EUROPEAN COMMISSION

Brussels,

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COMMISSION DECISION

of ***

ON THE TAX AMORTIZATION OF FINANCIAL GOODWILL FOR FOREIGN SHAREHOLDING ACQUISITIONS n° C 45/2007 (ex NN51/2007, ex CP9/2007)

implemented by Spain

(Only the Spanish version is authentic)

(Text with EEA relevance)

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THE EUROPEAN COMMISSION

Having regard to the Treaty on the Functioning of the European Union, and in particular the first subparagraph of Article 108(2) thereof,

Having regard to the Agreement on the European Economic Area, and in particular Article 62(1)(a) thereof,

Having called on interested parties to submit their comments pursuant to the provisions cited above[1] and having regard to their comments,

Whereas:

I. PROCEDURE

(1) By Written Questions addressed to the Commission (No E-4431/05, E-4772/05 and E-5800/06) several Honourable MEPs indicated that Spain had enacted a special scheme allegedly providing an unfair tax incentive for Spanish companies acquiring significant shareholdings in foreign companies, pursuant to Article 12(5) of the Spanish Corporate Tax Act ("*Real Decreto Legislativo 4/2004, de 5 de marzo, por el que se aprueba el texto refundido de la Ley del Impuesto sobre Sociedades*"[2], hereinafter "TRLIS").

(2) By Written Question No P-5509/06, the Honourable MEP Mr. David Martin complained about the unsolicited acquisition of control by way of shares' purchase of the UK energy generator and distributor Scottish Power by the Spanish energy producer Iberdrola, which - according to the Honourable MEP - would have unfairly benefited from State aid in the form of an acquisition tax-premium. The Honourable MEP demanded that the Commission examined all competition issues arising from the acquisition, which had been notified on 12 January 2007 for review by the Commission pursuant to Article 4 of Council

[1] OJ C 311, 21.12.2007, p. 21.
[2] Published in the Boletin Oficial del Estado of 11.03.2004

Regulation (EC) No 139/2004 of 20 January 2004 on the control of concentrations between undertakings[3] ("Merger Regulation"). By Decision dated 26 March 2007 (Case No COMP/M.4517 – IBERDROLA/SCOTTISHPOWER, SG-Greffe(2007) D/201696)[4], the Commission decided not to oppose to the notified operation and to declare it compatible with the internal market in application of Article 6(1)(b) of the Merger Regulation.

(3) By letter dated 15 January 2007 and 26 March 2007, the Commission asked the Spanish authorities to provide information in order to assess the scope and the effects of Article 12(5) TRLIS with respect to its possible qualification as State aid and its compatibility with the internal market.

(4) By letters dated 16 February 2007 and 4 June 2007, the Spanish authorities provided an answer to these questions.

(5) By fax dated 28 August 2007, the Commission received a complaint by a private operator alleging that the scheme set up by Article 12(5) TRLIS constitutes State aid and is incompatible with the internal market. The complainant has asked his identity not to be divulged.

(6) By decision of 10 October 2007 (hereinafter "the Opening decision"), the Commission initiated the formal investigation procedure laid down in Article 108(2) of the Treaty on the Functioning of the European Union (former Article 88(2) of the EC Treaty) on the tax amortization of financial goodwill provided for by Article 12(5) TRLIS, because it appeared to fulfil all the conditions to be considered State aid within the meaning of Article 107(1) TFEU. The Commission informed Spain that it had decided to initiate the procedure laid down in Article 108(2) TFEU. The Opening decision was published in the Official Journal of the European Communities[5], inviting interested parties to submit their comments.

(7) By letter dated 5 December 2007, the Commission received comments from Spain on the Opening decision.

(8) Between 18 January 2008 and 16 June 2008, the Commission received comments from thirty-two third parties on the Opening decision. The third parties not having requested to be treated anonymously are listed in the Annex 1 to the present decision.

(9) By letters of 9 April 2008, 15 May 2008, 22 May 2008 and 27 March 2009, the Commission forwarded the above mentioned observations to the Spanish authorities, in order to give them the opportunity to react. By letters of 30 June 2008 and 22 April 2009, the Spanish authorities presented their comments to third parties' observations.

(10) On 18 February 2008, 12 May 2009 and 8 June 2009, technical meetings took place between the Spanish authorities and the Commission representatives to

[3] OJ L 24, 29.01.2004, p. 1 – 22.
[4] See: http://ec.europa.eu/competition/elojade/isef/case_details.cfm?proc_code=2_M_4517
[5] See footnote 1.

clarify, amongst others, certain aspects of the application of the scheme at hand and the interpretation of the Spanish legislation relevant for the analysis of the case.

(11) On 7 April 2008, a meeting took place between the Commission's representatives and Banco Santander; on 16 April 2008 a meeting took place between the Commission's representatives and Garrigues representing various interested third parties; on 2 July 2008 a meeting took place between the Commission's representatives and Altadis; on 12 February 2009 a meeting took place between the Commission's representatives and Telefonica.

(12) On 14 July 2008, the Spanish authorities submitted additional information regarding the contested measure, in particular data extracted from the 2006 tax providing a general overview of the taxpayers benefiting from the contested measure.

(13) By email dated 16 June 2009, the Spanish authorities provided additional elements arguing that Spanish companies still face a number of obstacles to cross border mergers within the European Union.

(14) On 28 October 2009, the Commission adopted a negative decision[6] with recovery concerning aid granted to beneficiaries on the basis of the contested legislation when realising intra-EU acquisitions (hereinafter "the Previous decision"). As indicated in paragraph 119 of this decision, the Commission maintained the procedure, as initiated by the Opening decision, open for Extra-EU acquisitions, in light of new elements that the Spanish authorities committed to provide as regards the obstacles to cross border mergers outside the EU.

(15) On 12, 16 and 20 November 2009, the Spanish authorities submitted summary information concerning foreign direct investment of Spanish companies in Extra-EU countries.

(16) On 16 December 2009, the Commission services sent a request for information to the Spanish authorities concerning transactions in Extra-EU countries which it deemed necessary in order to realise the State aid assessment of the scheme along the lines suggested by the Spanish authorities.

(17) By letter dated 3 January 2010 the Spanish authorities submitted detailed information on 15 Extra-EU countries in which the vast majority (+/- 70%) of Spanish foreign direct investment was located. More precisely, the Spanish authorities presented two reports prepared by the law firm Garrigues and by KPMG, which include an analysis of alleged fiscal and legal obstacles in such Third countries.

(18) By letter of 27 January 2010 the Commission received comments from Banesto, member of the Santander Group.

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6 See Commission Decision C(2009) 8107 final and subsequent corrigendum C (2009) 8107 corr, available since January 2010 on Commission website: http://ec.europa.eu/competition/elojade/isef/case_details.cfm?proc_code=3_C45_2007.

(19) By email of 3 March 2010, the Spanish authorities answered to a technical question addressed to them on 26 February 2010.

(20) By letter of 9 July 2010 the Commission received comments from Santander.

(21) By letter of 25 November 2010 the Commission received comments from Telefonica.

(22) On 27 November 2009, 16 June 2010 and 29 June 2010, technical meetings took place between the Commission services and the Spanish authorities.

II. DETAILED DESCRIPTION OF THE CONTESTED MEASURE

(23) The measure at stake provides for a fiscal amortization of the financial goodwill arising from the acquisition of a significant shareholding in a foreign Target company.

(24) The measure is governed by Article 12(5) TRLIS (hereinafter "the contested measure"). More precisely, Article 2(5) of the Law 24/2001 of 27 December 2001 amended the Spanish Company Tax Act 43/1995 of 27 December 1995, by adding Article 12(5). The Real Legislative Decree 4/2004 of 5 March 2004 which provides a consolidated version of the Spanish Company Tax Act.

(25) The Commission is aware that the Spanish legislation has evolved since the date of the Opening decision[7]. Nonetheless, the Commission considers that the latter amendments are not susceptible to modify or alter the doubts expressed in the Opening decision. For the sake of consistency, the Commission will refer in the present decision to the numbering of the Spanish law as described in the Opening decision, even though they may have been modified. Any new legal provision will be expressly identified as such.

(26) Article 12(5) TRLIS, within Article 12 TRLIS entitled *"Correcciones de valor: pérdida de valor de los elementos patrimoniales"*, entered into force on 1 January 2002. It essentially provides that a company, which is taxable in Spain, may deduct from its taxable income the financial goodwill deriving from the acquisition of a shareholding of at least 5% of a foreign company, in yearly instalments, over not less than the 20 years following the acquisition.

(27) Goodwill is understood to represent the value of well-respected business name, good customer relations, employee skills, and other such factors expected to translate into greater than apparent earnings in the future. Under Spanish accounting principles[8], the price paid for the acquisition of a business in excess of the market value of the assets composing the business is termed "goodwill" and has to be booked as a separate intangible asset as soon as the acquiring company takes control on the target company[9].

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7 Law 4/2008 of 23 December 2008, which introduced modifications to several tax law provisions.

8 See Article 46, 39 of *Código de Comercio de 1885*.

9 Resulting from the implementation of Law 16/2007 of 4 July 2007 on "reforma y adaptación de la legislación mercantil en materia contable para su armonización internacional con base en la normativa de la Unión Europea".

(28) Under Spanish tax purpose principles, except under the contested measure, goodwill can only be amortised following a business combination that materialises either in case of acquisition or contribution of the assets composing an independent business or following a business combination or a de-merger transaction.

(29) "Financial goodwill", as used in the Spanish fiscal system, amounts to the goodwill that would have been booked if the shareholding company and the participated company would have combined. The financial goodwill concept provided under Article 12(5) TRLIS therefore introduces into the area of share acquisitions a notion usually used in transfer of assets or business combination transactions. According to Article 12(5) TRLIS, the financial goodwill is determined by deducting the market value of the tangible and intangible assets of the acquired company from the acquisition price paid for the shareholding.

(30) Article 12(5) TRLIS provides that the amortization of financial goodwill is conditional upon the following conditions being fulfilled, as set by reference to Article 21 TRLIS:

a) More than 5% of the foreign company must be held directly or indirectly by the Spanish acquiring company for an uninterrupted period of at least one year[10]

b) The foreign company has to be subject to a tax similar to the tax applicable in Spain. Such a condition is presumed to be fulfilled if the country of residence of the target company has signed with Spain a tax convention to avoid double taxation and prevent tax evasion[11] with a clause on exchange of information;

c) The revenue of the foreign company shall mainly derive from business activities carried out abroad, or revenue that could be assimilated. Such a condition is met when at least 85% of the income of the target company:

I is not of the kind subject to the Spanish controlled foreign company (CFC) anti-deferral rules and taxed, as if income earned in Spain[12]. The incomes from the following activities are expressly considered as fulfilling these requirements:

- Wholesale trading, when neither the country of the transfer of the goods nor the one of the clients of the participated company is Spain,
- Services, provided to beneficiaries not fiscally resident in Spain,
- Financial services provided to clients not resident in Spain,
- Insurance services relating to risks not linked to Spain.

10 See Article 21(1)(a) TRLIS.
11 See Article 21(1)(b) TRLIS.
12 See Article 21(1)(c)(1) TRLIS.

II is dividend income, whenever the conditions on the nature of the income of the shareholding provided for Article 21(1)(a) and the level of direct and indirect shareholding of the Spanish shareholder company are fulfilled (Article 21 (1)(c)(2) TRLIS)[13].

(31) In addition to the contested measure, it is worth presenting briefly the following TRLIS'provisions to which the present decision will refer:

- Article 11(4) TRLIS[14], within Article 11 TRLIS entitled "*Correciones de valor: amortizaciones*", which is contained in Chapter IV of TRLIS defining the tax base, provides the amortization of goodwill over minimum 20 years deriving from an acquisition for value under the following conditions: (i) the goodwill results from an outright purchase; (ii) the seller should be unrelated to the acquirer company. The amendments to this provision after the Opening decision, introduced by Law n. 16/2007 of 4 July 2007, further clarified that if condition (ii) is not fulfilled, the price paid used for the calculation of the goodwill will be the price paid for the share acquired by a related company to the unrelated seller and further requests that (iii) an indivisible reserve has been credited to an amount at least equivalent to the amount that has been deducted under Article 12(5) TRLIS.

- Article 12(3) TRLIS, which is contained in Chapter IV TRLIS, permits partial write downs for impairment of domestic and foreign shareholdings, which are not traded on a secondary market, up to the difference of the theoretical accounting value between the beginning and the end of any tax period. The contested measure can apply in conjunction with Article 12(3) TRLIS[15].

- Article 89(3) TRLIS, within Article 89 entitled "*Participaciones en el capital de la entidad transmitente y de la entidad adquirente*", is contained in Chapter VIII, Section VII on "*Régimen especial de las fusiones, escisiones, aportaciones de activos y canje de valores y cambio de domicilio de una sociedad Europea o una Sociedad Cooperativa Europea de un Estado miembro a otro de la Unión Europea*". Article 89(3) TRLIS provides the amortization of goodwill arising from business restructuring. Under this provision, the following conditions have to be fulfilled in order to apply Article 11(4) TRLIS to the goodwill arising from a business combination: (i) a shareholding of at least 5% in the target company before the business combination; (ii) it should be established that the goodwill has been taxed in the hand of a seller (iii) which has to be unrelated to the acquirer. If the condition (iii) is not fulfilled, the amount deducted will have to correspond to an irreversible depreciation of the intangible assets.

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13 See Article 21(1)(c)(2) TRLIS.

14 Under the current legislation, this provision is numbered as Article 12(6) TRLIS.

15 As explicitly stated in the second alinea of Article 12(5): "The deduction of this difference [i.e. Article 12(5) TRLIS] will be compatible, if it were, with the deduction referred to in point 3 of this article."

- Article 21 TRLIS, entitled "*Exención para evitar la doble imposición económica internacional sobre dividendos y rentas de fuente extranjera derivadas de la transmisión de valores representativos de los fondos propios de entidades no residentes en territorio español*", is contained in Title IV TRLIS. Article 21 TRLIS provides for the conditions under which dividends and incomes perceived from a foreign company are tax exempted when perceived by a company which is tax resident in Spain.

- Article 22 TRLIS, entitled "*Exención de determinadas rentas obtenidas en el extranjero a través de un establecimiento permanente*", is contained in Chapter IV TRLIS. Article 22 TRLIS provides for the conditions under which incomes generated by a foreign permanent establishment are tax exempted.

(32) For the purpose of the present decision:

- Transfer of assets shall mean an operation whereby a company transfers without being dissolved all or one or more branches of its activity to another company.

- Business combination shall mean an operation whereby one or more companies, on being dissolved without going into liquidation, transfer all their assets and liabilities to another existing company or to a company that they form in exchange for the issue to their shareholders of securities representing the capital of that other company.

- Share acquisition shall mean an operation whereby one company acquires a shareholding in the capital of another company without obtaining a majority or the control of the voting rights of the participated company.

- Target company shall mean a company not resident in Spain, whose income is fulfilling the conditions described in point (30) c) and in which a shareholding is acquired by a company resident in Spain.

- Intra-EU acquisitions shall mean shareholding acquisitions, which meets all the relevant conditions of Article 12(5) TRLIS, in a Target company which is formed in accordance with the law of a Member State and having its registered office, central administration or principal place of business within the Union.

- Extra-EU acquisitions shall mean any shareholding acquisitions, which meets all the relevant conditions of Article 12(5) TRLIS, in a Target company which has not been formed in accordance with the law of a Member State or not having its registered office, central administration and principal place of business within the Union.

1. III. GROUNDS FOR INITIATING THE PROCEDURE

(33) In the Opening decision, the Commission initiated the formal investigation procedure laid down in Article 108(2) TFEU (former Article 88(2) of the EC Treaty) on the contested measure, because it appeared to fulfil all the conditions to be considered State aid within the meaning of Article 107(1) TFEU. The Commission also had doubts as to whether the contested measure could be considered compatible with the internal market, as none of the exceptions provided for in Article 107(2) and (3) seemed applicable.

(34) In particular, the Commission considered that the contested measure departed from the ordinary scope of the Spanish corporate tax system, which is the tax system of reference. The Commission also held that the fiscal amortization of the financial goodwill arising from the acquisition of a 5% shareholding in a foreign Target company seemed to constitute an exceptional incentive.

(35) The Commission observed that the tax amortization was available only to a specific category of undertakings, namely the undertakings which acquire certain shareholdings, amounting to at least 5% of the share capital of a Target company, and with sole respect to foreign target companies provided that the criteria foreseen by Article 21(1) TRLIS are fulfilled. The Commission also underlined that pursuant to the case law of the Court, a tax reduction favouring only national products being exported constitutes State aid[16]. The contested measure in question therefore seemed selective.

(36) In this context, the Commission also considered that the selective advantage did not appear to be justified by the inherent nature of the tax system. In particular it considered that the differentiation created by the contested measure, which departed from the general rules from the Spanish accounting and tax system could not be justified by reasons linked to technicalities of the tax system. Indeed, goodwill can only be deducted in case of business combination or transfer of assets, except under the provision of the contested measure. The Commission also considered that it was disproportionate for the contested measure to ensure the attainment of the neutrality objectives pursued by the Spanish system because they are only limited to the acquisition of significant shareholdings in foreign companies.

(37) In addition, the Commission considered that the contested measure implied the use of State resources by foregoing tax revenues by the Spanish Treasury. Finally, the contested measure was susceptible to distort competition in the market of European business acquisition by providing a selective economic advantage to Spanish companies engaged in the acquisition of a significant shareholding in foreign companies. The Commission did not either identify any ground for considering the contested measure compatible with the internal market.

[16] See the Judgement of the Court of Justice of 10.12.1969, joined Cases 6 and 11/69, *Commission v France*, [1969] ECR 523. See also point 18 of the Commission Notice on the application of State aid rules to measures relating to direct business taxation, OJ C 384, 10.12.1998, p. 3.

(38) The Commission therefore concluded that the contested measure could represent incompatible state aid. In such a case, recovery should take place according to Article 14 of Council Regulation (EC) n° 659/1999 of 22 March 1999. In this respect, the Commission invited Spanish authorities and interested parties to submit their observations as to the possible presence of legitimate expectations or any other general principle of Community law, which would permit the Commission to exceptionally waive recovery pursuant to Article 14(1), second phrase, of the above mentioned Council Regulation.

IV. THE FIRST PARTIAL NEGATIVE DECISION

(39) In the Previous decision, the Commission concluded that Article 12(5) TRLIS constitutes an aid scheme within the meaning of Article 107(1) TFEU to the extent that it applies to Intra-EU acquisitions.

(40) The Commission also found that the contested measure having been implemented in breach of Article 108(3) TFEU, it constituted an unlawful aid scheme to the extent that it applied to Intra-EU acquisitions.

(41) The Commission maintained the procedure, as initiated by the Opening decision of 10 October 2007, open for Extra-EU acquisitions in light of new elements which the Spanish authorities had committed to provide as regards the obstacles to cross border mergers outside the EU.

V. COMMENTS FROM THE SPANISH AUTHORITIES AND INTERESTED THIRD PARTIES

(42) The Commission received comments from the Spanish authorities[17] and from thirty two interested third parties[18], out of which eight were sent by associations.

(43) In summary, the Spanish authorities consider that Article 12(5) TRLIS constitutes a general measure, not a derogation to the Spanish tax system since this provision allows the amortization of an intangible asset, which applies to any taxpayers purchasing a significant shareholding in a foreign company. In the light of the Commission practice and the case law, the Spanish authorities conclude that the contested measures cannot be qualified as State aid within the meaning of Article 107 TFEU. In addition, the Spanish authorities consider that a different conclusion would violate the notion of legal certainty. The Spanish authorities also contest the competence of the Commission to challenge this general measure: state aid rules would not allow the Commission to harmonize fiscal matters on that basis.

(44) In general, thirty interested third parties (hereinafter "the Thirty parties") support the views of the Spanish authorities, whereas two interested third parties (hereinafter "the Two parties") consider that Article 12(5) TRLIS constitutes an unlawful State aid measure incompatible with the internal market. Hence, the

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17 See point (7) here above.

18 See point (8) here above.

arguments of the Thirty parties will be presented together with the position of the Spanish authorities, whereas the arguments of the Two parties will be described separately in the following sections.

