business which has great

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1 M. de Wilde & C. Wisman, *OECD Consultations on the Digital Economy: 'Tax Base Reallocation' and I'll Tax If You Don't?*, in *Taxing the Digital Economy: The EU Proposals and Other Insights* 1–23 at 5 (P. Pistone & D. Weber eds, IBFD 2019).

2 W. Schön, *Ten Questions About the Why and How to Tax the Digitalized Economy*, 11 Max Planck Inst. Tax L. & Pub. Fin. 1 (2017).

3 OECD, *Base Erosion and Profit Shifting Project. Tax Challenges Arising from Digitalisation – Interim Report 2018* (2018).

4 Schön, *supra* n. 2, at 23.

implications for the tax systems all over the world. Particularly, digitalization has facilitated the internationalization of enterprises, which difficulties the allocation of their profits. Also, it has increased the changeability of profits to lower tax jurisdictions, as well as made easier for Multinational Enterprises (MNE) selling their products in jurisdictions where they have minimal or no physical presence at all.[5]

The companies that have benefited the most are known as the 'Technological Giants', which have been enjoying great advantages from a fiscal point of view in comparison to the traditional enterprises through intensive tax planning,[6] namely because the tax systems until now had not foreseen this new model of business with minimum or no physical presence. This problem has global consequences and, thus, requires a global answer which has not been found yet.

A full analysis of the origins of the OECD's and EU's attempts to solve the situation over the last decade is beyond the scope of this article. Nevertheless, it is worth highlighting that, in 2021, more than 130 countries (including the US) agreed on a global minimum tax of 15%.[7] This consensus is supposed to be translated in the short term to the DST disappearing, as some European governments have already indicated.[8] However, given the timeline until the agreement was reached and the reluctance that some countries have expressed,[9] it seems prudent to not rule out that DST will continue existing or come into force over the next few years, and the issues that may arise from them still need to be analysed.

At an EU level, the Commission made two legislative proposals in 2018 planned with different timelines. The first one was a long-term plan aimed to reform corporate tax rules so that profits are taxed where business, through digital channels, have significant interaction with users, introducing the concept of 'significant digital presence'.[10] The second proposal, and the one that affects us more in depth, was an *interim* measure that, by its own nature, was meant to be a short-term solution to a very pressing matter: the Directive on the common system of a digital services tax on revenues resulting from the provisions of certain digital services (Digital Services Tax Directive, DSTD).[11]

The characteristics of the DSTD are of interest as most of the DST proposed by the Member States share them. It has a targeted scope and would only apply to revenues which were not being totally or partially taxed under the current framework, and that derived from certain digital activities.[12] The taxable revenues are: (1) user-targeted advertising on a digital interface; (2) intermediation services through multi-sided digital interfaces; and (3) the transmission of collected user data.[13]

Furthermore, the taxable person is also quite restricted as the entity in question needs to surpass two revenue thresholds in the relevant financial year: (1) having a total worldwide revenue superior to EUR 750 million[14]; and (2) obtaining more than EUR 50 million within the EU (Article 4 DSTD). The tax will be applied at a 3% rate (Article 8 DSTD), which had been estimated to generate more than EUR 5 billion in revenues yearly for the Member States.

As a reaction to the comings and goings of both the international community and the Member States, various of the latter have adopted unilateral taxes with the aim of covering this great legal gap the international taxation system has.[15] These unilateral measures can be grouped in three categories: (1) digital services taxes (DST); (2)

[5] M. P. Devereux & J. Vella, *Implications of Digitalization for International Corporate Tax Reform* 5–7 (Oxford University Centre for Business Taxation 2017).

[6] *Ibid.*, at 3.

[7] OECD, *International Community Strikes a Ground-Breaking Tax Deal for the Digital Age* (8 Oct. 2021), https://www.oecd.org/tax/international-community-strikes-a-ground-breaking-tax-deal-for-the-digital-age.htm (accessed 16 Sep. 2022).

[8] B. Sevilla Bernabéu, *Tax Law in the Face of the Paradigm Shift Resulting from the Digital Revolution*, in *Derecho digital y nuevas tecnologías* 685 (A. Madrid Parra & L. Alvarado Herrera (dir.) eds, Aranzadi 2022).

[9] European Parliament, *National Vetoes of Global Tax Deal*, Strasbourg plenary session (30 Jun. 2022), https://www.europarl.europa.eu/news/en/agenda/briefing/2022-07-04/8/national-vetoes-of-global-tax-deal (accessed 16 Sep. 2022).

[10] Proposal for a Council Directive laying down rules relating to the corporate taxation of a significant digital presence, COM (2018) 147 final, 21 Mar. 2018.

[11] Proposal for a Council Directive on the common system of a digital services tax on revenues resulting from the provision of certain digital services, COM (2018) 148 final, 21 Mar. 2018 (hereinafter, DSTD). This proposal was rejected, as was also the 2019 Directive for a digital advertising tax. Since 2020, the Commission has advanced the introduction of a digital levy before Jan. 2023 that has not seen the light yet. Special meeting of the European Council (17, 18, 19, 29 and 21 Jul. 2020), Conclusions, 21 Jul. 2020, EUCO 10/20, at 9.

[12] *Ibid.*, at 7.

[13] *Ibid.*, Art. 3.

[14] This amount is not arbitrary but reproduces the already established in other norms. Particularly, it is the threshold established in the Directive 2011/16/EU regarding mandatory automatic exchange of information in the field of taxation, and also the threshold established in Art. 2 of the Proposal for a Council Directive on a CCCTB, Strasbourg, 25 Oct. 2016, 2016/0336 (CNS); as established in J. M. Macarro Osuna, *Los equalization Levis sobre Servicios Digitales y art. 2 del Modelo de Convenio OCDE: ¿un caso de Treaty override?*, in *Retos del Derecho Financiero y Tributario ante los desafíos de la Economía Digital y la Inteligencia Artificial* 69–92 at 74 (A. Navarro Faure (dir.) ed., Tirant Lo Blanch 2021), Commission Staff Working Document. Impact Assessment, accompanying the document Proposal for a Council Directive laying down rules relating to the corporate taxation of a significant digital presence and Proposal for a Council Directive on the common system of a digital services tax on revenues resulting from the provision of certain digital services, SWD (2018) 81 final/2, 21 Mar. 2018, (hereinafter, Impact Assessment), 1.20.4, at 67.

[15] As an example, France has pointed out that multilateral solutions normally require a few years to work (using as an example the 'Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting' which took more than five years to show its effects), which led her to act unilaterally. Rapport fait au nom de la Commission des Finances, de l'Économie Générale et du contrôle budgétaire sur le projet de loi, après engagement de la procédure accéléré, portant création d'une taxe sur les services numériques et modification de la trajectoire de baisse de l'impôt sur les sociétés, 1737, 3 Apr. 2019, at 29–30.

digital advertising taxes; and (3) unilateral adjustments to Permanent Establishment definitions in the national income tax code.[16]

We will focus on the DST, which take on 'multiple digital business models', and are greatly influenced by the EU's 2018 DSTD proposal, that failed in avoiding a 'patchwork' of national responses. Examples of these taxes inside the EU are the French, Italian and Spanish already in place, the Czech under approval, and, before its withdrawal, the United Kingdom one.[17]

Not few are the problems that these taxes have encountered, and not few are the possible incompatibilities that the literature has found, especially regarding the fundamental freedoms and state aid rules consecrated in the EU.[18] Other criticism made is the risk that the taxes will be passed on to consumers.[19] Furthermore, the imposition of unilateral (from the Member States) or regional (EU) taxes is liable to suffer retaliation from other countries.[20] Moreover, some, like Bauer, have even argued that focusing the attention to DST reduces the interest in the negotiations of the reform of the international taxation system worldwide.[21] However, this last argument is not entirely true, as the DST have been presented since the beginning as *interim* measures while there was no consensus surrounding the reform, but always leaving the door open for future long-term solutions.

3 On the compatibility of digital services taxes and state aid rules

3.1 An Approximation to the Main Challenge

Taxation is a contentious field in the heart of the UE, mainly because Member States retain their sovereignty to establish their preferred tax system. However, such freedom is not without its limits, as the jurisprudence has repeatedly established: this area is also within the 'scope of the State aid rules', and the Member State 'must therefore exercise their competence in the field of taxation consistently with EU law', by refraining 'from adopting any measure, in that context, liable to constitute State aid incompatible with the internal market'.[22]

It is undisputed that when a Member State establishes some tax exemptions, they can provide a selective advantage; however, the CJEU has also ascertained that imposing a tax may also confer a selective advantage and thus be prohibited under Article 107 of the Treaty on the Functioning of the European Union (TFEU), when such tax favours certain undertakings or products by not subjecting them to it. In this sense, the *British Aggregates* Saga confirms that 'a tax that does not apply to all competing products tilts the level of competition in favour of those products that are untaxed'.[23]

In relation to the DST, the question is whether these national measures could be considered as state aid, especially because most of them have the same characteristics and elements as the DSTD. If the DTSD had passed, this tax would not have been considered as state aid according to the jurisprudence of the CJEU.[24] The General Court (GC), in the judgment *Deutsche Bahn*,[25] established that when Member States transpose the provisions, they are fulfilling their obligation of implementing the Community's norms as established in the Treaty and, thus, 'the provision at issue is not imputable to the German State'.[26] Following the same reasoning, if the DSTD had passed (or the new Directive that is being prepared by the Commission enters into force), the transposition of this measure by the Member States could never fall under the consideration of state aid, as 'that measure cannot be imputed to the Member States (but rather stems from an act of the Union legislature)'.[27]

Moreover, given the support that Executive Vice-President of the European Commission Margrethe Vestager gave to the actions taken by some Member States imposing unilateral DST, while admitting that an OECD global solution would be preferable, it seems unlikely that the Commission will start proceedings to

[16] S. Geringer, *National Digital Taxes-Lessons from Europe*, 35(1) S. Afr. J. Acct. Res. 4 (2021).

[17] *Ibid.* For an overview of all the national measures presented worldwide, *see* V. Grondona, A. M. Chowdhary & D. Uribe, *Mesures nationales sur l'imposition de l'économie numérique*, 111 S. Ctr. 1–32 (2020); E. Asen, *What European OECD Countries Are Doing About Digital Service Taxes*, Tax Foundation (22 Nov. 2021), https://taxfoundation.org/digital-tax-europe-2020/ (accessed 30 Nov. 2021).

[18] For an in-depth appraisal of their relationship with the fundamental freedoms, *see* C. Dimitropoulou, *The Digital Services Tax and Fundamental Freedoms: Appraisal Under the Doctrine of Measures Having Equivalent Effect to Quantitative Restrictions*, 47(2) Intertax 201–218 (2019); R. Mason & L. Parada, *The Legality of Digital Taxes in Europe*, Virginia Public Law and Legal Theory Paper Series 2020-50, 1–10 (2020). For a general overview of possible interferences with EU Law, *see* G. Kofler & J. Sinnig, *Equalization Taxes and the EU's 'Digital Service Tax'*, 47(2) Intertax 196 (2019).

[19] M. Bauer, *Digital Service Taxes as Barriers to Trade: Case Study*, International Trade Barrier Index, 6 (2019).

[20] This was the case when the French DST was first introduced, and the United States retaliated. *Ibid.*, at 6.

[21] *Ibid.*, at 7.

[22] Joined cases T-131/16 and T-263/16, *Kingdom of Belgium v. European Commission*, 14 Feb. 2019, ECLI:EU:T:2019:91, para. 63.

[23] P. Nicolaides, *State Aid Uncovered: Critical Analysis of Developments in State Aid 2019* 141 (Lexxion 2019).

[24] S. Moreno González, *Impuestos sobre determinados Servicios Digitales y ayudas de Estado: una reflexión provisional*, in Faure, *supra* n. 14, at 93–131, 101.

[25] Case T-351/02, *Deutsche Bahn*, 5 Apr. 2006, ECLI:EU:T:2006:104, para. 102. In this case, the German law transposed the Directive 92/81 which exempted certain mineral oils from excise duty, and Deutsche Bahn (a German railway company) alleged that such exemption constituted state aid.

[26] This position has been later ratified by the Case C-460/07, *Sandra Puffer v. Unabhängiger Finanzsenat*, 23 Apr. 2009, ECLI:EU:C:2009:254; Case C-89/98 P, *European Commission v. Ireland*, 2Dec. 2009, ECLI:EU:C:2009:742; Case C-272/12 P, *European Commission v. Ireland,* 10Dec. 2013, ECLI:EU:C:2013:812.

[27] Kofler & Sinnig, *supra* n. 18, at 196; J. F. Pinto Nogueira, *The Compatibility of the EU Digital Services Tax With EU and WTO Law: Requiem Aeternam Donate Nascenti Tributo*, in Pistone & Weber, *supra* n. 1, at 247–286, 254–255.

investigate such taxes.[28] In that regard, she declared that the DST will not be considered state aid as 'the European Commission would not support measures that contravene EU law'.[29]

However, unlikely does not mean impossible, and there is always the possibility that the question as to whether there is an incompatibility with state aid rules may come from the national jurisdictions through a preliminary reference to the CJEU (Article 267 TFEU).

3.2 On the Conditions for the Digital Services Taxes to Be Considered State Aid

To consider if the DST could be considered state aid and, thus, prohibited under EU law, we must establish whether they fulfil the criteria determined in the Treaty and the jurisprudence. As each DST is different, the test here developed would need to be adapted to the specificities of each one. However, as some of the most contentious characteristics are common (heritage of the DSTD) we will discuss them as a group.