A. COMMENTS FROM THE SPANISH AUTHORITIES AND THE THIRTY PARTIES

(45) As preliminary remarks, the Spanish authorities stress that direct taxation lies within the competence of Member States. Therefore, the Commission's action in this field should be in line with the subsidiarity principle stated in Article 5 EC Treaty [now replaced in substance by Article 5 TFEU]. Moreover, the Spanish authorities recall that Article 3 EC Treaty [now replaced in substance by Article 3 to 6 TFEU] and 58(1)(a) EC Treaty [now replaced by Article 65 TFEU] allow Member States treating investments differently under their tax system, according to the localization or the fiscal residence of the taxpayer, without this being considered as a restriction to the free movement of capital.

(46) The Thirty parties additionally submit that a negative Commission decision would breach the principle of national fiscal autonomy set forth in the TFEU, as well as Article 56 EC Treaty [now replaced by Article 63 TFEU] prohibiting restrictions to the free movement of capital.

A.1 The contested measure does not constitute State aid

(47) The Spanish authorities and the Thirty parties consider the contested measure not to constitute State aid within the meaning of Article 107(1) TFEU since: (i) it does not confer an economic advantage; (ii) it does not favour certain undertakings; (iii) it does not distort or threatens to distort competition between Member States. In line with the logic of the Spanish tax system, they consider that the contested measure should be considered a general measure applying to any type of company and to any activity indiscriminately.

A.1.1 The contested measure does not confer an economic advantage

(48) Contrary to the Commission's position as expressed in the Opening decision, Article 12(5) TRLIS would not constitute an exception to the Spanish corporate tax system since (i) the Spanish accounting system would not be an appropriate point of reference to base the existence of an exception to the tax system; (ii) and even if it were, the characterization of financial goodwill as a depreciable asset over time would have historically been a general feature of Spanish accounting and corporate tax system.

(49) Firstly, because of the lack of harmonisation of accounting rules, accounting statements could not serve as a reference point to establish the exceptional character of the contested measure. Indeed, in Spain, the tax base is calculated on the basis of the accounting statement, as rectified according to fiscal rules.

Therefore, in the case at hand, accounting considerations could not constitute a reference point for a fiscal measure.

(50) Secondly, it would be incorrect to consider goodwill amortization not to be within the logic of the Spanish accounting system since both goodwill[19] and financial goodwill[20] can be amortized over periods up to 20 years. These empirical rules reflect the loss of value of the underlying assets whether intangible or not. Therefore, Article 12(5) TRLIS would not constitute an exception as it would not depart from the rules on amortization of goodwill established in the Spanish accounting and tax systems.

(51) Thirdly, the Spanish authorities point out that the contested measure would not constitute a true economic advantage since, in case of a sale of the acquired shareholding, the amount deducted would be recaptured by taxation of the capital gain, thus placing the taxpayer in the same situation as if Article 12(5) TRLIS would have not been applied.

(52) Fourthly, the Commission would incorrectly refer to Articles 11(4) and 89(3) TRLIS to establish the advantageous feature. In the Opening decision, the Commission states that neither the existence of a business combination, nor the control of the target is necessary to benefit from the Article 12(5) TRLIS. This statement would reflect an inexact understanding of the Spanish tax system since these two articles do not prevent a group of companies acquiring jointly the control of a Target company to deduct a corresponding fraction of goodwill arising from the operation. Hence, there would be no requirements for these two articles to apply of an individual control of the Target company to benefit from the contested measure. In this context, it would be inappropriate to consider that Article 12(5) TRLIS would offer more favourable treatment compared to Article 11(4) or 89(3) TRLIS as regards controlling position of the beneficiaries. Finally, as regards the 5% investment criterion, it should be underlined that it would be consistent with the conditions set under Article 89(3) TRLIS, but also with the Commission directives and practice[21].

(53) The Commission would also refer incorrectly to Article 12(3) TRLIS to establish an alleged advantageous feature of Article 12(5) TRLIS: Article 12(3) would apply to situations of depreciation in case of an objective loss recorded by the acquired company, whereas Article 12(5) TRLIS would complement this provision and reflect the loss of value imputable to the depreciation of the financial goodwill.

(54) Fifthly, the Commission Notice on the application of the State aid rules to measures relating to direct business taxation[22] (hereinafter "the Commission Notice") would explicitly mention that amortization rules would not imply State aid. Since the current amortization ratio of the financial goodwill over minimum

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19 The Spanish authorities referred to Article 194 of the Spanish real decree 1564/1989 of 22.12.1989

20 The Spanish authorities referred to the resolution of ICAC – nº 3, BOICAC, 27.11.1996

21 See Commission decision of 22.09.2004, N 354/2004, Irish Holding Company Regime, OJ C 131, 28.5.2005, p. 10.

22 OJ C 384, 10.12.1998, p. 3.

20 years would be in line with the ratio to amortize goodwill, the rule would not constitute a derogation to the general tax system.

(55) Finally, the Thirty parties also consider that if the contested measure would constitute an advantage, the ultimate beneficiaries would be the acquired company's shareholders since they would perceive the price paid by the acquiring company benefiting from the contested measure.

A.1.2 The contested measure does not favour certain undertakings or production

(56) Firstly, Article 12(5) TRLIS would be a general measure since it would be opened to any Spanish company whatever its activity, sector, size, form or other characteristic. The only condition, provided for in the contested measure, in order for the taxpayer to benefit from such measure, would be to be a tax resident in Spain. The fact that all taxpayers do not benefit from the contested measure would not make it selective. Therefore, Article 12(5) TRLIS could not be either *de jure* selective or *de facto* selective within the meaning of Article 107(1) TFEU. In this perspective, by letter of 14 July 2008[23], the Spanish authorities provided data extracted from the 2006 Spanish tax returns, which would highlight that all types of companies (SMEs and large companies), as well as companies active in different economic sectors, benefitted from the contested measure. The Spanish authorities also underline that, in a recent judgment[24], the General CourtGeneral Court would have indicated that a limited number of beneficiaries should not *per se* turn the contested measure into a selective one since it can represent the whole class of undertakings placed in a similar legal and factual situation. In particular, the Spanish authorities stress that the contested measure would present similarities with a recent case[25] that was considered as a general measure by the Commission, and therefore ask for the same treatment.

(57) Secondly, according to the Spanish authorities and the Thirty parties, the Commission would have mixed up, in its Opening decision, the concept of selectivity and the objective conditions of the contested measure which would be related only to certain transactions (i.e. shareholding in foreign Target company). Indeed, the Commission alleges that Article 12(5) TRLIS is selective since the same treatment would not be granted for comparable investments in Spanish companies. However, the Commission would fail to recognise that the selectivity criterion would not be determined by the fact that the beneficiary of the contested measure is a holding or multinational company that holds shareholding in a Target company. The fact that a measure would only benefit those entities, which comply with the objective criterion set forth in the contested measure, would not make it *per se* selective. The selectivity criterion would imply that subjective restrictions should be imposed on the beneficiary of the contested measure. The selectivity criterion created for this proceeding would be inconsistent with earlier

23 See point (12) here above.

24 See judgement of the General Court of 10.4.2008, case T-233/04, *Netherlands/Commission*, [2008] ECR, II-591.

25 See Commission decision of 14.02.2008, N 480/07, Tax reduction from intangible assets, OJ C 80, 1.4.2008, p. 1.

Commission practice and would be too vague and broad. The expansion of this notion would lead to conclude incorrectly that most of the expenses that are tax deductible fall within the scope of Article 107(1) of the TFEU.

(58) Limiting the amortization of financial goodwill to the one arising from significant shareholdings of a Target company would not be sufficient to remove the general character of the contested measure, since it would apply indistinctively to any company tax resident in Spain without further requirements. In line with the case law of the European Court of Justice[26], a measure that benefits all undertakings in national territory, without distinction, could not constitute State aid.

(59) Thirdly, as regards the 5% threshold, this level would not set a minimum amount to be invested and therefore the contested measure would not only be to the benefit of large companies. As regard the absence of requirement that capital gain were taxed in the hand of the seller for the contested measure to apply, is considered as irrelevant by the Spanish authorities since they would not have competence to control incomes perceived abroad by a non tax resident seller. Finally, limiting, for fiscal technical reason, the scope of a measure to shareholdings acquisitions in Target companies, would be consistent with the situation resulting from the implementation of various Community directives.

(60) Fourthly, the introduction of the contested measure would anyhow be justified by the principle of neutrality, which would inspire the entire Spanish tax legislation. This principle would imply that the fiscal treatment of an investment should be neutral irrespective of the instruments used, whether transfer of assets, business combination or share acquisitions. Therefore, the fiscal amortisation of an investment should be identical whatever the instrument used to carry out the acquisition at stake. The final aim of the contested measure, in this broader perspective, would be to ensure the free movement of capital by avoiding the discriminatory fiscal treatment between transactions with Target companies compared to purely domestic transactions. Given that significant domestic acquisitions could lead to the business combination of the acquiring and acquired companies without any legal or fiscal obstacles, goodwill, which would arise for tax purpose as a result of the combination, could be amortized[27]. However, goodwill of cross border operations could not arise because of the incompleteness of the harmonisation within the Community or even worse, because of the absence of any harmonisation outside the European Union.

(61) Moreover, in the course of the investigation, the Spanish authorities and some Thirty parties provided a quite detailed description of the legal obstacles that would exist in the legislation of 15 Third countries. The technical information contained in the submissions presented by the Spanish authorities and the Thirty Parties are summarized in Annex 2 and 3 of the present decision (hereafter "the Reports"). These descriptions have to be read more broadly in the context of the following statement by the Spanish authorities[28]: "*the Spanish tax system*

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26 See the judgement of the Court of Justice of 08.11.2001, *Adria-Wien Pipeline and Wietersdorfer & Peggauer Zementwerke*, [2001] ECR, I-8365.

27 In application of Article 89(3) TRLIS.

28 See the letter of 5 December 2007 addressed by the Spanish authorities to the Commission, p 35, mentioned in point (7) above.

provides different tax schemes for objectively different situations, as it is the case between domestic shareholding acquisition compared to cross border shareholding acquisition (impossibility to realize business acquisition, risk assumption,...), in order to achieve the tax neutrality which is requested by the Spanish system and by the proper European rules but also in order to achieve a consistent and efficient logic of the Spanish tax system". According to those authorities and the Thirty Parties, the obstacles described in those Reports would make business combinations between companies from different Member States impossible. Therefore, the contested measure would aim at removing the negative impact of these obstacles, whose existence would not be imputable to Spain. Thus limiting the contested measure's scope to cross border acquisitions would be necessary to enforce the neutrality principle. The Spanish tax system would thus treat differently taxpayers placed in different situations[29], therefore ensuring that the Spanish tax system is neutral as required by the proper Spanish tax system and by the TFEU.

(62) As a conclusion, the contested measure would be aimed at removing the fiscal obstacles that the Spanish tax system would generate in the investment decision by penalizing shares acquisitions in foreign companies compared to domestic one. The contested measure guarantees the same tax treatment to two types of acquisitions (direct acquisitions of assets and indirect acquisitions by acquiring shareholdings): goodwill arising from both of them (direct goodwill and financial goodwill) could thus be identified in order to promote the integration of the different markets, until factual and legal obstacles to cross-border business combinations have been removed. The Spanish authorities would thus ensure that taxpayers would choose to invest locally or cross border without being impacted by these obstacles. Indeed, Article 12(5) TRLIS re-establishes a level playing field by suppressing the negative impacts of the obstacles.

A.1.3 The contested measure does not distort competition nor affects the Community trade

(63) The Commission would not have established to the requisite legal standard that Article 12(5) TRLIS would restrict competition, as (i) the alleged "market for the acquisition of shares in companies" does not constitute a relevant market for the purposes of competition law; and (ii) even if it did, the amortization of the financial goodwill does not affect *per se* the competitive position of Spanish undertakings.

(64) First, the Commission would have qualified the contested measure as an anticompetitive advantage on the fact that Article 12(5) would allow Spanish taxpayers to pay a premium for the acquisition of significant shareholdings in a Target company. However, the Commission would have failed to carry out any benchmarking study on the economic reality of the Spanish and international companies.

(65) Second, since the contested measure would be opened to any Spanish company without any limitation, it could not distort competition. Indeed, any company

[29] As stated at p.8 of the Spanish authorities' letter dated 30 June 2008, see point (9) here above.

placed in the same situation than a beneficiary of the contested measure would have the capacity to benefit from the contested measure, by that way it would reduce its fiscal burden and therefore this would suppress any competitive edge that could derive from it. In addition, a lower taxation within a Member State that can increase the competitive edge of local companies should not fall under the State aid rules as long as it would remain general.

(66) Finally, the Commission already would have examined many Spanish cross border operations[30] under the merger regulation that would have been susceptible to have benefited from the contested measure. However under this exercise, the Commission did not raise any concerns about potential competition distortions.

(67) The Commission's allegations would not only be flawed because distant from reality, but would also be foreign to the investment reality of Spanish companies. The contested measure would neither distort competition nor would it adversely affect the conditions of intra-Community trade in a way contrary to the Community interest.

(68) In a non harmonized market, as a result of the competition amongst tax systems, identical operations would have a different fiscal impact depending on the residence of the operators. This situation would distort competition even if the national measures at stake are general measures. This distortion would, in other words, not result from State aid, but from a lack of harmonisation. If the Commission reasoning were to be followed, the Commission would have to open formal investigations on hundreds of national measures and thus would create legal uncertainty highly detrimental for foreign investments.

A.2 Compatibility

(69) Even if the Commission were to consider Article 12(5) TRLIS as a State aid in the meaning of Article 107(1) TFEU , this provision would be compatible with Article 107(3) TFEU since it contributes to the Community interest of promoting the integration of international companies.

(70) As stated in the State Aid Action Plan[31], a measure can be considered as compatible if it addresses a market failure, if it fulfils clearly defined objectives of common interest and if it does not distort intra-Community competition and trade to an extent contrary to the common interest. In the case at hand, the market failure would be the difficulty (or almost the impossibility) to carry out cross-border business combinations. The effect of Article 12(5) TRLIS would be to promote the creation of pan-European undertakings, by placing domestic and cross-border acquisitions on the same foot.

(71) Therefore, Article 12(5) TRLIS would be compatible with the internal market since it would achieve the objective, in the absence of European tax harmonization, of breaking down obstacles to cross-border investment in a

[30] See the Commission decisions of 10.06.2005 on Cesky Telecom, of 10.01.2005 on O2, of 23.05.2006 on Quebec, GIC, BAA, of 15.09.2004 on Abbey National, of 26.03.2007 on Scottish Power available at http://ec.europa.eu/competition/mergers/cases/.

[31] State aid action plan - Less and better targeted state aid: a roadmap for state aid reform 2005-2009, COM/2005/0107 final, OJ L 1, 04.01.2003, p. 1.

proportionate manner. Indeed, the contested measure would be aimed at removing the negative impact of obstacles to cross border business combinations and equalizing the fiscal treatment of cross border business combinations and local ones in order to ensure that the decisions taken as regards such operations would not be based on fiscal considerations, but exclusively on economic considerations.

A.3 Legitimate expectations and legal certainty

(72) Finally, and in the event that the Commission would declare that Article 12(5) TRLIS constitutes State aid incompatible with the internal market, the Commission should accept the existence of certain circumstances that justify the non-recovery of the alleged State aid received pursuant to Article 12(5) TRLIS. The beneficiaries should have the right to complete the outstanding amortization of the financial goodwill in relation to acquisitions carried out before the date on which a final decision is published.

(73) Firstly, the Commission seems to recognize, in the Opening decision, the probable existence of legitimate expectations. Therefore, in line with the case-law of the General Court[32], this statement would constitute clear indicative evidence that legitimate expectations would exist. Since the Opening decision would not prejudge the outcome of the formal investigation, the legitimate expectation should be recognized for all operations, which have taken place before the date of publication of the final decision.

(74) Secondly, in its answers to written questions[33] addressed by members of the European Parliament, the Commission would have stated that Article 12(5) TRLIS would not constitute State aid. This statement would constitute a clear position from the Commission providing obvious legitimate expectations to the Spanish authorities and the beneficiaries of the contested measure.

(75) Thirdly, in line with the conclusion drawn by the Commission in similar cases[34], the Commission would have provided a series of indirect evidence that Article 12(5) TRLIS would not constitute State aid. Taking into account these decisions, a prudent company would not have been able to predict that the Commission could take an opposite position.

(76) Finally, the contested measure should continue to apply to all operations dating from before the publication date of a negative decision until the outstanding amortization of the financial goodwill. Indeed, the contested measure would correspond to a right to deduct a given amount, determined at the moment of the acquisition, whose deduction is fractioned over the following 20 years.

[32] Judgment of the General Court of 12.9.2007, T-348/03, *Koninklijke Friesland Foods v Commission*, [2007] ECR II-101.

[33] Written questions E-4431/05 and E-4772/05

[34] Amongst which the Commission decision of 30.07.2004, case N 354/2004, *Irish Holding Company Regime*, OJ C/131/2004, the Commission decision of 13.07.2006, case C4/2007 (ex. N 465/2006), *Groepsrentebox,* OJ C/131/2005.

Moreover, because of the Commission position in similar cases[35], it would be justified to consider that the legitimate expectation should remain until the date of publication of the final decision.

B. COMMENTS FROM THE TWO PARTIES

(77) According to the Two parties, Article 12(5) TRLIS would constitute State aid. They contest that legitimate expectations are present in the case at hand. Therefore they request the Commission to order recovery of any unlawful aid granted. Their arguments are summarized hereunder.

B.1 The contested measure does constitute State aid

B.1.1 The contested measure confers an economic advantage

(78) Article 12(5) TRLIS would be exceptional in nature due to the fact that the Spanish tax system, with the exception of this provision, would not permit any amortization of financial goodwill but only write downs in the event of an impairment test. Amortization of shareholdings regardless of whether an impairment has actually occurred would not be permitted by the Spanish corporation tax rules until the introduction of Article 12(5) TRLIS. They stress that Article 12(5) TRLIS would be probably unique in Europe in the context of a cross border transactions relating to non controlling shareholdings.

(79) Under the Spanish tax system, with the exception of the contested measure, goodwill could be amortised only if there is a business combination, except under the contested measure that would allow amortisation in an exceptional case: if minority shareholding is acquired in a Target company. This would diverge from the general tax system since the depreciation is available not only in the absence of business combination but also in circumstances where the purchaser would not even acquire control of the foreign target. Article 12(5) TRLIS thus would provide a benefit to certain Spanish companies *vis a vis* both (i) other Spanish companies that operate only at national level and (b) other EU operators, which compete internationally with the Spanish beneficiaries of the contested measure.

(80) From an economic point of view, the Spanish authorities would provide not only an interest free loan, that would be drawn over a period of twenty years (interest free tax deferral), but also would effectively leave to the discretion of the borrower the date of the repayment of the interest free loan, if indeed this loan would be repaid. If the investor would not transfer at all the significant shareholding, the effect would be the same as forgiving debt by the Spanish authorities. The measure would then become a permanent tax exemption.

(81) One of the Two parties estimates that, as a result of the contested measure, Spanish acquirers, for instance in the banking sector, would be able to pay circa 7% more than they would otherwise be able to pay. However, it also recognises that offer price being a combination of various additional elements the contested

[35] See the Commission decision of 31.10.2000, nº 2001/168/ECSC, *Spain's corporation tax laws*, OJ L 60, 1.3.2001, p. 57.

measure would not be the only factor, but probably one of the most important factors determining the aggressiveness of the Spanish bidders benefitting from the contested measure. This party considers also that the contested measure would provide a definite advantage to Spanish bidders in international auctions.

B.1.2 The contested measure favours certain undertakings or production

(82) There would be a clear parallel between the case at stake and the circumstances which lead to the Court judgment of 15 July 2004[36]. Despite the arguments raised by the Spanish authorities that the contested measure in that case would not be selective due to the fact that Article 37 TRLIS would be applicable to all Spanish undertakings investing internationally, the Court concluded that the measure constituted State aid since it was limited to one category of undertakings, namely undertakings making certain international investments. The very same reasoning could be applied to Article 12(5) TRLIS. The selectivity of Article 12(5) TRLIS would therefore result from the fact that only companies acquiring shareholdings in foreign companies are eligible.

(83) In addition, only enterprises of a certain size and financial strength with multinational operations would qualify for the benefit of Article 12(5) TRLIS. Although company's balance sheet disclose assets' book values, it would be unlikely that the assets' fair market values would also be given. Therefore, in practice, only operators with controlling interests in target companies would have sufficient access to a company's records to ascertain the fair market value of the company's assets necessary to implement the contested measure. Accordingly, it would appear that the 5% threshold would favour companies performing multinational operations.