The case law relays on the concurrence of four cumulative conditions:[30] (1) whether there is intervention of the state (by directly granting the aid and through state resources); (2) whether such intervention is liable to hinder or affect trade across between Member States; (3) whether there is a selective advantage for the certain undertakings; and (4) whether such measure distorts or threatens to distort competition.

On the first condition, a measure has to be financed 'directly or indirectly through State resources'[31] and be imputable to the state.[32] The Commission has pointed out that its transfer 'may take many forms' and as established in the case law, it is enough for the state to forego revenue.[33]

Thus, applied this to the case of the DST, on the one hand, the measure is adopted by law by the Member States, consequently being imputable to them; and, on the other hand, the tax will only affect the companies whose activity falls under the scope of application previously explained and who surpass the thresholds established, not collecting the states as a consequence the revenue from the other companies. As the CJEU has previously deemed, even measures that do not involve 'a positive transfer of State resources, [but that] place the persons to whom it applies in a more favourable financial situation than other taxpayers constitutes State aid'.[34] Therefore, the first condition to consider the DST as state aid is fulfilled.

In second place, it is necessary to contemplate whether the effects of the DST in question result in an intervention liable to hinder or affect trade between Member States.[35] Two precisions must be made in this regard: on the one hand, the CJEU has accepted that there is no need for the effect to be 'actual', but it can also be considered when the measure is 'liable' to have such effect on trade[36]; and, on the other hand, the effect in question can be deemed to exist although the beneficiaries of the measure are not 'directly involved in cross-border trade'.[37] This occurs because the favoured undertakings can increase or maintain their levels of activity, thus making it more challenging for business of other Member States to penetrate the market.[38] Hence, an examination of 'the foreseeable effects on competition (…) and the actual effects of the aid'[39] is mandatory, and cannot be presumed or hypothetical.

The Commission has, in various cases, accepted the lack of effect of trade because the measures 'had a purely local impact'.[40] However, the taxable revenues of the DST (particularly in the case of user-targeted advertisement as well as intermediation services by digital interfaces) do not have, by nature, a locally restricted audience, as the advantage of the digital business is that they can be accessed anywhere.

To understand the possible effect on trade a simple yet clarifying example can be made. Google and Amazon have raised advertising fees to offset the Spanish and French DST.[41] To illustrate this imagine that a videogame that comes from Croatia is currently sold for 30 euros across the EU. Amazon normally charges a 15% in Germany for the concept of 'Referral Fee', while in France it charges 15.45% in the concept of 'Referral Fee (including DST)'.[42] Thus, the Croatian company

[28] González, *supra* n. 24, at 119.

[29] CFE's Tax Top 5, *Key Tax News of the Week, CFE Tax Advisers Europe* (2 Mar. 2020), https://maintax.org/news/cfe-tax-top-5-2-march-2020/ (accessed 2 Apr. 2021).

[30] Article 107(1) TFEU; Joined Cases C-105/18 to C-113/18, *Asociación Española de la Industria Eléctrica (UNESA) y otros v. Administración General del Estado*, 7 Nov. 2019, ECLI:EU:C:2019:935, para. 58.

[31] Article 107(1) TFEU; Commission Notice of 19 Jul. 2016, on the notion of state aid as referred to in Art. 107(1) of the TFEU, [2016] O.J. 2016/C 262/01 (hereinafter, Commission Notice), para. 38.

[32] *Ibid.*

[33] *Ibid.*, para. 51.

[34] Joined Cases C-106/09 P and C-107/09 P, *Commission and Spain v. Government of Gibraltar and United Kingdom of Great Britain and Northern Ireland*, 15 Nov. 2011, ECLI:EU:C:2011:732, para. 72.

[35] Commission Notice, *supra* n. 31.

[36] Case C-518/13, *Eventech v. The Parking Adjudicator*, 14 Jan. 2015, ECLI:EU:C:2015:9, para. 65; Joined Cases C-197/11 and C-203/11, *Libert and others*, 8 May 2013, ECLI:EU:C:2013:288, para. 76.

[37] Commission Notice, *supra* n. 31, para. 191.

[38] Case C-518/13, *supra* n. 36, para. 67.

[39] Joined Cases T-447/93, T-448/93 and T-449/93, *AITEC and others v. Commission*, 6 Jul. 1995, ECLI:EU:T:1995:130, para. 141.

[40] In this respect, the Commission has only considered that the effect on trade would be hypothetical and therefore not constitute state aid in the case of cultural products which, for geographical or linguistic reasons, have a restricted audience (which is not the case for the DST). Commission Notice, *supra* n. 31, para. 196.

[41] M. Pollet, *Google to Raise Advertising Fees to Offset French, Spanish GAFA Tax*, Euractiv (11 Mar. 2021), https://www.euractiv.com/section/digital/news/google-to-raise-advertising-fees-to-offset-french-spanish-gafa-tax/ (accessed 30 Nov. 2021).

[42] Data provided by the Amazon website. The referral fee is effective since 31 Mar. 2022. For more information *see* FR Amazon website, https://sellercentral.amazon.fr/help/hub/reference/external/GF9K4BWLZXRPC62U?ref=efph_200336920_bred_59841&locale=en-FR (accessed 7 Sep. 2022); DE Amazon website, https://sellercentral.amazon.fr/help/hub/reference/external/GGYND54PM5WB84UM?ref=efph_200336920_bred_59841&locale=en-FR (accessed 7 Sep. 2022).

will be more likely to trade in countries such as Germany without a DST than those which have it; and in those that have adopted it, the company will likely increase the prices of its products to offset the new costs. As a result, it is the consumers that are losing and will lose the most.

In third place, we examine the last requirement, which focuses on whether such measure distorts or threatens to distort competition,[43] leaving the more controversial condition to be separately analysed later. This criterion is often analysed with the previous one,[44] even if normally the CJEU focuses its reasoning only on the criteria regarding the 'selective advantage'.

The CJEU considers that the last criterion is fulfilled when the measure 'is liable to improve the competitive position of the recipient compared to other undertakings with which it competes'.[45] In this sense, it is included when the advantage given relives the undertaking of expenses that it would normally have.[46]

In the case of the DST, we could understand that there are no expenses normally for the undertakings not taxed and, consequently, nothing would change. However, adding a new tax to the taxation scheme for companies results in a supplementary cost for the undertakings subjected to the DST, which distorts the regular competition and, therefore, the criterion is also fulfilled.