(84) Moreover, only a Spanish operator with existing business in Spain would have the Spanish tax liabilities to realise the benefit of the amortisation. Therefore, only company resident in Spain with a significant Spanish tax base could in reality benefit of this, since the potential benefit would be linked to the size of the Spanish operation and not of the acquisition. Although Article 12(5) TRLIS would be drafted to apply to all operators established in Spain, in practice, only a limited and identifiable number of companies with Spanish tax base, that make foreign acquisitions in the relevant year and which have sizable taxable income against which to set the financial goodwill deduction, would enjoy its benefit on an annual basis. As a result, the contested measure would reserve different tax treatment even for Spanish operators in the same position of making acquisitions abroad.

(85) The Two parties consider that they would not have been able to identify any objective or horizontal criteria or conditions that would justify the contested measure. To the contrary, they are of the view that the contested measure's basic intention would be to provide a benefit to certain Spanish operators. In addition, if the contested measure would be inherent to the Spanish tax system, foreign

[36] Judgment of the Court of Justice of 15.7.2004, case C 501/00, *Spain v. Commission*, [2004] ECR I-6717.

shareholdings acquired prior to that date should also qualify for relief, which is not the case since the tax relief is granted only for shareholdings acquired after 1.1.2002.

(86) As a consequence and taking into account the policy of the Commission[37], the contested measure should be considered as selective.

B.1.3 The contested measure distorts competition and affects Union trade

(87) The contested measure would be clearly discriminatory by providing to the Spanish operators a clear fiscal and monetary benefit that the non Spanish operators are not able to enjoy. In a situation of an auction or other competitive process for the acquisition of Target company, such an advantage would make a significant difference.

(88) Take-over bids would usually presuppose the payment of a premium over the share price of the target that would almost always result in financial goodwill. On various occasions, the financial press would have reported about large acquisitions by Spanish companies and the respective tax benefits accruing from the Spanish tax rules relating to the amortization of financial goodwill. For one of those acquisitions by an investment bank, the tax benefit of Article 12(5) TRLIS would have been estimated to be at € 1.7 billion, or 6.5% of the offer price. Another report indicated that the Spanish acquirer would have been able to bid about 15% more than non Spanish competitors.

(89) The contested measure would also seem to favour certain export activities (export aid for foreign share acquisitions) of Spanish companies, something that is contrary to established Commission policy[38] in this area.

B.1.4 The contested measure impacts State resources

(90) The contested measure would enable the beneficiaries to reduce the amount of their taxable income and thereby the amount of tax that would normally be due in a given year without this provision. It therefore provides the beneficiary with a financial advantage, the cost of which is directly borne by the Member State concerned.

V. REACTION FROM SPAIN TO THIRD PARTIES' COMMENTS

(91) The Spanish authorities note that the vast majority of third parties' comments support their point of view. Only the Two parties would support the qualification of the contested measure as State aid, whereas all the other would reach the conclusion that Article 12(5) TRLIS does not constitute State aid within the meaning of Article 107(1) TFEU. If this would not have been the case, more

[37] See Section II.1.b) ff) of the Commission report on the application of the State aid rules to contested measures relating to direct business taxation, available on http://ec.europa.eu/competition/state_aid/studies_reports/rapportaidesfiscales_en.pdf.

[38] See Commission Decision of 17.05.1982, 82/364/EEC, *subsidizing of interest rates on credits for France to Greece after the accession of that country to the EEC*, OJ L 159, 10.6.1982, p. 44, in particular part IV, which refers to Court cases 6/69 and 11/69, *Commission v. France*.

economic operators would have presented comments. In addition, the diversity as regards the activity and size of the interested third parties would demonstrate the general character of the contested measure.

(92) Regarding the derogatory nature of the contested measure, the Spanish authorities reject this qualification by recalling the common feature of goodwill and financial goodwill amortization according to the Spanish accounting rules[39]. In addition, the deduction of the goodwill amortization would constitute the general rule of the Spanish corporate tax system in accordance with the provisions laid down in Article 11(4) and 89(3) TRLIS. Article 12(5) TRLIS would follow the same logic. Article 12(3) TRLIS would have been incorrectly presented as a general rule of amortization of financial goodwill since this article would refer to the deduction of shareholdings in non listed entities. This provision would be related with the decrease of the theoretical accounting value, not with financial goodwill. Article 12(3) and 12(5) TRLIS would be two complementary general rules: the first would refer to the deductibility of losses generated, whereas the second would refer to the amortization of the financial goodwill. Finally, the fact that no other Member State would have a similar contested measure would be irrelevant since tax system is not harmonized within the European Union.

(93) Regarding the selective character of the contested measure, the parallelism established with the Court judgement of 15 July 2004[40] would be incorrect since in that case the Commission would have clearly defined the profile of the beneficiary, whereas in the present case this could not be done. Indeed, Article 12(5) TRLIS would not require any link between the shareholding acquisition and the export of goods and services. Therefore the effect of the contested measure would not be to increase the export of Spanish goods or services. The fact that this non selective measure would not be available for domestic operations would not affect its general nature. Indeed, the final objective of the contested measure would be shared with the one of the Tax cross border directive which would be to ensure that investment decisions are based on economic and not on fiscal considerations. Therefore, given the possibility to carry out business combinations with domestic acquisitions and not with cross border acquisitions, treating differently domestic operations and cross border operations would be not only legally justified to establish the neutrality of the fiscal tax system but necessary.

(94) Regarding the alleged distortive features of the contested measure, the Spanish authorities recall that any fiscal relief reducing the operating costs of a company would increase the competitive edge of the beneficiary. But this statement would be irrelevant since the contested measure would be a general measure. The different tax rates applied across Member States, which impacts on the competitiveness of its resident companies, would not fall under State aid rules. In addition, it would not have been demonstrated that the contested measure would impact trade between Member States. Moreover, the consequence of amortizing

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39 Refering to the Instituto de Contabilidad y Auditoria de Cuentas' resolution of November 1996, nº 3, BOICAC 27.

40 See footnote 36 here above.

financial goodwill would not be necessarily to increase the price offered by a bidder.

(95) Regarding the compatibility of the contested measure with the Internal market, the Spanish authorities consider Article 12(5) TRLIS to be appropriate and proportionate to address a market failure by establishing a neutral tax system of domestic and cross border operations to favour the development of pan European companies.

VI. ASSESSMENT OF THE SCHEME

(96) In order to ascertain whether a measure constitutes an aid, the Commission has to assess whether the contested measure fulfils the conditions of Article 107(1) TFUE. This provision states that "*Save as otherwise provided in the Treaties, any aid granted by 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, in so far as it affects trade between Member States, be incompatible with the internal market*". In the light of this provision, the Commission will assess hereunder whether the contested measure constitutes State aid.

A. SELECTIVITY AND ADVANTAGE CHARACTER OF THE MEASURE

(97) To be considered State aid, a measure must be specific or selective in that it favours only certain undertakings or the production of certain goods.

(98) The Commission stated in the Commission Notice[41] that "*The main criterion in applying Article 92(1)* [now Article 107(1) TFEU] *to a tax measure is therefore that the measure provides in favour of certain undertakings in the Member State an exception to the application of the tax system. The common system applicable should thus first be determined. It must then be examined whether the exception to the system or differentiations within that system are justified 'by the nature or general scheme' of the tax system, that is to say, whether they derive directly from the basic or guiding principles of the tax system in the Member State concerned.*"

(99) According to the case-law of the Court of Justice[42], "*as regards the assessment of the condition of selectivity, which is a constituent factor in the concept of State aid, it is clear from settled case-law that Article 87(1) EC* [now Article 107(1) TFEU] *requires assessment of whether, under a particular statutory scheme, a State measure is such as to 'favour certain undertakings or the production of certain goods' in comparison with other undertakings which are*

[41] See footnote (22) here above

[42] See, to that effect, judgement of the Court of Justice of 29.4.2004, case C-308/01, *GIL Insurance* [2004] ECR I-4777, paragraph 68, and judgement of the Court of Justice of 3.3.2005, case C-172/03, *Heiser* [2005] ECR I-1627, paragraph 40, judgement of the Court of Justice of 6.9.2006, case C-88/03, *Portugal v. Commission* [2006] ECR I-7115, paragraph 54.

in a legal and factual situation that is comparable in the light of the objective pursued by the system in question"[43].

(100) The Court has also held on numerous occasions that Article 107(1) TFUE does not distinguish between the causes or the objectives of State aid, but defines them in relation to their effects[44]. In particular, fiscal measures, which do not constitute an adaptation of the general system to particular characteristics of certain undertakings, but have been conceived as a means to improve their competitiveness, fall into the scope of Article 107(1) TFUE[45].

(101) The concept of State aid does not apply however to State measures, which differentiate between undertakings where that differentiation arises from the nature or the overall structure of the system of which they form part. As explained in the Commission Notice[46], *'some conditions may be justified by objective differences between taxpayers'.*

(102) As explained in more detail in the following section, the Commission considers that the contested measure is selective in that it only favours certain groups of undertakings carrying out certain investments abroad and that this specific character of the scheme is not justified by the nature of the system. The Commission considers that the contested measure should be assessed in the light of the general provisions of the corporate tax system, and more precisely the rules on the tax treatment of the financial goodwill (see section A.1. hereunder).

(103) The Commission has also analysed whether the factual hypothesis on which the Spanish authorities rely is founded by reviewing whether obstacles are present in Third country legislations. However, it should be stressed that this exercise cannot constitute a recognition that such obstacles could justify a different tax treatment in the present case. Moreover the purpose of the present decision is not to set out the conditions which would have allowed the Member State concerned to avoid the qualification of the contested measure as State aid.

(104) Even if an alternative reference system inspired by the one suggested by the Spanish authorities were chosen, the Commission concludes that the contested measure would still constitute a selective advantage essentially due to the absence of different factual and legal conditions required for the different scenarios benefiting from goodwill or financial goodwill provisions for foreign transactions to apply. Most prominently, the contested measure allows the financial goodwill to arise separately and be amortized also in cases where the beneficiary acquires a minority 5% shareholding, a level far below the one

43 See, to that effect, judgement of the Court of Justice of 6.9.2006, case C-88/03, *Portugal v. Commission* [2006] ECR I-7115, paragraph 54

44 See for instance judgement of the Court of Justice of 29.2.1996, case C-56/93, *Belgium v Commission* [1996] ECR I-723, paragraph 79; judgement of the Court of Justice of 26.9.1996, case C-241/94, *France v Commission*, [1996] ECR I-4551, paragraph 20; judgement of the Court of Justice of 17.6.1999, case C-75/97, *Belgium v Commission*, [1999] ECR I-3671, paragraph 25; and judgement of the Court of Justice of 13.2.2003, case C-409/00, *Spain v Commission*, [2003] ECR I-10901, paragraph 46.

45 See for instance judgement of the Court of Justice of 15.12.2005, case C-66/02, *Italy v. Commission*, [2005] ECR I-10901, paragraph 101.

46 See footnote (22) here above.

required for the general rules related to amortization of goodwill[47] to apply. Therefore the contested measure constitutes an exception from the system of reference, whatever its definition.

(105) In addition to this, the Commission notes other differences as regards the implementing conditions applying to the contested measure and the provisions of the reference system. Indeed, under the contested measure, shareholding acquisitions realised before 1.1.2002 are not taken into account for the calculation of the base to be amortised. By contrast, under a business combination scenario, such a cut off date does not exist when calculating the goodwill and the taxpayer has to prove that the main objective of the combination derives from economic considerations to avoid combinations being aimed at purely obtaining fiscal benefits[48], whereas the contested measure only provides fiscal benefits. The Spanish authorities have not been able to provide convincing arguments to justify these differences, and thus the measure cannot be considered to be justified by the logic of the Spanish tax system.

(106) Hence, the contested measure is too imprecise and indiscriminate by not rendering its benefit conditional upon the presence of specific, legally circumscribed situations which would justify a differentiated fiscal treatment. As a consequence of this, the benefit of the contested measure is extended to situations which have not been sufficiently demonstrated to be differentiated in order to justify a selective derogation to general goodwill rules. Hence, the Commission considers that the contested measure concerns the tax deduction of specific types of costs and covers a broad category of transactions in a discriminatory manner, which cannot be justified by objective differences between taxpayers.

(107) Moreover, in line with the case law of the Court of Justice[49], the Commission considers that it is not necessary, in order to arrive at a conclusion regarding the state aid qualification of a scheme to demonstrate that all individual aid granted under that scheme qualifies as State aid in the meaning of article 107(1) TFEU. For this purpose, it is sufficient that the implementation of the scheme under review leads to situations which qualify as aid to be able to conclude that the scheme contains aid elements in the meaning of Article 107(1) TFUE. Hence, reviewing the legislation of all possible Third countries for which the Commission investigation procedure is still outstanding in the context of the present decision, is unnecessary. Therefore, as indicated already in paragraphs 115 and following of the Previous decision[50], the Commission has verified – on the basis of a methodology explained in detail hereafter - whether some of the individual applications of the contested aid scheme in Extra-EU transactions yield state aid. This analysis was focused on those Third countries with whom Spain maintains tight economic relations and therefore selected according to their importance in terms of foreign direct investment between 1.1.2002 and 1.6.2009 ("FDI"

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47 Article 89(3) TRLIS, see point (31) here above

48 See Article 96 (2) TRLIS

49 See the Judgment of the General Court of 9 September 2009, Joined Cases T-227/01 to T-229/01, T-265/01, T-266/01 and T-270/01, *Diputación Foral de Álava and Others v Commission*, [2006] ECR p. II p.1, points 381 and following.

50 See point (14) here above

hereinafter). Among such Third countries, the Commission has focused its analysis on the countries which were most likely to yield individual applications of the contested measure: United States of America (EUR 35 billion FDI), Mexico (EUR 18 billion FDI), Argentina (EUR 15 billion FDI) and Brazil (EUR 13 billion FDI). According to the information submitted by the Spanish authorities in the course of the procedure, it would appear that, amongst the 15 Third countries for which the Spanish authorities presented information, transactions would have taken place not only in the above mentioned four Third countries but also in the Republic of Colombia, the Republic of Peru and the Republic of Ecuador. The Commission has therefore extended its review also to these additional three Third countries.

(108) This reasoning of the Commission summarized here above is developed in the following paragraphs.

A.1. Tax treatment of the financial goodwill under the Spanish tax system linked to Extra-EU acquisitions

A.1.1. System of reference

(109) In the Opening decision as well as in the Previous decision, the Commission considered that the adequate system of reference is the Spanish corporate tax system, and more precisely the rules on the tax treatment of the financial goodwill contained in the Spanish tax system. This approach is in line with earlier practice of the Commission and with the case-law of the European Courts, which consider the ordinary corporate tax system as the system of reference[51] and is also maintained in the present decision.

(110) The Spanish authorities underline that the constraints imposed on cross border business combinations would, in general, place taxpayers buying shareholdings in domestic companies in a different legal and factual situation than the ones buying shareholdings in non resident companies, and in particular in companies located in Third countries. The objective of the contested measure would be to avoid a difference of tax treatment between, on the one hand, an acquisition followed by an outright business combination and, on the other hand, a share acquisition without business combination. On this basis, the scope of the contested scheme would be limited to the acquisition of significant shareholdings in a company non-resident in Spain because some obstacles would make it more difficult to perform a cross-border business combination as compared to a local one[52]. As a consequence of the existence of these obstacles, Spanish taxpayers investing abroad would be placed, legally and factually, in a different situation than the ones investing domestically. In this respect, the Spanish authorities state that[53]: "*In summary, the mere differential treatment of tax measures does not lead*

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51 See, *inter alia*, judgement of the General Court of 1.7.2004, case T-308/00, *Salzgitter v. Commission*, [2004] ECR II-1933, par. 82.

52 See the Spanish authorities email dated 16 June 2009 mentioned in point (13) here above.

53 See in particular the Spanish authorities letter dated 22 April 2009 (A-9531), page 6 mentioned in point (9) here above.

necessarily to the qualification of the measure as State aid, since this situation can be due to measures which are necessary for the efficiency of the tax system as described in the Notice. Therefore, the fact that the tax system treats differently situations objectively different, as it is the case for acquisitions of shareholding in non resident company or in domestic company (impossibility to realize business combination, risk management, ...) aimed at achieving tax neutrality as imposed by the proper Spanish tax system and the Community Law, as well as ensuring a consistent and efficient logic of the Spanish tax system".

(111) Providing a specific fiscal treatment for cross border shareholding acquisitions would, according to these authorities, be necessary to ensure the neutrality of the Spanish tax system, and avoid domestic shareholding acquisitions to be treated more favourably. Therefore, the Spanish authorities' and Thirty parties' consider that the correct reference framework for the assessment of the contested measure would be the tax treatment of the goodwill for foreign acquisitions.

(112) In the Previous decision, the Commission maintained the procedure open in order to allow the Spanish authorities to provide new information as regards the existence of explicit legal obstacles to cross border business combinations in Third countries.

(113) In this context, the Commission has, essentially on the basis of the elements contained in the Reports, investigated the legislation of various Third countries merely in order to verify the allegations of the Spanish authorities about the existence of explicit legal obstacles to cross border combination, without this examination constituting anyhow a recognition of the fact that such obstacles could justify a different reference system in the present case. To do so, the Commission verified in essence whether a Spanish mother company had the legal capacity to combine with a subsidiary resident in a Third country.

(114) The following premises underpin this investigation limited to the examination of the veracity of the allegations made in the arguments raised:

- First, the Commission has checked whether, as stated in the Previous decision[54], the Spanish companies face an explicit legal barrier, imputable to the Third country concerned and not to Spain[55], that prevent them from converting a foreign subsidiary into a branch. Such legal provisions can however only constitute a barrier if the company concerned would have been able to exercise effective influence, most notably by means of a majority shareholding, over the target company to such a level that it would be able to impose a merger if the obstacles had not been there. Hence, legal provisions from Third countries which impede a Spanish taxpayer to take control of a Target company in that Third country cannot be considered as a relevant explicit legal barrier in the sense alleged by the Spanish authorities: as a result of such provision, Spanish companies/taxpayers can never fulfil the condition of effective influence, as they will remain minority shareholders of the Target company. Therefore, they can never hold

54 See paragraphs 117 and 118 of the Previous decision
55 See, in this sense, point 94 of the Previous decision.

the necessary factual capacity to impose a business combination. The Commission also wants to clarify that the condition of control has been assessed at the level of the beneficiary of the measure (and not of the group to which it may belong) in line with the Spanish tax system. Following the same line of reasoning, the Commission considers that an explicit prohibition for non resident entities to own directly specific assets (immovable property on the seaside for instance) cannot constitute an explicit legal barrier in the context of this exercise.

The Commission considers that a mere administrative burden or formality[56] required from non resident companies by Third countries cannot be considered as an explicit legal barrier, because it should merely generate additional costs - which may be tax deductible under the Spanish tax system – without rendering the business combination impossible.

- Second, an allegation of absence of known examples of cross border business combination between Spanish companies with companies from a given Third country cannot constitute sufficient evidence either proof of the existence of obstacles. Indeed, elements which are taken into account by companies when deciding to realise a business combination are diverse and not limited only to the capacity of the companies concerned to combine the business. This is clearly illustrated by the fact that certain of the Thirty Parties own numerous fully controlled Spanish subsidiaries without having combined their Spanish businesses, even though the Spanish authorities recognise that there are no obstacles to domestic business combinations. Therefore, the Commission considers that amongst the elements contained in the Reports only explicit prohibitions of cross border business combinations under Third countries legislations can be accepted. Indeed, as already indicated in point 93 of the Previous decision, if unsubstantiated elements of general nature were taken into account, this analysis would risk becoming largely arbitrary.

(115) The findings presented hereunder are based on the information provided by the Spanish authorities in the Reports, whose veracity and completeness has been checked by the Commission in the light of the methodological remarks developed above. On this basis, the Commission considers that, contrary to the allegations of the Spanish authorities, not all of the legislations of Third countries can be considered to raise explicit legal obstacles to cross border business combinations. Therefore, similarly to what was stated as regards intra EU transactions in the

[56] The Commission underlines that any technicalities necessary to realize a cross border business combination, such as establishing a permanent establishment in the country of residence of the Target company prior to the combination or complying with certain formalities with Third countries' central bank, constitute administrative formalities. The Commission also considers that there exist valid tax reasons to adopt rules aimed at avoiding arrangements which do not reflect economic reality or whose main reason is to achieve a tax reduction. Such rules also exist in the Spanish tax system.

Previous decision[57], the Commission cannot share the views expressed by the Spanish authorities, supported in their allegations by the Thirty Parties, as regards the generalised existence of these alleged obstacles. The Commission considers that beyond the EU member States, at least in the following relevant Third countries no explicit legal obstacles can be recognised, as described further hereafter:

- *United States of America:*

  i. First of all, the Commission notes, that in a report presented by the Spanish authorities[58], when assessing whether there are precedents of cross border business combinations, the author states "*Not found, but it is likely that this event happened in Delaware*". In contradiction with the Spanish authorities' essential allegations, the conclusion in one of the Reports[59] regarding this country seems to consider that there is no general and explicit legal prohibition to cross border business combinations.

  ii. Second, under the general rules of company law[60] and fiscal[61] law, there is no explicit prohibition to business combinations with foreign entities.

  iii. Third, specific company law provisions[62] apply to domestic business combinations. There is, to the Commission's knowledge, no explicit prohibition to apply those provisions to cross border business combinations, even if the applicable administrative formalities may differ. The Commission underlines that, at least, the State of Delaware makes cross border business combinations[63] explicitly feasible on the condition that a reverse transaction would be allowed by the legislation where the foreign company is resident. Therefore, if such transaction would not be feasible between companies located respectively in Delaware and Spain, the Commission considers that such obstacles would be imputable to Spain, and therefore not relevant for the present assessment. This finding should be put in the perspective of the recognized

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57 See in particular points 93 and following.

58 See page 19 of KPMG report entitled "Analysis of the existence of specific legal and tax obstacles in cross-border mergers in a number of jurisdictions" – December 2009

59 See in Annex 2 of the present decision which presents a summary of the KPMG report, the section regarding United States of America

60 See footnote 61 here under

61 See, amongst other, section 351 and following of the Internal Revenue Code of 1986, as amended, section 7874 of the same code, Treasury Regulation of 23 January 2006 (T.D. 9242) available on http://www.law.cornell.edu/uscode/

62 See footnote 61 here above, See section 361 and following, 367 and following of the Internal Revenue Code http://www.law.cornell.edu/uscode/

63 See, amongst other, section 252(a) of the Delaware General Corporation Law available on: http://delcode.delaware.gov/title8/c001/sc09/index.shtml

importance of the State of Delaware for the localisation/incorporation of companies in USA[64].

iv. Fourth, specific tax provisions apply to domestic business combinations for avoiding adverse taxation when carrying out restructuring operations. There is, to the Commission's knowledge, no explicit prohibition to apply them to cross border business combinations, even if the applicable administrative formalities may differ.

v. Finally, the Commission did not find any case law from competent US courts that would contradict its conclusion as regards the absence of explicit legal obstacles to cross border business combinations with a company resident in the United States of America.

- *Mexican United States:*

  i. First of all, the Commission notes that in Article 8(3) of the tax convention[65] between the Kingdom of Spain and the Mexican United States signed on 24 July 1992 and still in force, cross border business combination transactions are explicitly contemplated. As a consequence of this provision, such transactions benefit from roll-over relief in the sense that unrealised capital gains are not taxed. To the Commission's understanding this international tax convention is intended to supersede the possible exclusion[66] of cross border business combination from the benefit of the specific tax rules applying to domestic business combinations.

  ii. Second, under the Mexican legislation (company law and fiscal law), taking into account the above tax convention, there is no explicit legal prohibition of business combination with Spanish entities.

  iii. Finally, the Commission did not find any case law from competent Mexican courts that would clearly contradict its conclusion as regards the absence of explicit legal obstacles to cross border business combinations with a company resident in the Mexican United States.

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64 According to the official website of the State of Delaware, available on http://www.corp.delaware.gov/aboutagency.shtml, "*The State of Delaware is a leading domicile for U.S. and international corporations. More than 850,000 business entities have made Delaware their legal home. More than 50% of all publicly-traded companies in the United States including 63% of the Fortune 500 have chosen Delaware as their legal home*".

65 Available on http://www.agenciatributaria.es/wps/portal/Listado?channel=de40217740119010VgnVCM100000050f01e0a____&ver=L&site=56d8237c0bc1ff00VgnVCM100000d7005a80____&idioma=es_ES&menu=1&img=8

66 See, amongst other, Article 14(b) of the tax code of the Mexican Federation available on: http://info4.juridicas.unam.mx/ijure/fed/7/18.htm?s=

- *Federative Republic of Brazil:*

  i. First of all, the Commission notes that a precedent of a cross border business combination (not with Spain) was found by the Spanish authorities[67].

  ii. Second, under the general rules of company law and fiscal law[68], there is no explicit legal prohibition of business combinations with foreign entities, although administrative formalities may differ[69].

  iii. Third, some explicit legal restrictions apply to the performance of economic activities in certain sectors[70] by entities controlled by foreign companies. However, as explained above (see point (114)), legal provisions from Third countries, which impede a Spanish taxpayer to take control of a Target company in that Third country, cannot be considered as a relevant explicit legal barrier in the sense alleged by the Spanish authorities: as a result of such provision, Spanish companies/taxpayers can never fulfil the condition of effective influence, as it will remain a minority shareholder of the Target company. To the Commission's knowledge, this is precisely the situation occurring with the Brazilian legislation referred to in the two reports.

  iv. Finally, the Commission did not find any case law that would contradict its conclusion as regards the absence of explicit legal obstacles to cross border business combinations with a company resident in Brazil.

- *Argentine Republic:*

  i. First of all, the Commission notes that in Article 5 of the tax convention[71] between the Kingdom of Spain and the Argentine Republic signed on 26 August 1994 and still in force, cross border business combinations are explicitly contemplated. As a consequence of this provision, cross border restructuring operations shall not trigger adverse taxation.

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[67] See page 29 of the second report. In 2004, Labatt Brewing Canada Holding Ltd, a beverage company headquartered in Bahamas and Beverage Associates Holding Lts, also headquartered in Bahamas, were combined into the Brazilian Companhia de Bebidas das Américas, headquartered in Sao Paolo.

[68] See, amongst other, Lei 10.460/02, Lei 9.249/95, Lei 6.404/76, Lei 9.249/95

[69] See, amongst other, Decreto Lei 2.627/40, Lei 10.406/02, Lei 4.132/62, Lei 5.709/1, Lei 6.634/79 and Federal Decree 74.965/74 available on http://www.jusbrasil.com.br/

[70] See, amongst other, Lei 9.472/97, Decree 2.617/98 available on http://www.jusbrasil.com.br/

[71] Available on http://www.agenciatributaria.es/wps/portal/Listado?channel=de40217740119010VgnVCM10000050f01e0a____&ver=L&site=56d8237c0bc1ff00VgnVCM100000d7005a80____&idioma=es_ES&menu=1&img=8

ii. Second, under the general rules of company law[72] and fiscal[73] law, there is no explicit legal prohibition of a business combination with foreign entities although the applicable administrative formalities may differ.

iii. Third, the Commission did not find any case law that would contradict its conclusion as regards the absence of explicit legal obstacles to cross border business combinations with a company resident in the Argentine Republic. Moreover, the Commission does not share the interpretation given in the two reports to the rulings[74] issued by the tax administration in certain planned cross border transactions. Indeed, these rulings only clarify under which conditions the Argentine fiscal roll over regime may apply, without indicating the existence of a general and explicit prohibition of applying this regime to cross border restructuring operations. Moreover, the interpretation given in the Reports of these specific rulings would contradict the general provision of the tax convention[75] between the Kingdom of Spain and the Argentine Republic mentioned above.

- *The Republic of Ecuador:*

    i. First of all, the Commission notes that under the general rules of company law and fiscal law, there is no explicit legal prohibition of a business combination with foreign entities[76].

    ii. Second, the Commission notes, that a report presented by the Spanish authorities[77] recognises that a cross border business combination would be feasible at the condition that the Spanish acquirer would have set up beforehand a branch in Ecuador.

- *The Republic of Peru:*

    i. First of all, the Commission notes that under the general rules of company law and fiscal law, there is, to the Commission's

72 See, amongst other, Ley de Sociedades Comerciales nº 19.550, Ley nº 25.156 available on http://infoleg.mecon.gov.ar/

73 See, amongst other, Decree 649/97 (Ley del Impuesto de Ganancias), Decree 1344/98 available on http://infoleg.mecon.gov.ar/

74 See dictamen of the AFIP nº 37/1997 of 8 July 1997, nº 6/1998 of 30 January 1998 available on http://biblioteca.afip.gob.ar/

75 Available on http://www.agenciatributaria.es/wps/portal/Listado?channel=de40217740119010VgnVCM10000050f01e0a____&ver=L&site=56d8237c0bc1ff00VgnVCM100000d7005a80____&idioma=es_ES&menu=1&img=8

76 See, amongst others, Ley de Compañias del Ecuador, Ley Organica de Regimen Tributario, Codigo Tributario available on http://www.supercias.gov.ec/

77 See the conclusion of the Annex on the legislation of Equator prepared by Garrigues

knowledge, no explicit legal prohibition of a business combination with foreign entities[78].

ii. Second, the Commission notes that Article 2074 of the Peruvian civil code sets out principles to carry out cross border business combinations and the General corporate act allows business combination of a branch of a foreign entity with a company resident in Peru[79].

iii. Third, the corporate tax act ensures a neutral treatment of a business combination of a branch of a foreign entity with a company resident in Peru[80].

iv. Hence, the Commission understands that, at least, a cross border business combination would be feasible at the condition that the Spanish acquirer would have set up beforehand a branch in Peru.

- *The Republic of Colombia:*

i. First of all, the Commission notes that Superintendencia de Sociedades[81] explicitly confirms that cross border business combination are feasible under the Colombian legislation[82].

ii. Second, under the general rules of company law and fiscal law[83], there is no explicit legal prohibition of a business combination with foreign entities even though the applicable administrative formalities may differ.

iii. Third, the Commission notes, that a report presented by the Spanish authorities[84] recognises that a cross border business combination would be feasible at the condition that the Spanish acquirer would have set up beforehand a branch in Colombia.

(116) The Spanish authorities have presented information on eight other Third country legislations. As already described in point (107), the Commission considers that the above findings are sufficient to confirm that, in any event, even if one were to admit that the existence of legal obstacles to cross-border business combination

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78 See, amongst others, the Civil code, Ley General de Sociedades, Ley del impuesto de la rentaavailable on http://www.supercias.gov.ec/

79 See footnote 3 of the annex on Peru of the Garrigues report.

80 See page 8 of the annex on Peru of the Garrigues report.

81 This institution is described as the technical organismo by which the President of the Colombian republic inspect, control the comercial companies (see http://www.supersociedades.gov.co/ss/drvisapi.dll?MIval=sec&dir=280).

82 See, for instance, the position of the Superintendencia de Sociedades when answering to question registered under the number 220-16478 or number 220-62883 available on http://www.supersociedades.gov.co/ss/drvisapi.dll?MIval=sec&dir=45&id=18036

83 See the Estatuto tributario, available on: http://www.secretariasenado.gov.co/senado/basedoc/codigo/estatuto_tributario.html#14-1

84 See the conclusion of the Annex on the legislation of Peru prepared by Garrigues

would be relevant, the system of reference are the rules on, the tax treatment of the financial goodwill contained in the Spanish system. Nonetheless, when applying the same methodology and criteria as the ones described in point (114) and following the Commission understands, on the basis of the information available, that no explicit legal obstacles to cross border business combinations of a general nature exist in the respective legislations of the Republic of Chile, the Bolivarian Republic of Venezuela, the People's Democratic Republic of Algeria, the Commonwealth of Canada, the Commonwealth of Australia, Japan and the kingdom of Morocco.

(117) Therefore, based on the above findings, the Commission cannot share the views of the Spanish authorities that each individual potential beneficiary of the contested measure would face, be it only in practice, insurmountable obstacles to cross border business combinations.

(118) In the light of the above, the Commission considers that there is no reason to depart from the system of reference of the Opening decision and of the Previous decision: the appropriate reference framework for the assessment of the contested measure is constituted by the general Spanish corporate tax system, and more precisely by the rules on the tax treatment of the financial goodwill contained in the Spanish tax system. This conclusion cannot be affected by the fact that the Commission found two Third countries where explicit legal obstacles exist (India and China). Indeed, as indicated already in point (107) above, in line with the case law of the Court of Justice[85], the Commission considers that it is not necessary, in order to arrive at a conclusion regarding the state aid qualification of a scheme to demonstrate that all individual aid granted under that scheme qualifies as State aid in the meaning of article 107(1) TFEU.

(119) More precisely, as regards China, the Company Law of 2005 for mergers involving only limited liability companies or joint stock limited companies established in China Mainland as well as Articles 2 and 55 of the regulation entitled "Provisions on Acquisitions of Domestic Enterprises by Foreign Investors", issued by the Chinese Ministry of Commerce on 22.6.2009, explicitly exclude non-resident companies from the scope of application of the business combination rules to such an extent that a Spanish company would not be able to combine its business with a Chinese controlled subsidiary.

(120) With reference to the legislation in force in India, the Indian Companies act of 1956 in sections 391 to 394 explicitly excludes non-resident companies from the scope of application of the business combination rules, in such a way that a Spanish company would not be able to combine its business with any Indian controlled subsidiary.

[85] See the Judgment of the General Court of 9 September 2009, Joined Cases T-227/01 to T-229/01, T-265/01, T-266/01 and T-270/01, *Diputación Foral de Álava and Others v Commission*, [2006] ECR p. II p.1, points 381 and following.

A.1.2. Existence of a derogation from that system of reference

(121) Under the Spanish tax system, the tax base is calculated from the accounting statement, to which adaptations are made by applying specific tax rules. As preliminary remarks and in subsidiary order, the Commission notes that the contested measure derogates from the Spanish accounting system. The appearance of financial goodwill can only be computed in abstract by consolidating the accounts of the Target company with the ones of the company holding the participation. However, under the Spanish accounting system, the consolidation of accounts is required in case of "control"[86] and is done both for domestic and foreign associations of companies, in order to provide the global situation of a group of companies subject to unitary control. Such a situation is deemed[87] to take place, for instance if the majority of voting rights of the associate company is held by the mother company. Nonetheless, the contested measure does not require any such type of control and applies as from a 5% level of shareholding. Finally, the Commission also observes that, starting from 1 January 2005[88], financial goodwill can no longer be amortized anymore by most of Spanish companies under accounting rules. Indeed, in this respect the Thirty Parties refer to provisions[89] not in force anymore under the current Spanish accounting system. Due to the Law 16/2007 of 4 July 2007 on the reform and adaptation of the accounting rules for its International harmonization in line with European Union legislation, as well as Royal Decree 1514/2007 of 16 November 2007 on the General Accounting Plan, from an accounting point of view, the amortization of goodwill or of the financial goodwill are not allowed anymore. These modifications of the Spanish accounting law are in line with Regulation n° 1606/2002 of the European Parliament and of the Council of 19 July 2002 on the application of international accounting standards[90]. Therefore, given these considerations, the contested measure constitutes an exception from the ordinary accounting rules applicable in Spain.

(122) This being said, because of the fiscal nature of the contested measure, the existence of a derogation has to be assessed in comparison to the fiscal system of reference, and not on a pure accounting basis. In this context, the Commission notes that the Spanish tax system has never made possible the amortization of the financial goodwill, except under the Article 12(5) TRLIS. In particular no such amortisation is possible for domestic transactions. This is highlighted by the following elements:

(123) For Spanish tax purposes, goodwill can only be separately booked following a business combination[91], which materialises either in case of acquisition or contribution of the assets composing an independent business, or following a legal business combination. In such cases, the goodwill arises as the accounting

86 In application of Article 42 of the *Codigo de Comercio de 1885*.

87 See Article 42(1) of the *Codigo de Comercio de 1885*.

88 Companies having issued securities admitted to trading on a regulated market of any Member State within the meaning of Article 1(13) of Council Directive 93/22/EEC, in application of Article 4 of the mentioned regulation.

89 Article 194 of the Real Decree 1564/1989 of 22 December 1989 of Ley de Sociedades Anónimas.

90 OJ L 243, 11.09.2002, p. 1.

91 In application of Article 89(3) TRLIS

difference between the acquisition cost and the market value of the assets composing the business acquired or held by the combined company. When the acquisition of a business of a company is made by way of the acquisition of its shares, as it is the case for the contested measure, goodwill can only arise if the acquiring company combines subsequently with the acquired company, of which it shall thus have control.

(124) However, under the contested measure, control is not necessary, nor is the combination between the two businesses. The mere acquisition of a shareholding of at least 5% of a foreign company is sufficient. Thus, by allowing the financial goodwill, which is the goodwill that would have been booked if the businesses would have combined, to arise separately even in the absence of a business combination, the contested measure constitutes an exception to the system of reference. It should be stressed that the derogation does not result from the duration of the period during which the financial goodwill is amortized as compared to the period applying for amortising traditional goodwill[92], but rather on the different treatment of domestic and cross border transactions. The contested measure cannot be considered a new general accounting rule in its own right because the amortisation of financial goodwill deriving from the acquisition of domestic shareholdings is not allowed.

(125) Given all the above considerations, the Commission concludes that the contested measure constitutes a derogation from the system of reference. As demonstrated further in paragraphs (153) to (163)(163), the Commission considers that neither the Spanish authorities nor the Thirty parties have advanced any argumentation which would be sufficiently articulated to alter this conclusion.

A.1.3. Existence of an advantage

(126) Article 12(5) TRLIS allows to deduct from the tax base part of the financial goodwill deriving from the acquisition of shareholdings in foreign company in derogation to the system of reference. Therefore, by reducing the tax burden of the beneficiary, Article 12(5) TRLIS provides them an economic advantage. It takes the form of a tax reduction, to which the companies concerned would otherwise be subject to. This reduction is proportionate to the difference between the acquisition price paid and the market value of the underlying booked assets of the shareholdings purchased.

(127) The precise amount of the advantage with respect to the acquisition price paid corresponds to the net discounted value of the tax burden reduction provided by the deductible amortization during the whole amortization period following the acquisition. It is therefore contingent on the company tax rate in the years concerned and on the discount interest rate applicable.

(128) In the event that the acquired shareholdings are resold, part of this advantage is indeed recaptured by means of capital gain taxation. Indeed, by allowing amortisation of financial goodwill, if the foreign shareholding in question is resold, the amount deducted would lead to an increase of the capital gain taxed at

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[92] In application of Article 11(4) TRLIS

the moment of the sale. However, if such uncertain circumstance arises, the advantage does not disappear completely since the taxation at a later stage does not take into account the liquidity cost. As rightly pointed out by the Two Parties, from an economic point of view, the amount of the advantage is at least similar to the one of a free credit line allowing up to twenty annual withdrawals of a twentieth of the financial goodwill for a duration as long as the shareholdings are held on the book of the taxpayer.

(129) By means of hypothetical example, as already mentioned by the Commission in the Opening decision, a participation acquired in 2002 would yield an advantage corresponding to 20,6 % of the financial-goodwill amount, assuming a discount interest rate of 5 %[93] and considering the existing structure of company tax rates over the years until 2022 as currently set by Law No 35/2006[94]. Third parties have not contested these figures. In the event that the acquired shareholdings are resold, the advantage would correspond to the interests that would have been charged on the taxpayer for a credit line presenting the characteristics described in the previous paragraph.

(130) Finally, the Commission cannot share the views of the Spanish authorities and the Thirty parties that the final beneficiary of the contested measure would only be the seller of the foreign shareholding since they would perceive a higher price. The Commission reject this argument after assessing the effect of the contested measure as it is now designed. First, there is no mechanism guaranteeing that the advantage is passed on in full or in part to the seller. Second, the acquisition price results from a series of different elements, not just from the contested measure. Third, even if the two above conditions would be fulfilled, the Spanish taxpayer benefiting from the contested measure should still be considered as a beneficiary of the measure. Indeed, even if an economic advantage would be transferred to the seller, the contested measure would still provide for the acquirer an increase capacity to offer higher price which is of upmost importance in case of competitive acquisition operation.

(131) Therefore, the Commission concludes that, in any event, the contested measure provides an advantage at the moment of the acquisition of foreign shareholdings.

A.1.4. Justification of the measure by the logic of the Spanish tax system

(132) The Commission considers that, under the settled case law of the Court[95], the measures introducing a differentiation between undertakings when that differentiation arises from the nature and overall structure of the system of

93 As stated in TRLIS modified by the Law 35/2006, the standard corporate tax rate used for the calculation has been 35% from 2002 to 2006, 32,5% in 2007, 30% onward.