4 A CLOSER LOOK TO THE NOTION OF 'SELECTIVE ADVANTAGE'

The ultimate criterion that needs to be studied in relation with the DST is the notion of 'selective advantage'. The CJEU considers that 'a measure by which the public authorities grant certain undertakings a tax exemption which *places the recipients in a more favourable financial position* than other taxpayers amounts to State aid' is an 'advantage'.[47] And, that to establish the 'selectivity' it:

> is necessary to consider whether, under a particular statutory scheme, a State measure is such as to favour "certain undertakings or the production of certain goods" within the meaning of Article 87(1) EC [Article 107 (1) TFEU] *in comparison with other undertakings in a comparable legal and factual situation in the light of the objective pursued* by the measure concerned.[48]

Thus, when there is comparatively an advantage that favours a number of the taxpayers (regardless of whether they are actual or potential), to not fall under the scope of state aid rules Member States are obligated to not treat with partiality some of the undertakings.[49] Nevertheless, the only agreement reached is limited to this idea, because outside of it there are a lot of 'terminological ambiguities and substantive differences'.[50] Particularly because the concepts of 'advantage' and 'selectivity' are often confused and, even the CJEU frequently analyses them together or focuses only on the selectivity of the measure in question.

The motion of determining an 'advantage' is defined as a 'benchmarking or comparative exercise'.[51] Not all advantages are *per se* selective. In this respect, if they are bestowed to all undertakings ('general measures'), there is no selectivity and, therefore, Article 107 TFEU is not applicable.[52] In relation to taxes, the CJEU has recognized that the reduction of a company's tax burden should be considered as an advantage because it leaves those undertakings in a more favourable position.[53] In the case of the DST, it could be argued that the undertakings that do not meet the criteria established are given an advantage over those who fall under their scope and are taxed.

The most 'decisive criterion'[54] to establish the possible incompatibility with state aid rules of the DST is the element of the 'selectivity'. The CJEU, in order to establish that a tax is selective, follows a three-step test, also called a review of abstract *de jure* selectivity.[55] In the first step, it identifies a 'common or normal regime applicable in the Member State concerned'.[56] In the second step, it tries to demonstrate whether there is a derogation from such regime, 'inasmuch as it differentiates between economic operators who, in light of the objective assigned to the tax system of the Member State concerned, are in a comparable factual and legal situation'. In the third step, once it is established that the tax or measure in question fulfils the previous conditions, assesses whether they could be 'justified by the nature or general scheme of system of which they form part',[57] while examining the

[43] Commission Notice, *supra* n. 31.
[44] *Ibid.*, para. 186.
[45] *Ibid.*, para. 187.
[46] Case C-172/03, *Heiser*, 3 Mar. 2005, ECLI:EU:C:2005:130, para. 55.
[47] Case T-210/02 RENV, *British Aggregates Association v. European Commission*, 7 Mar. 2012, ECLI:EU:T:2012:110, para. 46 (*emphasis added*).
[48] *Ibid.*, para. 47 (*emphasis added*).
[49] W. Schön, *Tax Legislation and the Notion of Fiscal Aid: A Review of 5 Years of European Jurisprudence*, in *State Aid Law and Business Taxation* 3–26 at 7 (I. Richelle, W. Schön & E. Traversa eds, Springer 2016).
[50] *Ibid.*
[51] Nicolaides, *supra* n. 23, at 141.
[52] M. Lang, *State Aid and Taxation: Selectivity and Comparability Analysis*, in Richelle, Schön & Traversa, *supra* n. 49, at 27–37, 28.
[53] Case C-66/02, *Italian Republic v. Commission of the European Communities*, 15 Dec. 2005, EU:C:2005:76, para. 78; Case C-387/92, *Banco Exterior de España SA and Ayuntamiento de Valencia*, 15 Mar. 1994, EU:C:1994:100, para. 14; Case C-522/13, *Ministerio de Defensa and Navantia v. Concello de Ferrol*, 9 Oct. 2014, EU:C:2014:2262, para. 23.
[54] Opinion of Advocate General Kokott in Case C-66/14, *Finanzamt Linz v. Bundesfinanzgericht, Außenstelle Linz*, 16 Apr. 2015, ECLI:EU:C:2015:242, para. 114.
[55] R. Ismer & S. Piotrowski, *The Selectivity of Tax Measures: A Tale of Two Consistencies*, 43(10) Intertax 561 (2015).
[56] Joined cases C-78/08 to C-80/08, *Paint Graphos and Others*, 8 Sep 2011, ECLI:EU:C:2011:550, para. 49.
[57] *Ibid.*, para. 64.

compliance with 'principle of proportionality' of the measure, so as to not go 'beyond what is necessary'.[58]

4.1 On the Definition of a 'Normal' or 'Reference' System

As established by the CJEU, the first step is determining the 'normal' or 'reference system' to which compare the new measure imposed. But what is considered 'normal'? When the situation involves a tax exemption, the benchmark is the tax; but, when faced with a *ex novo* tax with 'an excessively narrow scope',[59] the parameter of comparison is imperceptible or non-existent.

When a situation like this was presented in front of the CJEU in the case *Kernkraftwerk Lippe-Ems*, the Court reasoned that the 'nuclear fuel tax' which was introduced by Germany could not be compared with the general tax system on energy production but as a 'self-standing implementation of the "polluter-pays" principle for nuclear waste'.[60] In this sense, the CJEU understood that a tax introduced with a specific objective and imposed to a particular sector should not be measured against the general taxation framework.

Shifting the focus of attention to turnover taxes, recently the CJEU has opened the door to what some understand as a possible defence for the DST.[61] In the case *Hungary v. European Commission*,[62] regarding the 2014 Hungarian tax on the turnover from the broadcasting or publication of advertisements, the Commission and the GC argued extensively on this matter, while later the CJEU ratified the GC's decision.[63]

The Commission, following the *Gibraltar*'s jurisprudence, understood that the tax introduced by Hungary was based on some elements (namely the progressive tax rates applicable to a tax basis relying on turnover) that had been conceived in an arbitrary manner to favour certain undertakings.[64] The progressive rate introduced subjected the different undertakings to different levels of taxation depending on their size (namely, it passed from a 0% rate to a 50%), thereby taxing less undertakings with a 'lower level of turnover (and thus smaller undertakings)',[65] to the disadvantage of the others which were the larger undertakings.

However, the GC disagreed with the reasoning, and annulled its decision, ruling on three errors which had been allegedly committed by the Commission: the determination of the 'normal' tax regime, the objective of the regime and the existence of selective advantages in the context of a progressive turnover tax structure.[66]

Regarding what is a 'normal' tax system, the GC points out that such system cannot exceed the sector[67] (which in the judgment was the broadcasting and publication of advertisements). Furthermore, the CJEU delineates that it will be established by the Member States, as they have the autonomy to determine, among other elements, the tax rate and the basis of the taxable event, which form part of the reference system,[68] thus leaving the determination of the 'normal system' to the national level.