94 Disposición adicional octava, Ley 35/2006, de 28 noviembre, del Impuesto sobre la Renta de las Personas Físicas y de modificación parcial de las leyes de los Impuestos sobre Sociedades, sobre la Renta de no Residentes y sobre el Patrimonio, B.O.E. Nº 285, 29/11/2006

95 See case C-88/03, *Portugal v. Commission*, paragraph 81 see footnote 49 here above, See judgement of the General Court of 9.9.2009, case T-227/01, *Territorio foral de Alava and others*, [2006] ERC II-1, paragraph 179 and judgement of the General Court of 9.9.2009, case T-230/01, *Territorio foral de Alava and others*, [2009] ERC II-139, paragraph 190.

charges of which they form part do not constitute State aid. This justification based on the nature or overall structure of the tax system reflects the consistency of a specific tax measure with the internal logic of the tax system in general.

(133) In this regard, the Commission considers, firstly, that the Spanish authorities have not demonstrated that the effect of the contested measure would be to eliminate double taxation. The scheme in fact does not provide any condition to prove that the seller has been effectively taxed on the gain derived from the transfer of the shareholding, even though such a condition is imposed for amortizing the goodwill arising from a business combination[96]. It should be underlined that although the Spanish authorities claim not to be competent to exercise control on a foreign seller realising operations abroad, the Commission notes that such condition is required for the application of other Spanish tax provisions[97] but not for the contested measure.

(134) Secondly, the contested measure does not either constitute a mechanism to avoid double taxation of future dividends that would be taxed upon realisation of future profits and should not be taxed twice when distributed to the company holding a significant shareholding for the acquisition of which financial goodwill was paid. Indeed the contested measure creates no relation between the dividends perceived and the deduction enjoyed owing to the contested measure. To the contrary, the dividends received from a significant shareholding in a foreign company already benefit from both the exemption provided for by Article 21 TRLIS and the direct tax neutrality provided for by Article 32 TRLIS to avoid international double taxation. In this respect, the amortization of the financial goodwill results in an additional advantage with respect to the acquisition of significant shareholdings in foreign companies.

(135) Thirdly, the Spanish authorities have not demonstrated that the contested measure would be an extension of the impairment rules which presuppose that there is objective evidence of losses based on a detailed and objective calculation that is not required by the contested measure. To the contrary, Article 12(3) TRLIS permits partial write downs of domestic and foreign shareholdings which are not traded on a secondary market for impairments occurring between the beginning and the end of any tax period. The contested measure – which is, for beneficiaries, compatible with Article 12(3) TRLIS[98] - provides for further deductions beyond the decrease of the theoretical accounting value linked to impairment.

(136) Fourthly, the Commission notes that the financial goodwill deriving from the acquisition of domestic shareholdings cannot be amortized whereas the amortization of financial goodwill of foreign companies is amortized under certain conditions. A different tax treatment of the financial goodwill of foreign company over domestic ones is a differentiation made by the contested measure which is neither necessary nor proportionate in the light of the logic of the tax

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96 In application of Article 89(3)(a)(1) TRLIS.

97 See Article 89 TRLIS, Article 21 TRLIS, Article 22 TRLIS.

98 As explicitly stated in the second alinea of Article 12(5) stating that "The deduction of this difference (i.e. Article 12(5) TRLIS) will be compatible, if it were, with the deduction to which refers point 3 of this article."

system. Indeed, the Commission considers that it is disproportionate for the scheme at hand to impose substantially different nominal and effective taxation on companies being in comparable situations just because some of them are involved in investment opportunities abroad.

(137) Moreover, the Commission understands the comments made by one of the Thirty Parties[99], to mean that even the rationale of the justification brought forward by Spain would be contrary to the logic of the Spanish tax system. Indeed, according to this submission, under a cross border business combination scenario, the goodwill that would arise would, in all likelihood, be located abroad, more precisely in the foreign permanent establishment resulting from the dissolution of the Target company. Therefore, according to this submission, even under a cross border business scenario, Spain would not allow goodwill to be amortised in Spain as the goodwill is not located in Spain. In addition to this, the Commission notes additional differences in the conditions applying to each of these two scenarios. Indeed, under the contested measure, shareholding acquisitions realised before 1.1.2002 are not taken into account for the calculation of the base to be amortised. However, under a business combination scenario, such a cut off date does not exist when calculating the goodwill. Moreover, under a business combination scenario, the taxpayer has to prove that the main objective of the combination derives from economic considerations to avoid combinations not only aimed at obtaining fiscal benefit[100], whereas the contested measure only provides fiscal benefits. The Spanish authorities have not been able to provide convincing arguments to justify these differences, which are thus to be considered as not being duly justified by the logic of the Spanish tax system.

(138) Finally, the Spanish authorities also argue that the contested measure is justified by the neutrality principle to be applied in the area of company tax[101]. Indeed, the statement of reasons of the tax company law[102] in force when the contested measure was introduced would clearly refer to this principle. In this respect, the Commission notes that the "*competitiveness principle*"[103] invoked by the Spanish authorities, which expressly refers to "*an increase of exports*" also drives this reform. In this context, it should be recalled that according to previous Commission's decisions[104], it is disproportionate to grant a different effective taxation to companies being in comparable situations just because some of them are involved in export related activities or pursue investment opportunities abroad. In addition, the Commission recalls that accordingly the Court stated

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99 See comments received from Telefonica on 20 september 2010, page 2.

100 See Article 96(2) TRLIS

101 See in particular point (60) above.

102 Tax Company Law 43/1995 which was derogated by Real legislative decree 4/2004.

103 Defined by the Spanish authorities in the statement of reasons of the Law 43/1995, as "The competitiveness principle looks for the corporate tax system to support and be consistent with the economical policy initiative in the field of competitiveness. […], and the incentive for the internationalisation of the company as long as this leads to an increase of the export derive from this principle."

104 See, inter alia, Commission Decision 22.3.2006 on direct tax incentives in favour of export related investments OJ C 302, 14.12.07, p.3, par. 51.

that[105] "*[...]whilst the principles of equal tax treatment and equal tax burden certainly form part of the basis of the Spanish tax system, they do not require that taxpayers in different situations be accorded the same treatment. [...]* ".

(139) In the light of the above, the Commission considers that the neutrality principle cannot justify the contested measure. Indeed, as highlighted also by the Two Parties, the fact that the acquisition of 5 % minority shareholdings which have been acquired after a given date benefits from the contested measure demonstrates that the contested measure would include certain situations which bear no significant similarity. In this manner it could be said that, under the reference system, situations which are both factually and legally different are treated in an identical manner. The Commission considers therefore that the neutrality principle cannot be invoked to justify the contested measure.

(140) Given the above considerations, the Commission concludes that the selective advantage character of the tax scheme in review is not justified by the nature of the tax system. Therefore, the contested measure is to be considered as including a discriminating element, in the form of a limitation regarding the country in which the transaction benefiting from a tax advantage is to take place, discrimination which is not justified by the logic of the Spanish tax system.

A.2. Complementary reasoning: Analysis of the contested measure under a reference system inspired by the one suggested by the Spanish authorities

(141) Although the Commission considers, as explained in the previous paragraphs, that the arguments raised by the Spanish authorities rely on an improper analysis of the factual legislation of Third countries, similarly to what was already done in the Previous decision, the Commission also analysed the contested measure under a hypothetical system of reference inspired by the one suggested by the Spanish authorities.

(142) The Spanish authorities have explained that the objective of the contested measure would be to avoid a difference of tax treatment between, on the one hand, an acquisition followed by an outright business combination and, on the other hand, a share acquisition without business combination. On this basis, the scope of the contested scheme would be limited to the acquisition of significant shareholdings in a company non-resident in Spain because some obstacles would make it more difficult to perform a cross-border business combination as compared to a local one[106]. As a consequence of the existence of these barriers, Spanish taxpayers investing abroad would be placed, legally and factually, in a different situation than the ones investing domestically. Indeed, the Spanish authorities state that[107]: "*In summary, the mere differential treatment of tax measures does not lead necessarily to the qualification of the measure as State aid, since this situation can be due to measures which are necessary for the efficiency of the tax system as described in the Notice. Therefore, the fact that*

[105] See paragraph 127 of the judgement mentioned in footnote 36 above.

[106] See the Spanish authorities email dated 16 June 2009 mentioned in point (13) here above.

[107] See in particular the Spanish authorities letter dated 22 April 2009 (A-9531), page 6 mentioned in point (9) here above.

the tax system treats differently situations objectively different, as it is the case for acquisitions of shareholding in non resident company or in domestic company (impossibility to realize business combination, risk management, ...) aimed at achieving tax neutrality as imposed by the proper Spanish tax system and the Community Law, as well as ensuring a consistent and efficient logic of the Spanish tax system." Hence, providing a specific fiscal treatment for cross border shareholding acquisitions would, according to these authorities, be necessary to ensure the neutrality of the Spanish tax system, and avoid domestic shareholding acquisitions to be treated more favourably. Therefore, the Spanish authorities' and the Thirty parties consider that the correct reference framework for the assessment of the contested measure should be the tax treatment of the goodwill for foreign acquisitions.

(143) Nonetheless, the Commission remarks that, even under such an alternative system of reference that could be defined as the tax treatment of goodwill and financial goodwill deriving from an economic interests taken in a company resident in a country other than Spain, the contested measure still constitutes a derogation which is not within the logic of the Spanish tax system. Indeed, the fact that the acquisition of 5 % minority shareholdings which have been acquired after a given date benefits from the contested measure demonstrates that the contested measure would include certain situations which bear no significant similarity with other transactions requiring at least majority control. In this manner it could be said that, under this hypothetical alternative reference system, situations which are both factually and legally different are treated in an identical manner. The Commission considers therefore that the contested measure constitutes a derogation even under this alternative system of reference and that the neutrality principle cannot be invoked to justify it.

B. PRESENCE OF STATE RESOURCES

(144) The measure implies the use of State resources by foregoing tax revenues for the amount corresponding to the reduced tax liability of the companies taxable in Spain acquiring a significant shareholding in foreign companies, for a period of minimum 20 years following the acquisition.

(145) The foregoing of tax revenues mitigates the charges which are normally included in the budget of an undertaking and which thus, without being subsidies in the strict sense of the word, are similar in character and have the same effect. Likewise, a measure allowing certain undertakings to benefit of a tax reduction or to postpone payment of tax normally due amounts to State aid. From a budget point of view and in line with the Court's case law[108] and the Commission Notice[109], the contested measure leads to a loss of tax revenue for the State, resulting from the reduction in the tax base, which is equivalent to consumption of State resources.

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[108] See judgement of the Court of Justice of 10.1.2006, case C-222/04, *Cassa di Risparmio di Firenze and others* [2006] ERC, I-289.

[109] See footnote (21) here above. In particular, see point 9 and 10 of the Commission Notice.

(146) For these reasons, the Commission considers that the contested measure involves State resources being used.

C. DISTORTION OF COMPETITION AND TRADE BETWEEN MEMBER STATES

(147) According to the Court's case law[110], " [...] *for the purpose of categorising a national measure as prohibited State aid, it is necessary, not to establish that the aid has a real effect on trade between Member States and that competition is actually being distorted, but only to examine whether that aid is liable to affect such trade and distort competition. In particular, when aid granted by a Member State strengthens the position of an undertaking compared with other undertakings competing in intra-Community trade, the latter must be regarded as affected by that aid. [...] In addition, it not necessary that the beneficiary undertaking itself be involved in intra-Community trade. Aid granted by a Member State to an undertaking may help to maintain or increase domestic activity, with the result that undertakings established in other Member States have less chance of penetrating the market of the Member State concerned.* " Moreover, under settled case law of the Court[111], for a measure to distort competition it is sufficient that the recipient of the aid competes with other undertakings on markets open to competition. The Commission considers that the conditions set out in the case law are fulfilled for the following reasons.

(148) First, the contested measure provides an advantage in terms of financing and therefore, it strengthens the position of the economic unit that can be formed by the beneficiary and the Target company. In that regard and in line with the Court's case law[112], the mere fact of owning controlling shareholdings in a participated company and exercising that control by involving itself directly or indirectly in the management thereof, must be regarded as taking part in the economic activity carried on by the controlled undertaking.

(149) Second, the contested measure is liable to distort competition, most prominently amongst European competitors, by providing a tax reduction to Spanish companies engaged in acquisition of a significant shareholding in Target companies. This analysis is confirmed by the fact that several companies have complained and / or intervened after the Opening decision to state that the contested measure provided a significant advantage fuelling the merger appetite of Spanish companies, in particular in the context of auction processes. These interventions confirm at least that a series of non Spanish companies consider that their position on the market is affected by the contested measure, irrespective of the correctness of their detailed submissions as regards the existence of aid.

(150) The Commission would finally like to underline that the selective advantage is granted to companies which are Spanish taxpayers, and not to the Extra-EU

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110 See footnote 42 points 139 – 143.

111 Judgement of the General Court, case T-214/95, *Vlaams Gewest v. Commission*, [1998] ECR II-717.

112 See the judgement of the Court in case C 222/04 already cited in footnote 108 above.

activity of the Spanish taxpayer. Indeed, the tax base which is eroded is the one which derives from the taxable economic activity in Spain. Hence, the advantage is granted directly to the activity of the beneficiary which is carried out in Spain, and not in the Extra-EU permanent establishment. Therefore, in the light of this fact, the Commission considers that it cannot be argued, in the case at hand, that the advantage could not distort competition or trade between Member States to the extent the contested measure applies to Third countries. The advantage being granted upon objective conditions related to transactions with Extra-EU countries does not alter the fact that the effect of the measure results in an erosion of the tax base deriving from an economic activity carried out within the internal market.

(151) Therefore the Commission concludes that the contested measure is liable to affect trade between Member States and distort competition, most prominently in the internal market, by potentially improving the operating conditions of the beneficiaries being directly engaged in economic activities, which are liable to pay tax in Spain.

D. COMMISSION REACTION TO THE COMMENTS RECEIVED

(152) Before concluding on the qualification of the measure, the Commission considers it appropriate to analyse in more detail certain arguments raised by the Spanish authorities and by third parties, which have not yet been explicitly or implicitly addressed in paragraphs concerning the assessment of the scheme (points (96) and following).

D.1. Reaction to the data extracted from the 2006 tax returns and to the comments about Court judgement C-501/00

(153) As regards the data extracted by the Spanish authorities from the 2006 tax returns in order to demonstrate the absence of selectivity of the contested measure[113], the Commission underlines the general lack of precision of the information submitted. First, the data presents the distribution of beneficiaries per classes (class of activity, class of turnover), but does not indicate whether the beneficiaries concerned represent a small or important part of each of the classes concerned. Secondly, although statistics based on the importance of the turnover of the beneficiaries could be an interesting indicator in order to demonstrate that the contested measure applies to all companies in Spain, it must be underlined that the contested measure is related to the acquisitions of shareholdings. Such an investment does not necessarily generate significant turnover, implying that holding companies for instance may be included as SMEs under the data concerned. Therefore, for the data to be considered as relevant, it would be necessary to take into account additional indicators, such as the total balance sheet figures, as well as whether the beneficiaries can tax consolidate their tax base with other Spanish taxpayers. Thirdly, the data also appear unrepresentative because they contain no indication on the level of shareholdings acquired (control or only minority shareholdings) by the beneficiaries. Finally, the data received do not provide any indication allowing determining whether the conditions of the

[113] See point (12) above.

2003 SME Recommendation of the Commission[114] are fulfilled. Therefore the Commission considers that its demonstration that the contested aid measure is selective due to the sole characteristics of the legislation at stake is not undermined by the partial and unrepresentative data provided by the Spanish authorities.

(154) Nonetheless, even if the arguments presented by the Spanish authorities had been complemented by additional evidence, this would not remove the selective feature of the contested measure as only certain undertakings do benefit from the measure also in the meaning of the Court judgment in case C-501/00 *Spain v Commission*[115]. Indeed, as regards the qualification of the measure as general measure[116] by the Spanish authorities for being opened to any undertakings resident in Spain, it is worth recalling this judgment of the Court. That case also concerned an exception to the Spanish company tax, more particularly a measure entitled "Deduction for export activities". The Spanish authorities contended before the Court that the scheme was open to any undertaking tax resident in Spain. However, the Court considered that the tax deduction could "*benefit only one category of undertaking, namely undertakings which have export activities and make certain investments referred to by the contested measure*"[117]. The Commission considers that also in the present case, the contested measure aims at favouring the export of capital out of Spain, in order to strengthen the position of Spanish companies abroad, thereby improving the competitiveness of the beneficiaries of the scheme.

(155) In this respect it is noteworthy that according to the Court of Justice, "*in order to justify the contested measures with respect to the nature or the structure of the tax system of which those measures form part, it is not sufficient to state that they are intended to promote international trade. It is true that such a purpose is an economic objective but it has not been shown that that purpose corresponds to the overall logic of the tax system. [...] The fact that the contested measures pursue a commercial or industry policy objective, such as the promotion of international trade by supporting foreign investment, is thus not sufficient to take them outside the classification of 'aid' within the meaning of Article 4(c) CS.* "[118]. In the present case, the Spanish authorities have simply declared that the contested measure intends to promote international trade and the consolidation of companies, without proving that such a measure is justified by the logic of the system. In the light of the above, the Commission confirms its analysis that the contested measure is selective.

D.2. Reaction to the comments on Commission practice

(156) As regards the reference made to alleged innovative interpretation of the notion of selectivity in the present case, it should first be underlined that this approach is fully in line with the Commission's decision making practice and the case law of the Court as described in point (109). The approach in this particular case does

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[114] OJ L 124 of 20.5.2003, p. 36.

[115] See footnote 36 above.

[116] See in particular points (43) and (56) above.

[117] See Case C-501/00, in particular paragraph 120 of the judgment.

[118] See Case C-501/00, footnote 36 above, paragraph 124 of the judgement.

not either depart from the Commission decision N 480/2007[119] to which the Spanish authorities refer. Indeed, this decision took into account the specific nature of the objective pursued by referring[120] to the Communication from the Commission to the Council, the European Parliament and the European Economic and Social Committee - Towards a more effective use of tax incentives in favour of R&D[121]. In the case at hand, the objective pursued by the contested measure does not follow such a similar objective. Moreover, unlike the present case, the Spanish measure at stake in the Commission decision N 480/2007did not make any distinction between national and international transactions.

(157) Finally, as regards the derogation to the corporate tax system resulting from the implementation of directives[122], such as the Parents-subsidiary directive or the Cross-border Interest and Royalty payments directive, the Commission considers that the situation resulting from the implementation of these directives is fully consistent with the reasoning developed in the present decision. Indeed, resulting from the harmonisation within the European Union, cross border operations within the European Union and within each Member States should be considered to be in a comparable legal and factual situation. In addition, the Commission would like to underline that the General Court stated that[123]: "*as Community law stands at present, direct taxation falls within the competence of the Member States, although it is settled case-law that they must exercise that competence consistently with Community law (see, in particular, Case C-391/97 Gschwind [1999] ECR I-5451, paragraph 20) and therefore avoid taking, in that context, any measures capable of constituting State aid incompatible with the common market.*"

D.3. Reaction to the comments on Article 65(1)(a) TFEU

(158) As already pointed out before, it must be borne in mind that, although direct taxation falls within competence of Member States, they must none the less exercise that competence consistently with Community law[124], including the provisions of the Treaty on State aid. Article 65(1)(a) TFEU only limits the scope of Article 63 TFUE and does not affect in any way the application of the Treaty rules on State aid including those granting control competences to the Commission in that area.

(159) Moreover, Article 65 of the TFEU, as invoked by the Spanish authorities, must be read together with Article 63 of the TFEU, which prohibits restrictions on the movement of capital between Member States. In fact, Article 65(1) of the TFEU provides that "*the provisions of Article 63 shall be without prejudice to the right of Member States: (a) to apply the relevant provisions of their tax law which*

119 See footnote 25 and point (56) above

120 See Commission decision of 14.02.2008, case N 480/07 already cited in footnote 25 above.

121 SEC (2006) 1515, COM/2006/0728 final, section 1.2.

122 See point (59) above.

123 See paragraph 123 of the judgment of the Court of Justice in case C-501/00, cited in footnote 36.

124 See judgment of the Court of Justice of 11.8.1995, case C-80/94, *Wielockx* [1995] ECR I-2493, paragraph 16; judgment of the Court of Justice of 11.12.1997, case C-264/96, *ICI* v *Colmer (HMIT)* [1998] ECR I-4695, paragraph 19; and judgment of the Court of Justice of 29.4.1999, case C-311/97, *Royal Bank of Scotland* [1999] ECR I-2651, paragraph 19

distinguish between taxpayers who are not in the same situation with regard to their place of residence or with regard to the place where their capital is invested".

(160) The possibility granted to the Member States by Article 65(1)(a) of the Treaty, of applying the relevant provisions of their tax legislation which distinguish between taxpayers according to their place of residence or the place where their capital is invested, has already been upheld by the Court. According to that case-law before the entry into force of Article 65(1)(a) of the Treaty, national tax provisions which established certain distinctions based, in particular, on the residence of taxpayers, could be compatible with Community European law provided that they applied to situations which were not objectively comparable[125] or could be justified by overriding reasons in the general interest, in particular in relation to the cohesion of the tax system[126]. In any case, objectives of a purely economic nature cannot constitute an overriding reason in the general interest justifying a restriction of a fundamental freedom guaranteed by the Treaty[127].

(161) Also as regards the period after the entry into force of Article 65(1)(a) TFEU, the Court has inquired into the possible presence of objectively comparable situations, which could justify a legislation restricting the free movement of capital. With reference to certain tax legislations, which had the effect of deterring taxpayers living in a Member State from investing their capital in companies established in another Member State and which also produced a restrictive effect in relation to companies established in other Member States, in that they constituted an obstacle to their raising capital in the Member State concerned, the Court constantly held that such legislations could not be justified by an objective difference in situation of such a kind as to justify a difference in tax treatment, in accordance with Article 65(1)(a) TFEU[128].

(162) In any case, it must be borne in mind that Article 65(3) TFEU states specifically that the national provisions referred to by Article 65(1)(a) are not to constitute a means of arbitrary discrimination or a disguised restriction on the free movement of capital and payments[129].

(163) In the light of the above, and in particular the light of the absence of explicit legal obstacles in some of the Third countries to which the contested scheme applies, the Commission considers that in the present case domestic share acquisitions and share acquisitions of companies established in all other Member States, as

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125 See, in particular, judgment of the Court of Justice of 14.2.1995, case C-279/93, *Schumacker* [1995] ECR I-225

126 See judgment of the Court of Justice of 28.1.1992, case C-204/90, *Bachmann* v *Belgian State* [1992] ECR I-249 and judgment of the Court of Justice of 28.1.1992, case C-300/90, *Commission* v *Belgium* [1992] ECR I-305

127 See judgment of the Court of Justice of 28.4.1998, case C-120/95 *Decker* v *Caisse de Maladie des Employés Privés* [1998] ECR I-1831, paragraph 39, and judgment of the Court of Justice of 28.4.1998, case C-158/96 *Kohll* v *Union des Caisses de Maladie* [1998] ECR I-1931, paragraph 41, judgment of the Court of Justice of 6.6.2000, case C-35/98, *Verkooijen*, cited above, par. 48

128 See judgment of the Court of Justice of 15.7.2004, case C-315/02, *Lenz* [2004] ECR I-7063; judgment of the Court of Justice of 7.9.2004, case C-319/02, *Manninen* [2004] ECR I-7477

129 See judgment of the Court of Justice of 6.6.2000, case C-35/98, *Verkooijen* [2000] ECR I-4071, par. 44.

well and as in some those Third countries where no explicit legal obstacles have been identified are, for the reasons highlighted above, in an objective comparable situation and that there are no overriding reasons of general interest which could justify a different treatment of taxpayers with regard to the place where their capital is invested in the presence of in the contested measure which does not include any distinction between Third countries on the basis of an objective criterion constituting an overriding reasons of general interest which is based on an objectively justified.

E. CONCLUSION ON THE QUALIFICATION OF THE CONTESTED MEASURE

(164) Due to the fact that the scheme applies both within the EU (see Previous decision), as well as to a number of Extra EU situations where no explicit legal obstacles have been identified, the Commission considers that the contested measure in its entirety, also to the extent that it applies to Extra-EU acquisitions, fulfils all conditions laid down in Article 107 (1) TFUE and should thus be qualified as State aid.

(165) In line with the case law of the Court of Justice[130], the Commission would like to reiterate that it is the purpose of this decision is not to set out the conditions which would have avoided classification as State aid of the contested measure. Such a question is rather a matter for dialogue between the Spanish authorities and the Commission, as part of the notification of the scheme at issue, which ought to have taken place before the scheme was put into effect.

F. COMPATIBILITY

(166) As stated in the Opening decision, the Commission considers that the aid scheme in question does not qualify for any of the derogations laid down in Article 107(2) and (3) of the TFEU.

(167) In the course of the procedure, the Spanish authorities and the Thirty Parties presented their arguments to indicate that the derogations provided for in Article 107(3)(c) of the TFEU would apply in the present case[131]. The Two Parties considered that none of the provisions of Article 107(2) or Article 107(3) of the TFEU apply in the present case.

(168) The derogations in Article 107(2) TFEU, concerning 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 apply in this case.

(169) Nor does the derogation provided for in Article 107(3)(a) apply, which authorises aid to promote the economic development of areas where the standard of living is abnormally low or where there is serious underemployment because

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130 See the Judgment of the General Court of 9 September 2009, Joined Cases T-227/01 to T-229/01, T-265/01, T-266/01 and T-270/01, *Diputación Foral de Álava and Others v Commission*, [2006] ECR p. II p.1, points 381 and following.

131 See point (69) and following.

the measure is not conditional on realising any type of activity in specific regions[132].

(170) In the same way, the contested measure adopted in 2001, cannot be regarded as promoting the execution of a project of common European interest or remedying a serious disturbance in the economy of Spain, as provided for in Article 107(3)(b). Nor does it have as its object the promotion of culture and heritage conservation as provided for in Article 107(3)(d).

(171) Finally, the contested measure shall be examined in the light of Article 107(3)(c), which provides for the authorisation of aid to facilitate the development of certain economic activities or of certain economic areas, where such an aid does not adversely affect trading conditions to an extent that is contrary to the common interest. In this respect, it should first be noted that the contested measure does not fall under any of the frameworks or guidelines, which define the conditions to consider certain types of aid compatible with the internal market.

(172) As regards the arguments raised by the Spanish authorities and by the Thirty Parties based on the State Aid Action Plan of 2005[133], where they consider that certain measures can be compatible if they essentially respond to a market failure, the Commission observes that alleged general difficulties in carrying out cross-border mergers cannot be considered as a market failure.

(173) The fact that a specific company may not be capable of undertaking a certain project or transaction without aid does not necessarily mean that there is a market failure. Only where market forces would not in themselves be able to reach an efficient outcome - i.e. where not all potential gains from trade are realised - can a market failure be considered to exist.

(174) The Commission does not dispute that the costs involved in some transactions may well be higher than those involved in other transactions. However, to the extent that these costs are real costs accurately reflecting the nature of the projects being considered - e.g. costs relating to their different geographic location or the different legal environment in which they are to take place - it is efficient for the companies to fully take these costs into account when making their decisions. On the contrary, inefficient outcomes would arise if these real costs were ignored or, indeed, compensated by state aid. The same type of real cost differences also arise when comparing different transactions within the same country as well as when comparing cross border transactions, and the existence of these differences does not mean that inefficient market outcomes would arise.

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[132] See, inter alia, for precedent Commission's practice Commission Decision of 13.5.2003, 2004/76/EC,*aid scheme implemented by France for headquarters and logistic centres*, , OJ L 23, 28.1.2004, p. 1 par 73; see also, for a similar reasoning, Commission decision of 17.2.2003, 2003/515/EC, *State aid implemented by Netherlands for international financing activities*, OJ L 180,18.7.2003, p. 52 par. 105; Commission Decision of 24.6.2003, 2004/77/EC, *aid scheme implemented by Belgium – tax ruling system for US foreign sales corporations*, OJ L 23, 28.1.2004, p. 14, par. 70.

[133] See footnote 31

(175) The examples provided by the Spanish authorities of alleged increased costs for conducting international transactions compared to national transactions are all related to real costs of conducting transitions, which should be fully taken into account by market participants in order for efficient outcomes to arise.

(176) For a market failure to be present there would notably have to be externalities (positive spillovers) being generated by the transactions or significant incomplete or asymmetric information leading to otherwise efficient transactions not being carried out. While these may be, theoretically, present in certain transactions, both international and national (e.g. in the context of joint R&D programmes), they cannot be considered inherently present in all international transactions, let alone in transactions of the type in question. In this respect, the Commission considers that the claim relating to market failures cannot be accepted.

(177) Moreover it should be remembered that when assessing whether an aid can be deemed compatible with the internal market, the Commission balances the positive impact of the measure in reaching an objective of common interest against its potentially negative side effects, such as distortion of trade and competition. The State Aid Action Plan, building on existing practice, has formalized a "balancing test", which operates in three steps. The first two steps address the positive effects of the State aid and the third addresses the negative effects and resulting balancing of the positive and negative effects. The balancing test is structured as follows:

> 1) assessing if the aid is aimed at a well-defined objective of common interest (such as: growth, employment, cohesion, environment, energy security);
>
> 2) assessing if the aid is well designed to deliver the objective of common interest that is to say, if the proposed aid addresses the market failure or other objective. For assessing this, it must be verified if:
>
> a) State aid is an appropriate policy instrument;
>
> b) there is an incentive effect, namely if the aid changes the behavior of undertakings;
>
> c) the measure is proportional, namely if the same change in behavior could be obtained with less aid.
>
> 3) assessing if the distortions of competition and effect on trade are limited, so that the overall balance is positive.

(178) It is first necessary to assess whether the objective pursued by the aid is indeed one that can be regarded as being in the common interest. Notwithstanding the alleged intention to favour the Single market integration, in the present case the objective pursued by the aid is not clearly well defined as it goes beyond market integration, by promoting the expansion of Spanish companies in the European market in particular.

(179) The second step requires assessing whether the aid is properly designed to reach the well-defined objective of common interest. More precisely, state aid must change the behaviour of a beneficiary undertaking in such a way that it engages in

activities that contribute to the achievement of a public-interest objective, that it would not carry out without the aid or which it would carry out in a restricted or different manner. The Spanish authorities and Thirty Parties did not present any specific argument demonstrating the likelihood that such incentive effect criterion would be fulfilled.

(180) The third question addresses the negative effects of State aid. Even if it is well-designed to address an objective of common interest, an aid given to a particular undertaking or economic sector may lead to serious distortions of competition and of trade between Member States. In this respect, the Thirty Parties consider that the aid scheme does not have an impact on the competitive situation of companies subject to corporate tax in Spain, since the financial effect of Article 12(5) would be negligible. However, as already indicated above in paragraphs (126) and following, there are serious indications that, the effect of Article 12(5) is far from negligible. Moreover, since the aid scheme is applicable only to foreign transactions, it clearly has the effect of focusing the distortions of competition on foreign markets.

(181) The last step in the compatibility analysis is to evaluate whether the positive effects of the aid, if any, outweigh its negative effects. As indicated above, in the present case, the Spanish authorities and Thirty parties did not demonstrate the existence of a well defined objective leading to clear positive effects. They consider, in general terms, that Article 12(5) TRLIS fulfils the Community objective of promoting cross-border transactions, without entering into the evaluation of the potential and actual negative effects of the contested measure. In any case, even considering that the positive effect of the measure would be the promotion of cross-border transactions by means of the elimination of obstacles in such transactions, the Commission considers that the positive effects of the measure do not outweigh its negative effects, in particular because the measure's scope is imprecise and indiscriminate.

(182) In conclusion, the Commission considers that, as regards in particular the analysis under article 107(3) c), the tax advantages granted under the contested measure are not related to investment, job creation or specific projects. They simply relieve the undertakings concerned of charges normally borne by those undertakings and must therefore be considered as operating aid. As a general rule, operating aid does not fall within the scope of Article 107 (3) c) since it distorts competition in the sectors in which it is granted and is at the same time incapable, by its very nature, of achieving any of the objectives laid down in that provision[134]. In line with the standard practice of the Commission, such aid cannot not be considered compatible with the internal market, as it does neither facilitate the development of any activities or economic areas nor it is limited in time, digressive or proportionate to what is necessary to remedy to a specific economic handicap of the areas concerned. The result of the "balancing test" confirms this analysis.

[134] See judgement of the General Court of 4.9. 2009, case T-211/05, *Italy v. Commission*, not published yet, par. 173; see also judgement of the General Court of 8.6.1995, case T-459/93, *Siemens v. Commission* [1995] ECR II-1675, par. 48.

(183) In the light of the above, it must be concluded that the entire aid scheme in review, also to the extent that it applies to Extra-EU acquisitions, is incompatible with the internal market.

G. RECOVERY

(184) The contested measure has been implemented without having been notified in advance to the Commission in accordance with Article 108(3) of the Treaty. Therefore, the measure constitutes unlawful aid.

(185) Where unlawfully granted State aid is found to be incompatible with the internal market, the consequence of such a finding is that the aid should be recovered from the recipients pursuant to Article 14 of Council Regulation (EC) n. 659/1999 of 22 March 1999, laying down detailed rules for the application of Article 93 of the EC Treaty[135]. Through recovery of the aid, the competitive position that existed before it was granted is restored as far as is possible. No arguments raised by the Spanish authorities or by the Thirty Parties justified a general departure from this basic principle.

(186) Nevertheless, Article 14(1) of Regulation (EC) n. 659/1999 provides that "*the Commission shall not require recovery of the aid if this would be contrary to a general principle of community law*". The case-law of the Court of Justice and the Commission's own decision-making practice have, amongst others, established that where, as a result of the Commission's actions, legitimate expectations exist on the part of the beneficiary of a measure that the aid has been granted in accordance with European law, then an order to recover the aid would infringe a general principle of European law[136].

(187) In its judgement in *Forum 187*[137], the Court stated that "*the right to rely on the principle of the protection of legitimate expectations extends to any person in a situation where a Community authority has caused him to entertain expectations which are justified. However, a person may not plead infringement of the principle unless he has been given precise assurances by the administration. Similarly, if a prudent and alert economic operator could have foreseen the adoption of a Community measure likely to affect his interests, he cannot plead that principle if the measure is adopted*".

(188) The Spanish authorities and the Thirty parties have essentially invoked the existence of legitimate expectations, based firstly, on certain Commission's replies to written parliamentary questions and, secondly, on the alleged similarity of the

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135 OJ L 83, 27.3.1999, p. 1.

136 See, *inter alia*, Commission Decision 2003/515/EC on the State aid implemented by the Netherlands for international financing activities (OJ 2003 L 180, p. 52); Commission Decision 2004/76/EC on the aid scheme implemented by France for headquarters and logistics centres (OJ 2004 L 23, p. 1); Commission Decision 2004/77/EC no the aid scheme implemented by Belgium – Tax ruling system for United States foreign sales corporations (OJ L 23/2004, p. 14).

137 Judgment of the Court of Justice of 22.6.2006, case C-182/03 and C-217/03, *Forum 187 ASBL* [2006] ECR I-5479, par. 147; see also judgment of the Court of Justice of 26.11.2005, case C-506/03, *Germany v. Commission*, unpublished, par. 58 and judgement of the Court of Justice of 11.3.1987, case C-265/85, *Van den Bergh en Jurgens BV v. Commission* [1987] ECR 1155, paragraph 44.

aid scheme with earlier measures, which have been declared compatible by the Commission. Thirdly, the Spanish authorities and the Thirty parties consider that the principle of legitimate expectations implies that the Commission can neither ask for recovery of the deductions already realised, nor ask for recovery of all outstanding deductions, up to the 20-year period indicated by the TRLIS.

(189) As regards the alleged similarity of the aid scheme with other measures, which have been considered not to constitute state aid, the Commission considers that the aid scheme is substantially different from the measures which have been assessed by the Commission in its decision of 1984 concerning the "Belgian coordination centres"[138]. The contested measure has a different field of application in that it does not concern intra-group activities, as in the case of the "Belgian coordination centres". Moreover, the contested measure has a different structure, which renders it selective, most notably because it only applies to transactions linked to foreign countries.

(190) As regards the impact of the Commission's declarations on legitimate expectations of the beneficiaries, the Commission considers that a distinction should be drawn between two periods: a) the period starting from the entry into force of the measure on 1.1.2002 until the date of publication of the Opening decision in the Official Journal on 21.12.2007; b) the period following the publication of the Opening decision in the Official Journal.

(191) With reference to the first period, the Commission acknowledges its answers to the parliamentary questions of Mr. Erik Mejier and Mrs. Sharon Bowles, regarding the possible nature of State aid of the contested measure. More precisely, in reply to the parliamentary question of the MEP Mr. Erik Meijer, on 19th January 2006 a Commissioner answered on behalf of the Commission as follows: "*The Commission cannot confirm whether the high bids by Spanish companies are due to Spain's tax legislation enabling undertakings to write off goodwill more quickly than their French or Italian counterparts. The Commission can confirm, however, that such national legislations do not fall within the scope of application of state aid rules, because they rather constitute general depreciation rules applicable to all undertakings in Spain*"[139]. On 17th February 2006, in reply to the parliamentary question of the MEP Mrs. Sharon Bowles, a Commissioner answered, on behalf of the Commission, as follows: "*According to the information currently in its possession, it would however appear to the Commission that the Spanish(tax) rules related to the write off of 'goodwill' are applicable to all undertakings in Spain independently from their sizes, sectors, legal forms or if they are privately or publicly owned because they constitute general depreciation rules. Therefore, they do not appear to fall within the scope of application of the state aid rules*"[140].

(192) By these declarations made to the European Parliament, the Commission has provided specific, unconditional and concordant assurances of such a nature as to give raise to justified hopes on the part of the beneficiaries under the contested

[138] Commission Decision SG(84) D/6421 of 16.5.1984
[139] Written Question E-4431/05
[140] Written Question E-4772/05

measure at issue that the goodwill amortization scheme was lawful, in the sense that it did not fall within the scope of the State aid rules,[141] and that any advantages derived from it could not, therefore, be subject to subsequent recovery proceedings. Although these declarations did not amount to a formal Commission decision establishing that the amortization scheme did not constitute State aid, their effect was equivalent from the point of view of the creation of a legitimate expectation, especially in view of the fact that the applicable procedures ensuring the respect of the collegiality principle had been respected in the present case. As the notion of state aid is an objective one[142] and the Commission does not have any discretionary power as regards its interpretation – contrary to a compatibility analysis - any precise and unconditional statement on behalf of the Commission to the effect that a national measure is not to be qualified as state aid will naturally be understood as confirming that the measure was "non-aid" from the outset (i.e. also before the statement in question). Any undertaking which had previously been uncertain as to whether or not it would in future be liable to recovery under the State aid rules of advantages it had obtained under the goodwill amortization scheme arising from transactions entered into before the Commission declarations could have concluded thereafter that such uncertainty was groundless, as it could not be expected to demonstrate greater diligence than the Commission in this respect. In these specific circumstances, and bearing in mind that Community law does not require the demonstration of a causal link between the assurances given by a Community institution and the behaviour by citizens or undertakings to which such assurances relate,[143] any diligent businessperson could reasonably expect the Commission not to subsequently impose any recovery[144] as regards measures which it had itself previously qualified, in a declaration to another Community institution, as not constituting aid, irrespective of when the transaction benefiting from the aid measure was entered into.

(193) Accordingly, the Commission concludes that some beneficiaries of the contested measure could have had a legitimate expectation that the aid would not be recovered and hence is not requiring recovery for fiscal aid granted to those beneficiaries in the context of any shareholdings held by a Spanish acquiring company, directly or indirectly in a foreign company before the date of the publication[145] in the Official Journal of the European Union of the Commission's decision to initiate the formal investigation procedure under Article 108(2) of the Treaty that could have then benefited from the contested measure.

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141 See, on the principle of legitimate expectation, the judgements of the Court of Justice, *Van den Bergh en Jurgens v. Commission*, cit., par. 44; judgment of the Court of Justice, cases 182/03 and C-217/03, *Forum 187 ASBL v. Commission* [2006] ECR I-5479, paragraph 147; judgement of the General Court ,Case T-290/97, *Mehibas Dordtselaan v. Commission* [2000] ECR II15, paragraph 59.

142 Judgment of the Court of 22 December 2008, British Aggregates/Commission, C-487/06 P, points 111-114 and 185-186; Judgement of the General Court of 17.10.2002, case T-98/00, Linde v. Commission, par. 33.