In the proceedings, Hungary argued that 'in the absence of the tax rate enabling the structure of the "normal" system to be determined, it is indeed impossible to examine whether there is a favourable derogation to the advantage of certain undertakings'.[69] Meanwhile, the Commission determined the 'normal system' a single rate taxation system which was developed hypothetically. However, the GC requires for the following analysis regarding the possible selective advantage, that the 'normal' tax system determined be actual and not a result of the assumptions of the Commission.[70] Thus, the Court agrees with Hungary in maintaining that 'the advertisement tax in itself, with its structure including its single scale of progressive rates and successive bands'[71] is the reference system.

Returning to the dilemma posed by the DST, most of the proposed European unilateral taxes are greatly inspired by the Commission's proposal which had a narrow material scope.[72] This means that it only taxes the 'business models where the user contribution plays a central role in the sense that the service would not exist if the user did not contribute to it'.[73] Therefore, and while every tax has its specific characteristics and a particular scope, in abstract terms, we can see how they are sectorial taxes based on user created value.[74]

Translated the reasoning presented by the GC and the CJEU in *Hungary v. Commission* and *Poland v. Commission* to the case of the DST, as well as the opinion of Advocate General Kokott, the 'normal' tax system should be the

[58] *Ibid.*, para. 75.
[59] Nicolaides, *supra* n. 23, at 141.
[60] Case C-5/14, *Kernkraftwerk Lippe-Ems GmbH v. Hauptzollamt Osnabrück*, 4 Jun. 2015, ECLI:EU:C:2015:354, paras 73–79.
[61] The notion of DST is brought up more than fifteen times to argue the defence of the Hungarian tax against the Commission's considerations. Opinion of Advocate General Kokott in Case C-596/19 P, *European Commission v. Hungary*, 15 Oct. 2020, ECLI:EU:C:2020:835.
[62] Case T-20/17, *Hungary v. European Commission*, 27 Jun. 2019, ECLI:EU:T:2019:448. For the purpose of this article we focus on this judgment, but *see also* a similar reasoning in: Joined Cases T-836/16 and T-624/17, *Republic of Poland v. European Commission*, 16 May 2019, ECLI:EU:T:2019:338; later confirmed in: Case C-562/19 P, *European Commission v. Republic of Poland*, 16 Mar. 2021, ECLI:EU:C:2021:201.
[63] Case C-596/19 P, *European Commission v. Hungary*, 16 Mar. 2021, ECLI:EU:C:2021:202.
[64] Case T-20/17, *supra* n. 62, para. 21.
[65] *Ibid.*, para. 14.
[66] *Ibid.*, para. 111.
[67] *Ibid.*, para. 79.
[68] Case C-596/19 P, *supra* n. 63, para. 44–45.
[69] Case T-20/17, *supra* n. 62, para. 80.
[70] *Ibid.*, para. 81.
[71] *Ibid.*, para. 83.
[72] Impact Assessment, *supra* n. 14, at 78, point 9.4.1.
[73] *Ibid.*, at 58, point 9.2.1.
[74] *Ibid.*, at 63, point 9.3.2.

tax itself.[75] In support of this idea is the fact that the DST is not a 'general tax on goods and services',[76] but a tax on digital business reliable on user-value creation. Moreover, it has also been signalled that a tax such as the DST should not be assessed in relation to the traditional system which, by nature, restricts the 'adoption of optimal taxes'.[77]

Therefore, we will continue the analysis on the basis that the reference system for the DST will be the tax itself, as it seems the most reasonable choice based on the recent jurisprudence of the CJEU and, particularly, given the specific and novel scope of the tax.

4.2 On the Possible Derogation from the Reference System Determined

Once established the 'normal' taxation system, to evaluate the selective nature of the advantage that results from the national measure in question (the tax), it must be assessed if it 'favour(s) certain undertakings or the production of certain goods'[78] over others 'which, in the light of the objective pursued by that regime, are in a comparable factual and legal situation and which accordingly suffer different treatment that can in essence, be classified as discriminatory'.[79]

To do so, first we must look at the objectives of the DST and the rationale behind their regime to compare if they do favour certain undertakings. The DSTD and the Member State's proposals all have the same purpose: taxing digital services 'to level the playing field in the *interim* period until a comprehensive solution is in place'[80] due to the lack of adequacy between the traditional international tax regime and the new models of business, as well as 'fighting against aggressive tax planning'.[81]

With that goal the taxes target certain activities which have been selected because: (1) firstly, the undertakings in those sectors have 'substantial market power'; (2) secondly, they are typically undertaxed with the current taxation system; and (3) finally, their lower costs to enter markets and render certain services permit a taxation based on 'gross revenue rather than net income, that would not otherwise be appropriate'. [82]

In the light of this objective, the CJEU has determined in multiple occasions the need to determine if undertakings are in a comparable situation putting the objectives disposed in the measure or tax introduced in the central part of the examination.[83]

Regarding their comparability, a case can be made that digital companies and traditional ones are not in a legal and factual comparable situation. For example, in the advertising field, digital companies make use of 'extremely sophisticated targeting mechanisms'[84] which the traditional companies do not have access, and that positions them in a different market.

With the proposed DST there are two alleged types of discrimination based on the undertakings taxed (their size) and the taxable revenues (namely, the type of service provided by the undertakings).

The first alleged derogation from the reference system based on size comes in the field of the DST because, given the high thresholds applicable, not all undertakings are equally taxed, affecting more those with a higher turnover.[85]

If we observe, on the one hand, the Commission's reasoning in the *Hungary v. Commission* case, a turnover tax is not optimal to tax the ability to pay of undertakings as taxing profits would be, in comparison, more likely to take into account the economies of scale and cost structures of the companies.[86] On the other hand, and following the argumentation of the CJEU[87] in the same case, a tax on turnover is not *per se* a measure constitutive of a selective advantage[88] because the undertakings which have higher turnover and, therefore, surpass the thresholds of the DST, enjoy lower costs and are able to pay proportionally more than other undertakings who do not exceed those limits.[89]

[75] This conclusion is sustained even when the scope changes from one tax to the other, as e.g., some of them only tax advertising services such as the Hungarian one, or tax two digital services like France, or three in the Spanish case. S. Kirchmayr & S. Geringer, *European Union/Austria – State Aid Issues Regarding National Digital Taxes*, 60 (7) Eur. Tax'n 4 (2020).

[76] W. Haslehner, *EU and WTO Law Limits on Digital Business Taxation*, in *Tax and the Digital Economy. Challenges and Proposals for Reform* 25–48, 38 (Wolters Kluwer 2019).

[77] W. Cui, *The Digital Service Tax: A Conceptual Defense*, 73(1) Tax L. Rev. 4 (2018).

[78] Article 107 (1) TFEU.

[79] *UNESA*, *supra* n. 30, para. 60.

[80] DSTD, *supra* n. 11, at 3.

[81] *Ibid.*, at 4.

[82] D. Shaviro, *Digital Services Taxes and the Broader Shift from Determining the Source of Income to Taxing Location-Specific Rents*, 19(36) NYU L. & Econ. Res. Paper 48–49 (2020); J. Becker et al., *Re-allocation of Taxing Rights for Big Data Business Models Working Paper*, International & Comparative Tax eJournal, 1–32 (2019).

[83] In connection with this it is interesting to regard the UNESA judgment, where Spain had levied a tax on hydroelectric producers of electricity who operated in autonomous communities, thus excluding those who produced it within a single community, as well as those who generated electricity from other sources. The CJEU underlined that, to determine whether there is a selective advantage, it needs to determine if they are in comparable situations. In the case it did not occur because hydroelectric producers generate electricity with water resources, which necessarily lead to 'an environmental impact' (para. 66), while the other undertakings not taxed base their production in other sources than water (para. 67).

[84] For a more detailed reasoning on their lack of comparability *see* F. Fichera, *Digital Service Taxes Under State Aid Scrutiny*, 20(4) Eur. State Aid L.Q. 486 (2021).

[85] L. Parada, *Ayudas de Estado e Impuestos Digitales en Europa: Sentencia del Tribunal General en los Asuntos Acumulados T–836/16 y T–624/17*, 7 Revista Aranzadi Unión Europea 7 (2019).

[86] Case T-20/17, *supra* n. 62, para. 68.

[87] Case C-596/19 P, *supra* n. 63, para. 51. As well, as the argumentation in the GC and of the AG: *Hungary v. Commission, supra* n. 62, para. 89; Opinion of AG Kokott in C-596/19 P, *supra* n. 61, para. 61.

[88] González, *supra* n. 24, at 127.

[89] Case T-20/17, *supra* n. 62, para. 89.

The reasoning behind the position of the Commission was that the structure of the tax ('with its progressive rates and successive bands')[90] was opposed to its objective (which was increasing the revenues of the state) and, hence, it had 'discriminatory effects between undertakings in that sector'.[91] Regarding the progressive tax structure introduced, the GC accepts, conversely, the presumption that undertakings with a higher turnover may incur in lower costs, which results in a 'greater disposable revenue' due, mainly, to economies of scale, and thus, they can pay 'proportionally more in terms of turnover tax'[92] (in line with the redistributive purpose which was the ultimate intention of the Hungarian authorities with the tax).

Furthermore, in previous case law the Court had already ruled that such structures are not *per se* constitutive of a selective advantage;[93] and that undertakings are found to be in different factual and legal situations when some of them pay less tax than others because of the measure in question.[94] In consequence, as long as the undertakings are not considered to be in a comparable situation, the measure that treats them differently does not constitute state aid under EU law.

However, as the DST have a fixed rate at 3%, some have argued that the rationale behind the CJEU's *Hungary v. Commission* will not be applicable.[95] Anyhow, the Court will have to decide whether this tax made up of these thresholds is compliant with the already exposed 'level-playing field' objective that underlies the objective of the tax.

The undertakings that surpass the thresholds established are the ones that can and do aggressive tax planning. Therefore, as we have stated that the goal of the DST is to help fight it, it could be argued that the undertakings that surpass them are not in a comparable situation as the ones that do not in line with the rationale of the tax, and, consequently, there would not be a selective advantage.

Moreover, it has been criticized that the distinction in size disguises a distinction based on nationality as, allegedly, most of the undertakings who comply with the requirements of the taxes are from the United States.[96] In relation to the national differences, it is interesting to extrapolate the reasoning of Advocate General Kokott in the case *Finanzamt Linz*,[97] as she acknowledges that the CJEU has taken on many occasions a wide approach to the notion of selectivity,[98] but that, when analysing the difference in treatment, there is a distinct need for a strict understanding of the concept.[99]

In this sense, the fact that most of the companies that may fall under the scope of application of the Member State's DST are foreigners does not have an effect when assessing whether they are state aid. It cannot be determined that there is discrimination simply because of the higher proportion of foreign companies affected, namely because they only reflect the composition of the market.[100] Anyhow, if any of the national undertakings grew to surpass the thresholds established, they would also fall under the scope of the tax.[101] Moreover, the recent jurisprudence of the CJEU seems to aval the idea that there is not a selective advantage in this case.[102] However, we leave this argument aside as it would be more relevant when analysing the compatibility of the DST with the fundamental freedoms.

The second alleged derogation is based on the taxable revenues, the activities taxed, because the DST limit their scope to certain digital services, setting aside others pursued by digital undertakings.[103] To determine whether that choice constitutes a discrimination between both undertakings it must be looked at from the perspective of the objectives of the taxes.

Each DST has a different scope, but the maximum activities covered by the proposed and adopted taxes until 2021 are three (following the example of the DSTD as does the Spanish tax): (1) user-targeted advertising on a digital interface; (2) intermediation services through multi-sided digital interfaces; and (3) the transmission of collected user data.[104] However, interfaces that supply digital content (such as Netflix) are explicitly excluded,[105] even though there is also a component in their business model of user participation.[106] Meanwhile, other Member States have chosen a more limited scope.[107] Thus, to determine whether the undertakings which fall and do not fall under

[90] *Ibid.*, para. 85.
[91] *Ibid.*
[92] *Ibid.*, para. 89.
[93] *Ibid.*, para. 92.
[94] *Ibid.*, para. 99.
[95] Fichera, *supra* n. 84, at 488.
[96] Office of the United States Trade Representative, *Section 301 Investigation: Report on Spain's Digital Services Tax* 13 (2021).
[97] Opinion of AG Kokott in Case C-66/14, *supra* n. 54.
[98] *Ibid.*, para. 112.
[99] *Ibid.*, paras 113 and 115.
[100] For a development of this reasoning *see* Case C-323/18, *Tesco-Global,* 3 Mar. 2020, ECLI:EU:C:2020:140, para. 72; Opinion of Advocate General Kokott in Case C-232/18, *Tesco-Global,* 4 Jul. 2019, ECLI:EU:C:2019:567, paras 62, 65 and 78.
[101] However, not all the companies affected are from the United States. E.g., in Jan. 2021, it was foreseen that, for the Spanish DST, 64% would be companies from the United States, but the rest would be from other countries, including two Spanish businesses. Office of the United States Trade Representative, *supra* n. 96, at 13.
[102] In agreement with this idea, Fichera highlights how the CJEU in the *Polish retail sales tax case* rejects the Commission's arguments of a de facto favouring of foreign undertakings. Fichera, *supra* n. 84, at 489.
[103] Furthermore, this choice of firms raises tensions with the principle of tax neutrality, even though Shaviro indicates that the DST may 'increase tax neutrality as between industries and firms', because they part from a different treatment with the actual taxation regime. Shaviro, *supra* n. 82, at 48.
[104] Article 3.1 DSTD.
[105] *Ibid.*
[106] Shaviro, *supra* n. 82, at 48.
[107] For example, France only taxes intermediation and advertisement services. Loi n° 2019-759 du 24 juillet 2019 portant création d'une taxe sur les services numériques et modification de la trajectoire de baisse de l'impôt sur les sociétés, Art. 1.

the foreseen taxable events are in the same situation, a case per case analysis should be made. In general terms, most of these taxes focus on services based on value creation by users but, this new principle[108] has been criticized because it is not clear how to distribute the allocation of profits across jurisdictions.[109]

In relation to user value creation, it could be argued that there is a distinction between business where 'the user's role in value creation is less central' and those where it is the main element,[110] and therefore say that they are not in a comparable situation and there is no difference in treatment that makes the DST fall under state aid rules. Nevertheless, the terms are quite vague to be sustained; and given the difficulty in establishing which companies are digital business or not, to differentiate between those that have a 'less' or 'more' central role in value creation seems quite unlikely to be possible.