143 That is, it is not necessary to demonstrate that the citizen or undertaking engaged in subsequent actions which it might not otherwise have done, in reliance on the assurance in question.

144 See, by analogy Commission decision of 17 February 2003 on the Belgian Coordination centres (2003/757/EC) and Decision of the Commission of 20 December 2006, GIE Fiscaux (C46/2004).

145 OJ C 311, 21.12.2007, p. 21.

(194) Beyond these considerations which are identical to those made in the Previous decision, the Commission considers that a series of additional elements should be taken into consideration.

(195) Indeed, according to paragraph 117 of the Previous decision although the Commission considered that the Spanish authorities and the Thirty Parties had provided insufficient elements justifying a differentiated tax treatment of Spanish shareholding transactions and transactions between companies established within the European Union, the Commission declared that it could not *"completely exclude a priori such a differentiation as regards transactions concerning third countries. Indeed, outside the EU, legal barriers to cross border business combinations may persist, which would place cross border transactions in a different legal and factual situation from transactions within the EU. As a result, extra-EU acquisitions which should have led to the possibility of goodwill amortization - this is the case for transactions including a majority shareholding - may be prevented from this fiscal opportunity out of their inability to make a business combination. Amortization of financial goodwill for these transactions, which are in a different legal and factual situation from intra-EU transactions, may be deemed necessary to ensure tax neutrality."* The Commission concluded its analysis by stating in point 119 of the Previous decision, available on the Commission's website as from the first days of January 2010, that *"In this context, the Commission maintains the procedure, as initiated by the Opening decision of 10 October 2007, open for Extra-EU acquisitions in light of new elements which the Spanish authorities have committed to provide as regards the obstacles to cross border mergers outside the EU. The procedure as opened on 10 October 2007 is therefore still ongoing for Extra-EU acquisitions".*

(196) In paragraphs 115 to 119 of that Previous decision, the Commission thus indicated that a differentiation between acquisition transactions which took place within the EU as opposed to transactions taking place outside the EU could exist. In particular, the Commission observed that *"barriers to cross border business combinations may persist, which would place cross border transactions in a different legal and factual situation from transactions within the EU".* The references to the criteria of "legal barriers" and of "majority shareholdings" are, in those specific circumstances, particularly relevant.

(197) In the light of these specific and peculiar elements of the present case, the Commission considers that the declaration contained in point 117 of the Previous decision could have given rise to legitimate expectations as regards the application of the contested aid scheme to transactions of Spanish companies in those Third countries where there exist explicit "legal barriers" to cross border business combinations and where a "majority shareholding" has been acquired by the Spanish company concerned, irrespective of the date at which the transaction took place before the adoption of the present decision.

(198) On the basis of the information submitted by the Spanish authorities in the Reports and without prejudice to the State aid qualification of the contested scheme and its application to individual transactions for the reasons outlined in

point(107), the Commission observes that, among the countries analyzed, the legislation in force in two of them, i.e. in India and China, presents explicit legal obstacles to cross border business combinations.

(199) In the light of the findings presented in points (119) and (120),, the Commission concludes that the beneficiaries of the contested measure for transactions relating to those two countries and which had acquired a majority shareholding could have a legitimate expectation that the aid would not be recovered.

(200) The same treatment will apply to those beneficiaries having realised a transaction in other Third countries, which could provide sufficient elements to demonstrate that an explicit legal barrier, in the meaning of the present decision, which had acquired a majority shareholding, exists in a legislation of that Third country . For the countries mentioned in the Reports, the Commission will take into account that, on the basis of the information provided by the Spanish authorities, it was not possible to identify such barriers, but is ready to examine further relevant evidence.

(201) For the beneficiary enjoying legitimate expectations either on the basis of the Commission declarations to MEPs or on the basis of the Previous decision, the Commission also considers that all those beneficiaries should continue to enjoy the benefits of the contested measure until the end of the amortisation period that it provides. The Commission acknowledges that the operations were planned and investments were made in the reasonable and legitimate expectation of a certain degree of continuity in the economic conditions, including the contested measure. Therefore, in line with the precedent case-law of the Court of Justice and the Commission's practice[146], in the absence of an overriding public interest[147], the Commission considers that the beneficiaries should be allowed to continue enjoying the benefits of the contested measure, over the entire amortisation period provided by Article 12(5)TRLIS.

(202) Moreover, the Commission considers that a reasonable transition period should be foreseen in order to allow companies enjoying legitimate expectations who had already acquired, in a longer term perspective, rights on foreign companies, without already holding those rights for an uninterrupted period of at least one year on the date of the publication of the Opening decision (legitimate expectations arising from Commission declarations to MEPs) or on the date of Publication of the present decision (legitimate expectations arising from the Previous decision). The Commission therefore considers that companies which fulfilled all other relevant conditions of Article 12(5) TRLIS by 21 December 2007, or respectively by the date of publication of the present decision in the Official Journal, apart from the condition that they hold their shareholdings for an uninterrupted period of at least one year, should be considered also to benefit

[146] See Commission Decision of 17 February 2003 on the aid scheme implemented by Belgium for coordination centres established in Belgium (OJ L 282, 30.10.2003, p. 25), and judgment of the Court of Justice of 22.6.2006, Case C- 182/03 and C-217/03, *Forum 187 ASBL* [2006] ECR, paragraph 162 and 163

[147] See the judgement in Forum 187, cited above in footnote 131, paragraph 149; see also the judgement of the Court of Justice of 14.5.1975, case 74/74, *CNTA v. Commission* [1975], ECR 533, paragraph 44.

from legitimate expectations, if they held those rights for an uninterrupted period of at least one year at the latest on 21 December 2008, or respectively one year after the publication of the present decision.

(203) By contrast, for cases where a Spanish acquiring company will not be enjoying legitimate expectation, any incompatible aid will be recovered from its recipient except when, firstly, an irrevocable obligation has been entered into, before 21 December 2007 (legitimate expectations arising from Commission declarations to MEPs) or before the date of Publication of the present decision (legitimate expectations arising from the Previous decision), by a Spanish acquiring company, to hold such rights and, secondly, the contract contains a suspensive condition linked to the fact that the operation at stake is subject to the mandatory approval of a regulatory authority and, thirdly, the operation has been notified before 21 December 2007 (legitimate expectations arising from Commission declarations to MEPs) or before the publication of the present decision (legitimate expectations arising from the Previous decision).

(204) The Commission also considers that the contested measure does not constitute aid if, at the time beneficiaries enjoyed its benefits, all the conditions laid down by a regulation adopted pursuant to Article 2 of Regulation (EC) No 994/98[148] which is applicable at the time the tax reduction is enjoyed are fulfilled.

(205) In the light of all the above considerations and as already highlighted in the Previous decision, on a given year, for a given beneficiary, the precise amount of the aid corresponds to the net discounted value of the tax burden reduction provided by the amortization provided by Article 12(5) TRLIS. It is therefore contingent on the company tax rate in the years concerned and on the discount interest rate applicable.

(206) For a given year and a given beneficiary, the nominal value of the aid corresponds to the tax reduction provided by the application of Article 12(5) TRLIS for rights on foreign companies that do not fulfil the conditions described in the points above.

(207) The discounted value is calculated by applying the interest rate to the nominal value, in accordance with Chapter V of Regulation (EC) No 794/2004 and to Regulation (EC) No 271/2008 amending Regulation (EC) No 794/2004.

(208) When calculating the tax burden of beneficiaries in the absence of the unlawful aid measure, the Spanish authorities must base themselves on the transactions, which were carried out in the period predating the publication of the Opening Decision in the Official Journal (legitimate expectations arising from Commission declarations to MEPs) or predating the date of Publication of the present decision (legitimate expectations arising from the Previous decision), as indicated above. It is not possible to argue that, had these illegal advantages not existed, the beneficiaries would have structured their transactions differently in order to

[148] This Regulation empowers, i.a, the Commission to adopt a Regulation setting out under which conditions aid measures are deemed not to meet all the criteria of Article 107(1) TFEU (de minimis aid).

reduce their tax burden. As clearly stated by the Court in the *Unicredito* judgement[149], in fact, such hypothetical considerations cannot be taken into account for the purposes of aid calculation.

VII. CONCLUSION

(209) The Commission considers that, in the light of the above-mentioned case law and of the specificities of the case, Article 12(5) TRLIS constitutes an aid scheme within the meaning of Article 107(1) TFEU, also to the extent that it applies to Extra-EU acquisitions. The Commission also finds that the contested measure having been implemented in breach of Article 108(3) TFEU constitutes an unlawful aid scheme to the extent that it applies to Intra-EU acquisitions.

(210) Nonetheless, given the presence of legitimate expectations until the publication date of the Opening decision, the Commission exceptionally waives recovery and accepts that the implementation can continue over the entire amortisation period provided by the aid scheme for any tax benefits deriving from the application of the aid scheme to shareholdings held by a Spanish acquiring company, directly or indirectly in a foreign company before the date of the publication in the Official Journal of the European Union of the Commission's decision to initiate the formal investigation procedure under Article 108(2), except when, firstly, an irrevocable obligation has been entered into, before 21 December 2007, by a Spanish acquiring company, to hold such rights and, secondly, the contract contains a suspensive condition linked to the fact that the operation at stake is subject to the mandatory approval of a regulatory authority the decision and, thirdly, the operation has been notified before 21 December 2007. Moreover, the Commission waives recovery and accepts that the implementation can continue over the entire amortisation period provided by the aid scheme also for any tax benefits deriving from the application of the aid scheme to majority shareholding transactions realised before the publication of the present decision which relate to those Third countries where the presence of explicit legal obstacles to cross border combinations will be duly justified in line with the principles laid down in the present decision.

HAS ADOPTED THIS DECISION:

Article 1

1. The aid scheme which has been implemented by the Kingdom of Spain in application of Article 12(5) of the Real Legislative Decree 4/2004 of 5 March 2004, consolidating the amendments made to the Spanish Company Tax Act, unlawfully put into effect by the Kingdom of Spain in breach of Article 108(3) of the TFUE is incompatible with the internal market as regards aid granted to beneficiaries, when realising Extra-EU acquisitions.

[149] Judgement of the Court of Justice of 15.12.2005 case C-148/04, *Unicredito Italiano Spa v. Agenzia delle Entrate* [ECR] 2005, I-11137, par. 117-119.

2. Nonetheless, tax reductions enjoyed by beneficiaries, when realising Extra-EU acquisitions, owing to Article 12(5) TRLIS which are related to rights held directly or indirectly in foreign companies fulfilling the relevant conditions of the aid scheme by 21 December 2007, apart from the condition that they hold their shareholdings for an uninterrupted period of at least one year, can continue to be implemented over the entire amortisation period provided by the aid scheme.

3. Tax reductions enjoyed by beneficiaries, when realising Extra-EU acquisitions, owing to Article 12(5) TRLIS which are related to an irrevocable obligation entered into, before 21 December 2007, to hold such rights when the contract contains a suspensive condition linked to the fact that the operation at stake is subject to the mandatory approval of a regulatory authority and the operation has been notified before 21 December 2007, can continue to be implemented over the entire amortisation period provided by the aid scheme for the part of the rights held as of the date of the lifting of the suspensive condition.

4. Furthermore, tax reductions enjoyed by beneficiaries owing to Article 12(5) TRLIS, when realising Extra-EU acquisitions by the date of publication of the present decision in the Official Journal of the European Union, which are related to majority shareholdings held directly or indirectly in foreign companies established in China, India and other countries where the existence of explicit legal obstacles to cross border business combinations have been or can be demonstrated can continue to be implemented over the entire amortisation period provided by the aid scheme.

5. Tax reductions enjoyed by beneficiaries, when realising Extra-EU acquisitions, owing to Article 12(5) TRLIS which are related to an irrevocable obligation entered into, before the publication in the Official Journal of the present decision, to hold such rights in foreign companies established in China, India and other countries where explicit legal obstacles to cross border business combinations have been or can be demonstrated, when the contract contains a suspensive condition linked to the fact that the operation at stake is subject to the mandatory approval of a regulatory authority and the operation has been notified before the publication of the present decision in the Official Journal, can continue to be implemented over the entire amortisation period provided by the aid scheme for the part of the rights held as of the date of the lifting of the suspensive condition.

Article 2

Tax reduction enjoyed owing to the scheme referred to in Article 1 does not constitute aid if, at the time it is granted, it fulfils the conditions laid down by a regulation adopted pursuant to Article 2 of Regulation (EC) No 994/98 which is applicable at the time the aid is granted.

Article 3

Tax reduction enjoyed owing to the scheme referred to in Article 1 which, at the time it is granted, fulfils the conditions laid down by a Regulation adopted pursuant to Article 1 of Regulation (EC) No 994/98 or by any other approved aid scheme is compatible with the internal market, up to maximum aid intensities applicable to that type of aid.

Article 4

1. The Kingdom of Spain shall recover the incompatible aid corresponding to tax reduction provided under the scheme referred to in Article 1(1) from the beneficiaries whose rights on foreign companies, acquired in the context of Extra-EU acquisition, does not fulfil the conditions described in Article 1(2) to 1(5).
2. The sums to be recovered shall bear interest from the date on which the tax base of the beneficiaries was reduced until their actual recovery.
3. The interest shall be calculated on a compound basis in accordance with Chapter V of Regulation (EC) No 794/2004.
4. The Kingdom of Spain shall cancel all outstanding tax reduction provided under the scheme referred to in Article 1(1) with effect from the date of adoption of this decision, except for the one attached to rights on foreign companies fulfilling the conditions described in Article 1(2).

Article 5

1. Recovery of the aid granted under the scheme referred to in Article 1 shall be immediate and effective.
2. The Kingdom of Spain shall ensure that this Decision is implemented within four months following the date of notification of this Decision.

Article 6

1. Within two months following notification of this Decision, The Kingdom of Spain shall submit the following information:

    (a) the list of beneficiaries that have received aid under the scheme referred to in Article 1 and the total amount of aid received by each of them under the scheme ;

    (b) the total amount (principal and recovery interests) to be recovered from each beneficiary ;

    (c) a detailed description of the measures already taken and planned to comply with this Decision;

    (d) documents demonstrating that the beneficiaries have been ordered to repay the aid.

2. The Kingdom of Spain shall keep the Commission informed of the progress of the national measures taken to implement this Decision until recovery of the aid granted under the scheme referred to in Article 1 has been completed. It shall immediately submit, on simple request by the Commission, information on the measures already taken and planned to comply with this Decision. It shall also provide detailed information concerning the amounts of aid and recovery interest already recovered from the beneficiaries

Article 7

This Decision is addressed to the Kingdom of Spain.

Done at Brussels,

For the Commission

Joaquín ALMUNIA
Vice President of the Commission

Notice

If the decision contains confidential information which should not be published, please inform the Commission within fifteen working days of the date of receipt. If the Commission does not receive a reasoned request by that deadline, you will be deemed to agree to publication of the full text of the decision. Your request specifying the relevant information should be sent by registered letter or fax to:

European Commission
Directorate-General for Competition
State Aid Greffe
Rue de la Loi/Wetstraat, 200
B-1049 Brussels
Fax No: +32.2.296 12 42

Annex 1: List of the interested third parties having presented comments to the Opening decision that have not requested to be treated anonymously

Abertis Infraestructuras SA
Acerinox SA
Aeropuerto de Belfast SA.
Altadis SA, Fomento de Construcciones y Contratas SA
Amey UK Ltd
Applus Servicios Tecnológicos SL
Asociación Española de Banca (AEB)
Asociación Española de la Industria Eléctrica (UNESA)
Asociación de Empresas Constructoras de Ámbito Nacional (SEOPAN)
Asociación de Marcas Renombradas Españolas
Asociación Española de Asesores Fiscales
Amadeus IT Group SA
Banco Bilbao Vizcaya Argentaria (BBVA)
Banco Santander
Club de Exportadores e Inversores Españoles
Compañía de distribución integral Logista SA
Confederacion Española de Organizaciones Empresariales
Confederacion Española de la Pequeña y Mediana Empresa (CEPYME)
Ebro Puleva SA
Ferrovial Servicios SA
Hewlett-Packard Española SL
La Caixa, Iberdrola
Norvarem SA
Prosegur Compañía de Seguridad SA
Sociedad General de Aguas de Barcelona SA (Grupo AGBAR)
Telefónica SA

Annex 2: Summary of the KPMG report presented by the Spanish authorities

Summary Chart

Country	Corporate Law governing mergers	Are cross-border mergers prohibited by Corporate law and subsequent regulations? (Yes/No/Not specifically addressed)	Case Law or Doctrine refers to the impossibility of a cross-border merger? (Yes/No/Not found)	Have relevant factual obstacles been identified that would impede a cross-border merger? (Yes/No)	Have tax rules been identified which would impose additional tax costs on a cross-border merger? (Yes/No/uncertain tax treatment)	Are there precedents of cross-border mergers in your jurisdiction? (Yes/No/Not found)	Summary
Argentina	Law N°19550 Articles 82-87 and 118	Not specifically addressed by either Corporate Law or main Commercial Registries regulations	Yes Relevant doctrine points out that cross-border mergers are not feasible in Argentina	Yes Registration issues with relevant Commercial Registry	Yes. Taxation for the absorbed company and its shareholders, since it is considered that the protocol of the Treaty signed by Argentina and Spain should not apply. Moreover, relevant doctrine and Argentinean tax administration points out that roll over regime can only apply to domestic mergers	No	Doctrinal authors point out that a cross-border merger is not feasible. Taxation of the absorbed company and its shareholders
Australia	Corporations Act 2001 (main sections are 606, 413 and 611)	The concept of cross-border mergers is unknown under Australian Corporate Act Corporations Act 2001 only allows for three specific procedures with regard to takeovers, none of which contemplates a cross-border merger	Not found	Yes A cross-border merger cannot feasibly be implemented in Australia	Uncertain tax treatment. A roll over regime only applies to domestic corporate transactions	Not found	A cross-border merger is not specifically addressed as a permitted transaction for Corporation Act 2001 purposes, and therefore cannot be feasibly implemented.