In general terms, the activities selected are in line with the objective of the tax of levelling the playing field, as they are focused on activities that currently fall outside the scope of the traditional tax system. Nevertheless, the selection is not all comprehensive and leaves aside certain activities that could be in line with the same objective, thus creating a difference in treatment between undertakings in a comparable situation.[111]

As a result, it could be argued that there is a difference in treatment between undertakings that are in a comparable situation because of the activities selected as taxable revenues, thus leading to a selective advantage.

4.3 On Possible Justifications

Finally, we will continue with the last step of the 'selective advantage' test and analyse the possible justifications Member States can claim to not consider the DST as state aid, as long as they can prove that the tax imposed is 'fully in line with the underlying rationale of the tax system itself'.[112]

In light of this, 'a measure which derogates from the reference system (*prima facie* selectivity) is non-selective if it is justified by the nature or general scheme of that system',[113] which occurs when the measure emanates from the 'intrinsic or guiding principles of the reference system or where it is the result of inherent mechanisms necessary for the functioning and effectiveness of the system'.[114] Therefore, a case-by-case analysis of each DST would be needed to establish whether its objectives justify the possible derogation of the reference system established. Anyhow, some of the main purposes of the taxes and logic behind the systems are shared, so we will look at some of the possible justifications in a broad sense.

Nevertheless, and in the name of transparency, the CJEU has accepted that '*a prima facie* selective measure could be justified' in very few cases.[115] And, in those in which it has, there has been fervent criticism to its reasoning.[116] Despite this, the analysis of the potential consideration as state aid of the DST would not be complete without mentioning some possible justifications that the defendants or the CJEU could bring forward in case of a future judgment.

The CJEU has admitted that 'objectives inherent in the general tax system concerned could justify an *a priori* selective tax regime'.[117] In *A-Brauerei*, the introduction of an exemption is accepted as it is done with the objective of 'avoiding taxation that is considered excessive'.[118] Moreover, the Court accepts the 'prevention of abuse' as a justification connected to the general scheme,[119] thus understanding that the tax advantage analysed does not fulfil the condition of the selective advantage.

In the case of the DST, the Court could argue *sensu contrario*, accepting, not the need to avoid excessive taxation, but to correct null taxation. The goal behind the DST, as we have seen, is to tax those digital companies that fall outside of the scope of the traditional taxation system. Therefore, it can be considered that, in trying to avoid this null or lacking taxation, the discrimination suffered by certain undertakings could be justified.

Moreover, in the case *Hungary v. Commission*, and if it were accepted that the undertakings who are in a comparable situation are treated in a different manner, 'that discrimination gives rise to a selective advantage which may constitute State aid if the other conditions laid down in Article 107(1) TFEU are met'.[120] The GC determines that the objectives that can justify the imposition of progressive tax structures are not only those aiming to redistribute wealth or offset negative externalities, but that the scope is broader as long as the criteria chosen is not arbitrary.[121]

While the *Hungary v. Commission* case deals with a progressive tax, the justification of the tax with criteria that is not arbitrary can be extended to other situations. In the case of the DST, the selection of the rates and

[108] The principle is based on the idea that 'corporate profits are taxed where value is created'. Shaviro, *supra* n. 82, at 13; W. Schön, *One Answer to Why and How to Tax the Digitalized Economy*, 10 Max Planck Inst. Tax L. & Pub. Fin. 6 (2019).

[109] For a developed analysis of all the problems that the notion generates, *see ibid.*, at 6–7.

[110] Cui, *supra* n. 77, at 6.

[111] An example is the exclusion of subscription fees of the taxable revenues, which have a great impact for companies such as Spotify. *See* R. Mason & L. Parada, *Digital Battlefront in the Tax Wars,* 92 Tax Notes Int'l 1193 (2018).

[112] Schön, *supra* n. 49, at 20.

[113] Commission Notice, *supra* n. 31, para. 138.

[114] Joined cases C-78/08 to C-80/08, *supra* n. 56, para. 69.

[115] R. Federico, *Case 'A-Brauerei' C-374/17 or on Selective Deafness of the European Court of Justice*, 8 Studi Tributari Europei 11 (2018).

[116] *Ibid.*, at 10–11.

[117] Case C-374/17, *Finanzamt B v. A-Brauerei*, 19 Dec. 2018, ECLI:EU:C:2018:1024, para. 49.

[118] *Ibid.*, para. 45.

[119] *Ibid.*, para. 51.

[120] Case T-20/17, *supra* n. 62, para. 102.

[121] *Ibid.*, para. 103.

thresholds has not been capricious or random but follows an elaborated reasoning. All the taxes proposed or adopted have a narrow scope as they have introduced precise thresholds to 'target more effectively the most relevant cases'.[122] The rationale behind them is to put the traditional and digital companies at the same level, reducing the benefits that some undertakings have enjoyed because of the difficulties encountered by national authorities of the territories where they operated when taxing profits of companies that act in several jurisdictions.[123]

In relation to the selection of the thresholds imposed, it appears that they have been established with the purpose of not discriminating. In this regard, we have already covered the reasoning of the general threshold of EUR 750 million,[124] which is shared with other regulations in the EU. And, in relation to the second specific threshold on turnover, it was found that '*de facto* discrimination' would only happen if it were fixed above EUR 50 million, while one between 10 to 50 million would balance such risk.[125] Given that all DST in the EU are below that threshold, the structure of the taxes imposed does not seem arbitrary.

In addition, one of the possible justifications most debated in the literature is the principle of the ability to pay. While the great majority of the authors disagree with the notion that it is an optimal defence,[126] the Court seems to aval the idea.[127] Contrary to its use, it has been argued that turnover 'needs to cover first costs and [that imposing] a higher tax on larger turnover may turn [a] viable company into unviable'.[128]

Nonetheless, the Impact Assessment of the DSTD already considered the possible shortcomings of introducing a tax on turnover instead of profit and concluded that the fact that it would not be the most optimal tax base did not reduce its effectiveness to accomplish the objectives for which it was established. On this basis, it expected an annual growth of the digital markets (including online advertisement) between 6% and 17%.[129] Therefore, even if there could be another solution (which in fairness is already being prepared, as the DST are only conceived as *interim* measures), the DST try to confront a reality that cannot be stopped and that does not find a reflect in the actual taxation system.

Moreover, using the DSTD as a model for the rest, it is said that the specific objective of the measure is helping to level the playing field while a long-term and complete solution is being developed.[130] Therefore, the aim of the tax is not discriminating between undertakings but setting all of them in the same position in relation to the taxation system, so that the digital business do not enjoy a lighter tax burden than they would if they had a traditional business model.[131]

Following this reasoning, it has also been previously accepted as justifications the fight against fraud and tax evasion.[132] Given that the DST were first conceived as a temporal solution to the problems derived from aggressive tax planning, besides to reduce the number of undertakings that are able to evade taxation due to the actual international taxation system,[133] it seems as if this objective would justify the possible difference in treatment encountered in the previous step. In consequence, while the tax may treat differently undertakings, it only targets those who have higher possibilities to evade paying taxes due to their activity in multiple jurisdictions.

Finally, the measure in question, even if justified, needs to comply with the principle of proportionality so as to 'not go beyond what is necessary to achieve the legitimate objective being pursued'.[134] The DST are born as *interim* measures whose ultimate goal is levelling the playing field between digital and traditional companies, but that always take into account the possibility of a global, more comprehensive solution. Thus, that temporality in their nature justifies that they do not go beyond what is necessary as they do not try to surpass the purpose of their creation. Nevertheless, it is well known that there is 'nothing more permanent than a temporary solution'.[135]

5 Conclusion

The process of digitalization is unstoppable, and the new business models that have originated in the last three decades are here to stay, resulting in a new hybrid

[122] The European DST is defined as narrow and, as most of the national measures have either copied the scope of application or reduced it, we will also characterize them as having a 'narrow scope'. Impact Assessment, *supra* n. 14, at 68.

[123] *Ibid.*

[124] *See supra* n. 14.

[125] Impact Assessment, *supra* n. 14, 1.20.4, at 68–69.

[126] *See* Kofler & Sinnig, *supra* n. 18, at 101–145, in Haslehner, Kofler, Pantazatou & Rust, *supra* n. 76, at 139; Schön, *supra* n. 2, at 26–27.

[127] In this vein, we have already seen in *Hungary v. Commission* how the Court understood that taxing turnover was coherent in a progressive tax structure because it taxed larger companies who had 'more disposable revenue' and, thus, we can understand, greater ability to pay. Case C-596/19 P, *supra* n. 63, para. 89.

[128] P. Nicolaides, *State Aid Uncovered: Critical Analysis of Developments in State Aid 2016* 152 (Lexxion 2016). For a further development of the error's in the judgment *Hungary v. Commission*, according to the author, *see* Nicolaides, *supra* n. 23, at 165.

[129] Impact Assessment, *supra* n. 14, at 72, 60. Notwithstanding the effects of the Covid-19 pandemic which have notably increased the turnover of some of these digital companies (e.g., Facebook doubled its profits). E. Dwoskin, *As Facebook's Profit Doubles, CEO Mark Zuckerberg Sounds Off on Reopening the Economy Too Soon*, The Washington Post (29 Apr. 2021), https://www.washingtonpost.com/technology/2020/04/29/facebook-earnings-coronavirus/ (accessed 30 Nov. 2021).

[130] DSTD, *supra* n. 11, at 3.

[131] For an opposing viewpoint, *see* Kirchmayr & Geringer, *supra* n. 75, at 4.

[132] Commission Notice, *supra* n. 31, para. 139.

[133] DSTD, *supra* n. 11, at 4.

[134] Commission Notice, *supra* n. 31, para. 140; Joined cases C-78/08 to C-80/08, *supra* n. 56, para. 75.

[135] M. Friedman, *Tyranny of the Status Quo* 115 (1984).

economy. The link between the provision of services and having a permanent establishment has been severely severed or at least, notably weakened. Therefore, it seems unreasonable to continue relying on a tax system that only considers a part of the market. The system as it exists nowadays is prone to be abused by the MNEs which have the capital and infrastructure to evade taxation through aggressive tax planning and does not properly tax the creation of value.

In this context, a global change of the international taxation regime is needed. However, until consensus is reach, it is a logical consequence of this necessity that states, in a display of their sovereignty, decide to find a remedy on their own. However, not every solution proposed is a good solution. In this sense, the DST that have been proposed and adopted in many Member States and other countries outside of the EU raise many questions and concerns.

Particularly, the main question analysed in this article is whether the adoption of these DST inside the EU poses an issue of incompatibility with state aid rules. To do so we have covered exhaustively all the conditions required for a measure to be considered as state aid, singularizing them for the case of the DST and presenting the following key findings.

Firstly, it seems unlikely that the Commission will raise the issue of the incompatibility of the DST with state aid rules as most of them have been heavily inspired by the Commission's 2018 DSTD proposal.

Secondly, in the case it is brought in front of the CJEU, the 'selective advantage' criterion will be the decisive one.

Thirdly, the reference system will be the tax itself if the Court follows the line that AG Kokott started in the case *Commission v. Hungary*, where she referenced fifteen times the DST, paving the way for a future case.

Fourthly, the alleged discriminations that lead to a selective advantage are based on the size of the undertakings (and, indirectly, on their nationality) and on the taxable revenues of the DST, namely, the activities selected to be taxed. The first one is most likely to be disregarded by the Court according to its latest jurisprudence. However, the second one may be proven, and thus, considered that there is a selective advantage given to certain undertakings, as there are taxable revenues that have not been included and which would be in line with the objective pursued by the tax, that is, 'levelling the playing field'.

Fifthly, the CJEU does not generally consider the justifications 'by the nature or general scheme of that system' to deem that a measure (a tax in this case) that is *prima facie* selective is not. Despite this, this article proposes some possible justifications the Court may bring forward when trying to justify these taxes, including the avoidance of null taxation, the much-debated ability to pay principle, and the fight against fraud and tax evasion.

To answer the question with which I began this article (are DST incompatible under EU State aid rules?) it will be necessary to wait for the CJEU to rule on this issue. However, as it has been pointed out, its previous rulings on sectoral taxes could be a foretaste of a future decision that would answer this question in the negative.

Throughout this article I have discussed the arguments and counterarguments of both positions, as well as the potential view of the Court according to its previous case law. Moreover, the shortcomings and weaknesses of the adopted DST have been established and, an attempt has also been made to reflect the need from which they arise and the appropriate elements they contain. Anyhow, in the end, and in the view of this author, everything will likely depend on the analysis and the prevalence given to the objectives and justifications of the DST in question, as well as the acceptance of a limited 'reference system' by the CJEU.