Country	Corporate Law governing mergers	Are cross-border mergers prohibited by Corporate law and subsequent regulations? (Yes/No/Not specifically addressed)	Case Law or Doctrine refers to the impossibility of a cross-border merger? (Yes/No/Not found)	Have relevant factual obstacles been identified that would impede a cross-border merger? (Yes/No)	Have tax rules been identified which would impose additional tax costs on a cross-border merger? (Yes/No/uncertain tax treatment)	Are there precedents of cross-border mergers in your jurisdiction? (Yes/No/Not found)	Summary
Brazil	Brazilian Civil Code (Law Nº 10.406/02) and the Law Nº 6.404/1976	Not specifically addressed	Not found	State Board Approval The register within the SISBACEN, whose approval would be uncertain Restriction in certain economic activities sectors would not allow a cross-border merger	Uncertain tax treatment Brazilian and non-Brazilian (i.e. shareholders of the Brazilian company)taxpayers involved in amerger transaction at market value will be subject to adverse tax consequences.	No. Only one transaction has been found but refers to a reverse merger in which some foreign companies were absorbed by a Brazilian entity	There are relevant obstacles which in practice impede the execution of a cross-border merger.
Canada	Canadian Business Corporation Act and applicable Corporate Laws in Canadian provinces	Yes Both merging entities need to apply Canadian legislation Only certain types of mergers (e.g. amalgamations) are theoretically permitted in British Columbia, but there is no precedent	Not found	Yes	Yes/Uncertain tax treatment In case of dissolution of a 100% subsidiary, taxation for the dissolved company and its shareholder would arise	Not found	In general cross-border merger is not possible (only in British Columbia under certain circumstances) except in dissolution of a 100% Canadian subsidiary Taxation of the dissolved company and its shareholders

Country	Corporate Law governing mergers	Are cross-border mergers prohibited by Corporate law and subsequent regulations? (Yes/No/Not specifically addressed)	Case Law or Doctrine refers to the impossibility of a cross-border merger? (Yes/No/Not found)	Have relevant factual obstacles been identified that would impede a cross-border merger? (Yes/No)	Have tax rules been identified which would impose additional tax costs on a cross-border merger? (Yes/No/uncertain tax treatment)	Are there precedents of cross-border mergers in your jurisdiction? (Yes/No/Not found)	Summary
Chile	Law N° 18.046 Article 99	Not specifically addressed	Not found	Yes Need to obtain a certificate of termination of business activity executed by the Internal Revenue Services, which can significantly delay the merger process. Other obstacles exist in relation to the rules of the Central Bank of Chile, which would require a special request in order to carry out such merger, foreign investment rules provided by Decree law No. 600 and the fact that in certain economic sectors a cross-border merger would not be feasible	Uncertain tax treatment There is no certainty that domestic roll-over regime can be applied in a cross-border merger to both the shareholders and the absorbed entity. A cross-border merger should not generate tax effects other than the taxation due on retained profits to the date of the merger by the company being acquired. The liquidation of a Chilean entity into its direct subsidiary is not considered similar to a merger for Chilean tax purposes. Thus, the shareholders will be subject to Chilean corporate tax to the extent that the assets transferred are stepped up.	Yes Just one, but the only precedent involved a holding entity with no Chilean activities or assets	There are relevant obstacles which may impede the execution of a cross-border merger Uncertain tax treatment for shareholders and absorbed entity

Country	Corporate Law governing mergers	Are cross-border mergers prohibited by Corporate law and subsequent regulations? (Yes/No/Not specifically addressed)	Case Law or Doctrine refers to the impossibility of a cross-border merger? (Yes/No/Not found)	Have relevant factual obstacles been identified that would impede a cross-border merger? (Yes/No)	Have tax rules been identified which would impose additional tax costs on a cross-border merger? (Yes/No/uncertain tax treatment)	Are there precedents of cross-border mergers in your jurisdiction? (Yes/No/Not found)	Summary
China	(a) PRC Company Law of 2005 for mergers involving only limited liability companies or joint stock limited companies established in China Mainland, and (b) Merger and Division of Foreign Investment Enterprises Provisions (issued in 2001) which govern mergers involving Foreign Investment in China Mainland Provisions on mergers of a foreign company issued in 2009	Existing rules only refer to domestic mergers On 22 June 2009, the Ministry of Commerce enacted a new set of provisions on mergers and acquisitions of a domestic company by foreign investors A cross-border merger as referred to in this document is not possible	Not found	Yes A cross-border merger is not allowed	Uncertain tax treatment Notice 59 (which governs the tax corporate reorganization rules) does not apply to cross-border mergers, and hence tax neutrality will not apply, even though a cross-border merger is not allowed in China	Not found	New Corporate Law legislation was enacted in 2009 as regards provisions on mergers by foreign investors. Yet, cross-border mergers (as referred to in this document) are not allowed
Colombia	Articles 172 and following of the Colombian Commercial Code	Not specifically addressed. Yet, cross-border mergers are accepted in practice as guidelines are provided by the Office of the Superintendent of Companies. A Colombian branch would need to develop the economic activity of the foreign entity in a relevant number of economic activities which impedes in practice the completion of a cross-border merger	No	Yes Foreign investment rules and mainly the impossibility of a Colombian branch to develop certain economic activities	Yes Taxation of shareholders	Yes, but not with Spanish companies	There are relevant obstacles which may delay or impede the execution of a cross-border merger Taxation of shareholders

Country	Corporate Law governing mergers	Are cross-border mergers prohibited by Corporate law and subsequent regulations? (Yes/No/Not specifically addressed)	Case Law or Doctrine refers to the impossibility of a cross-border merger? (Yes/No/Not found)	Have relevant factual obstacles been identified that would impede a cross-border merger? (Yes/No)	Have tax rules been identified which would impose additional tax costs on a cross-border merger? (Yes/No/uncertain tax treatment)	Are there precedents of cross-border mergers in your jurisdiction? (Yes/No/Not found)	Summary
Ecuador	Ecuadorian Company Law (i.e. R.O. 312 de 5 de noviembre de 1999; and "Ley Reformatoria a la Ley de Compañías" R.O. 519 de 15 de mayo de 2009 Articles 337 to 344	Not specifically addressed A cross-border merger cannot feasibly be implemented in Ecuador due to the fact that the liquidation of the Ecuadorian entity would be required.	Not found	Yes A cross-border merger cannot feasibly be implemented in Ecuador	Uncertain tax treatment A rollover regime exists only for domestic corporate restructurings	No	Cross-border mergers are not feasible in Ecuador
India	Sections 391 to 394 of Indian Company's Act of 1965	Upstream mergers aare prohibited as per Section 394 (4) (b) of Corporation Act	Not found	Yes An upstream merger is not feasible	Yes As regards upstream mergers, tax costs would exist for the absorbed company and its shareholders even though cross-border mergers are not allowed in India	No There are only precedents of reverse mergers (no precedents of upstream mergers)	Upstream mergers are not permitted
Japan	Companies Act n°86 of 26 July 2005	Not specifically addressed Yet, as per criterion of officers of Ministry of Justice when Company Law was introduced in 2006, cross-border mergers should not be allowed	Yes Relevant doctrine and officials of Ministry of Justice point out that cross-border mergers are not feasible in Japan	The Legal Affairs Bureau in Japan does not allow registering a cross-border merger	In theory, as Companies Act does not contemplate a cross-border merger, tax treatment would be uncertain	No	Legal Affairs Bureau in Japan does not allow registering a cross-border merger

Country	Corporate Law governing mergers	Are cross-border mergers prohibited by Corporate law and subsequent regulations? (Yes/No/Not specifically addressed)	Case Law or Doctrine refers to the impossibility of a cross-border merger? (Yes/No/Not found)	Have relevant factual obstacles been identified that would impede a cross-border merger? (Yes/No)	Have tax rules been identified which would impose additional tax costs on a cross-border merger? (Yes/No/uncertain tax treatment)	Are there precedents of cross-border mergers in your jurisdiction? (Yes/No/Not found)	Summary
Mexico	General Law of Mercantile Companies ("Ley General de Sociedades Mercantiles")	Not specifically addressed	Not found	Yes Restrictions in certain economic activities sectors would not allow a cross-border merger	Yes As regards upstream mergers tax costs exist for the absorbed company and its shareholders	Yes, but not with Spanish companies	Taxation of the absorbed company and its shareholders
Morocco	Law 17-95 relating *Societes Anonymes*. Articles 222 to 234. (Yet, all principles are also applicable to *Sociétés á Responsabilité Limiteé)*	Not specifically addressed	Not found in Morocco	Yes Foreign exchange regulations may impede the merger of a Moroccan entity into a Spanish entity	Uncertain tax treatment Tax neutrality rules only apply to mergers between national entities	Not found	No specific provisions exist and legal, tax and relevant factual obstacles would impede a cross-border merger
Peru	Law 268.87, General Corporate Act (GCA)	Not specifically addressed A cross-border merger cannot feasibly be implemented in Peru due to the fact that the liquidation of the Peruvian entity would be required	Yes	Yes A cross-border merger cannot be feasibly be implemented in Peru	Uncertain tax treatment A roll-over regime exists only for domestic corporate restructuring	Not found	Cross-border mergers are not feasible in Peru

Country	Corporate Law governing mergers	Are cross-border mergers prohibited by Corporate law and subsequent regulations? (Yes/No/Not specifically addressed)	Case Law or Doctrine refers to the impossibility of a cross-border merger? (Yes/No/Not found)	Have relevant factual obstacles been identified that would impede a cross-border merger? (Yes/No)	Have tax rules been identified which would impose additional tax costs on a cross-border merger? (Yes/No/uncertain tax treatment)	Are there precedents of cross-border mergers in your jurisdiction? (Yes/No/Not found)	Summary
United States	Applicable Corporate Laws in US States	US Laws do not prohibit or differentially treat mergers of other business combinations with foreign entities Yet, some States (e.g. Delaware) do not permit such mergers when the laws of the other jurisdiction do not permit a cross-border merger	No	Yes Strict limitations in certain sectors as per certain national security laws Strict rules for obtaining the approval of the cross-border merger process	No Yet, failure to comply with requirements of tax-free regimes would trigger adverse tax consequences In practice, shareholders of US companies often oppose cross-border mergers because of the tax burdens that could result for them	Not found, but it is likely that this event happened in Delaware	A cross-border merger would only be possible in certain States subject to the completion of a number of requirements
Venezuela	Commercial Code dated 26 July 1955 and Article 340 of Code of Commerce of Venezuela	Not specifically addressed A cross-border merger cannot feasibly be implemented in Venezuela due to the fact that the liquidation of the Venezuelan entity would be required	No	Yes A cross-border merger cannot feasibly be implemented in Venezuela	Uncertain tax treatment A rollover regime exists only for domestic corporate restructurings	Not found	Cross-border mergers are not feasible in Venezuela

Annex 3: Summary of the Garrigues report presented by the Spanish authorities

Legal and regulatory aspects

In the following countries a cross-border merger is not possible from the viewpoint of commercial law:

- **India,** under a combination of Articles 3, and 391 to 394 of the relevant Indian legislations ("1965 Companies Act").
- **Australia,** because neither the *"Corporation Act 2001"* nor the *"Foreign Acquisitions and Takeovers Act 1975"* recognizes a cross-border merger which, therefore, is not feasible under Australian laws.
- **Japan,** since, as confirmed by the *"Tokyo Legal Affairs Bureau"* (a department of the Japanese Justice Ministry, which keeps the register of mergers effected in Japan), the interpretation of Articles 2 and 748 of the "Companies Act" excludes the possibility of completing a cross-border merger.
- **Canada,** as Canadian law does not recognize cross-border mergers and the only similar operation recognized is the so-called "amalgamation", which requires, for the execution of the amalgamation, both companies to be governed by the same Canadian legislation (Sections 2 and 181 of the Federal Canada Business Corporations Act) and therefore, it is not possible to perform a cross-border merger as defined.
- **Ecuador,** in accordance with Articles 342 and 415 of the "Ecuador Companies Law", published in Official Register No. 312 on 5 November 1999, whereby the acquiring company, in order to complete a merger, must have its domicile in Ecuador or, otherwise, must previously form a new company in Ecuador, precluding a cross-border merger such as the one proposed. This approach has also been confirmed by the administrative body that controls and oversees Ecuadorian companies (*"Superintendence of Corporations"*), which is responsible for approving company mergers and other operations in Ecuador.
- **China,** as reflected in regulations governing the acquisition of local companies by non-residents (specifically, Articles 2 and 55 of the regulations "Provisions on Acquisitions of Domestic Enterprises by Foreign Investors", issued by the Chinese Ministry of Commerce on June 22, 2009.

There are other countries in which cross-border mergers are not specifically regulated but there are legal obstacles that complicate them to the point that, in the opinion of the law firms consulted and/or relevant administrative or academic doctrine, such mergers are practically impossible, particularly the countries listed below:

- **Argentina,** where the number of legal and practical obstacles (described in detail in the attached report on Argentina) precludes the execution of cross-border mergers. This same conclusion is drawn by most Argentinean doctrine, cited in the report, and by the Argentinean Justice Administration which, through the *"Pre-Classification Department of the Superintendence of Corporations"* (body that controls legal entities in the Autonomous City of Buenos Aires), describes such mergers as *"laboratory cases"* for which there are no precedents.

- **Brazil,** where, in the opinion of the law firm consulted, cross-border mergers are almost impossible due both to the incompatibility of foreign an Brazilian laws for the purposes of registering the merger in Brazil and to the need to open a branch into which the Brazilian company would be merged, which requires a large number of authorizations from political and economic bodies that are almost impossible to obtain (particularly the specific *"Presidential Decree"* mentioned in the Brazilian report).
- **Peru,** because, according to the information provided by the local law firm, Peruvian public Registers have rejected in the past the described cross-border mergers registering requests due to the fact that they are reorganization operation which are not under the scope of applicable law (the so-called *"Ley n° 26887 General de Sociedades"*).
- **Colombia,** a jurisdiction in which (i) the absence of a specific procedure for cross-border mergers, (ii) the need to open a branch in Colombia, following specific authorization procedures, together with (iii) legal and regulatory restrictions on certain activities in many business sectors, make it impossible to complete a cross-border merger in such sectors, in the opinion of the law firm whose report is attached.

Additionally, as explained in the report on Colombia, in some of the countries analyzed the <u>regulatory restrictions on foreign investments in certain business sectors</u> prevent the completion of cross-border mergers since, if such mergers were effected, the activities would be performed in each country directly by a non-resident, which would generate incompatibilities that would be totally prohibited or seriously restricted in those countries. Of the countries analyzed, this is the case of the Latin American countries, particularly **Colombia**, which prohibits all investments by foreign entities in numerous business sectors; **Brazil**, with similar total prohibitions; **Chile**, with significant prohibitions and restrictions affecting the telecommunications industry, concession holder companies, the electricity sector, healthcare and energy sectors, among others; **Ecuador**, with relevant restrictions affecting the financial and insurance sectors; **Venezuela**, particularly in the telecommunications industry; **Mexico**, and even the **United States**, with certain restrictions in connection with national security and the financial sector.

Tax aspects

Moreover, in the majority of countries analyzed there are <u>relevant tax obstacles</u> to the execution of cross-border mergers. In this sense, if it were possible, quod non, to execute a cross-border merger, in the majority of the countries analyzed unrealized capital gains would be taxed immediately at target company level and/or shareholder level, and indirect taxes would also be applicable as in any other transfer completed. The accompanying reports reflect this situation in detail in the following countries:

- In **Argentina**, the Law on Income Tax does not allow a cross-border merger to be treated as a "tax-free reorganization", as specifically confirmed by the *"AFIP"* (Argentina's national tax authority) in a number of rulings, meaning that income tax would be generated for the target company (and for its shareholders, regardless the provisions of the Spain-Argentina Double Taxation Treaty, as will be detailed below) on unrealized capital gains, as well as indirect taxes applicable to the transaction in Argentina: Value Added Tax, *"Impuesto sobre los Ingresos Brutos"*, *"Impuesto de Sellos"* (stamp duty), etc.

- In **Australia**, all "amalgamation" transactions are subject to Australian taxes for both the company that transfers its assets and liabilities (the dissolved company) and for its shareholders.
- In **Brazil**, these transactions would be subject to the general tax regime for transfers, with respect to all Brazilian taxes, for both the target company and its shareholders. The special regime provided by Article 21 of Law 9.249/95 is only applicable to mergers of Brazilian companies.
- In **Canada**, the only similar operations to cross-border mergers requires the target company to be liquidated and is therefore subject to all applicable Canadian taxes.
- In **Chile**, cross-border mergers would be taxed under the general tax rules for mergers. Under the Law on Income Taxes, all the profits of the dissolved company would be taxed at 35% and its shareholders would pay 17% or 35% tax on the gain obtained, provided they obtained "an increase in value for tax purposes". The dissolution of the target company would also be previously inspected by the Chilean tax authorities, which is an additional obstacle that discourages and could significantly delay the completion of such trasactions.
- In **Colombia**, no merger transaction gives rise to income tax (Article 14.1 of the *"Estatuto Tributario"*) or value added tax (Article 428.2 of the *"Estatuto Tributario"*) for the dissolved company. However, in view of the absence of legal provisions governing the tax treatment of shareholders, the Directorate of Taxes and Customs (Ruling number 053516, 6 July 2009) has stipulated that shareholders obtain a taxable capital gain if the market value of the shares, cash or other assets received is higher than the acquisition cost of the shares received as a result of the merger.
- In the **United States**, there are certain material adverse U.S. federal income tax consequences for a U.S. corporation (a "USCo") and its U.S. shareholders, as detailed in the U.S. report, that could result from a merger of USCo with and into a foreign corporation (a "ForCo") with the ForCo surviving. Because of concerns that the U.S. taxing authorities have about U.S. corporations moving offshore to minimize their U.S. federal income tax liability, the rules that allow a merger of two USCos to be tax-free are often rendered inapplicable in the case of a merger of a USCo into a ForCo. Although good business reasons may exist to undertake a cross-border merger, shareholders of U.S. corporations often oppose such mergers because of the punitive U.S. tax regimes that could result from the merger.
- In **Morocco**, a cross-border merger gives rise to tax for the company dissolved and its shareholders, in respect of all applicable Moroccan taxes, since the special regime provided by Article 162 of the *"Code Général des Impôts"* is only applicable to Moroccan companies subject to income tax, as specified in the Code. Moreover, as in the case of Chile, the dissolution of a Moroccan company always results in a previous tax audit, entailing an additional obstacle to such merger that could also significantly delay execution.
- In **Mexico**, the merger of a Mexican company with a foreign company will give rise to Mexican income tax for the merging company (the wording of the Mexican-Spanish Double Tax Treaty must also be considered for these purposes, as it will be explained below) and to other taxes applicable to all transfers of goods or rights: flat-rate business tax (*"Impuesto Empresarial a Tasa Única"* o *"IETU"*), value added tax (*"IVA"*), local taxes on property transfers (*"ISAI"*), etc. Article 14-B of the Federal Tax Code only allows

the application of a tax neutrality regime to mergers involving companies resident in Mexico.

As regards the target company's shareholders, Articles 1 and 179 of the Law on Income Tax stipulate that non-residents are also required to pay this tax on assets acquired by the merging company as a consequence of the merger.

- In **Peru**, if a cross-border merger could be completed, this would be treated as a sale for tax purposes and any gain would be taxed at 30% in the dissolved company. The shareholders would pay tax on the profits on liquidation, on the portion that exceeded the par value of the shares plus the additional paid-in capital. The merger would also be subject to indirect taxes (basically the so-called *"IGV"*) at the rate of 19% of the transfer value. This regime has been specifically confirmed by the Peruvian Tax Administration, on a binding basis, in its Report of 229-2005-SUNAT/2B0000 (28 September 2005).
- Finally, in **Venezuela**, if the merger could be completed from a commercial viewpoint it would give rise, as reported by the Venezuelan law firm in its report, to applicable Venezuelan taxes for the target company and its shareholders.

It should also be noted that none of the Double Taxation Treaties signed by Spain include additional specific advantages to cross-border mergers, as compared to other countries Double Taxation Treaties based on the OECD Convention Model.

On the contrary, apart from what we will explain below regarding the Double Taxation Treaties signed between Spain and Argentina and Mexico, some treaties provide for the possibility of charging tax in the State of origin of the transfer (including, for the present purposes, a transfer that is the consequence of the amortization of shares in a merger) of significant shareholdings in companies domiciled in that State.

In this regard, Spain has departed from the OECD's general approach to the taxation of capital gains from the sale by a resident of on Contracting State of stocks and share in companies of the other Contracting State (whether or not the sale takes place in the context of a merger). The OECD's general approach is to assign this tax authority exclusively to the transferor's State of residence (in this case Spain). However, in accordance with Spain's Reservations included in the Commentary on Article 13 of the OECD's Model Convention (point 45), and in accordance with the bilateral agreements concluded, the treaties generally stipulate shared taxation for that State and the State of residence of the company whose shares are sold (in this case, as a consequence of the amortization of shares in a merger), in cases in which the shareholding is "substantial" (of the States analyzed here, this applies to the Treaties with Argentina, Australia, Chile, India, China, United States and Morocco).

This notwithstanding, in the respective Protocols to the Treaties concluded with two of these countries (specifically, the Protocols to the Treaties signed with Mexico and Argentina), it could be interpreted[150] that, when the transfer forms part of a cross-border merger between companies of the same group, it is allowed the application of a tax deferral regime to the capital gains in the State of origin.

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[150] This interpretation is questionable, as these clauses refer more to mergers involving companies residing in one Contracting State that own assets in the other Contracting State which, if those clauses did not exist, would be taxed in that State, whereas, by contrast, the taxes would be deferred in the State of residence under a tax deferral regime.

In the case of the specific clause of the Protocol of the Double Taxation Treaty signed between Spain and Argentina, the law firm of this country interprets, in the same sense as the existing doctrine, that this clause does not allow the application of the Argentinean tax deferral regime to a cross-border merger of a Spanish and an Argentinean company.

In the case of the clause of the Protocol of the Double Taxation Treaty signed between Spain and México, the law firm of this country also considers very doubtful such an interpretation of considering it applicable to a cross-border merger of a Spanish and a Mexican company and, if it were acceptable (which seems remote), this circumstance could, in some cases, even result in a tax cost that is higher than the cost to be deferred, since the "deferred" tax would pay the "frozen" taxes irrespective of the existence of actual economic income (and even if the transfer gave rise to a definitive loss).

In any case, it must be taken into account that the abovementioned Protocols of the Double Tax Treaties does not affect to the indirect taxes applicable to these transactions in each jurisdiction.

Finally, as evidence of the fact that the above-mentioned tax, legal and de facto obstacles are real, it should be noted that, in general, as described in the different reports of the countries analyzed, there have been no cross-border mergers in those jurisdictions. […]