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<p>In the published version of this decision, some information has been omitted, pursuant to articles 30 and 31 of Council Regulation (EU) 2015/1589 of 13 July 2015 laying down detailed rules for the application of Article 108 of the Treaty on the Functioning of the European Union, concerning non-disclosure of information covered by professional secrecy. The omissions are shown thus [...]</p>		<p style="text-align: center;">PUBLIC VERSION</p> <p>This document is made available for information purposes only.</p>
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Subject: State aid SA.44888 (NN/2016) (ex EO/2016) – Luxembourg

Possible State aid in favour of GDF Suez

Sir,

The Commission wishes to inform Luxembourg that, having examined the information supplied by your authorities on the measure referred to above, it has decided to initiate the procedure laid down in Article 108(2) of the Treaty on the Functioning of the European Union (“TFEU”).

1. PROCEDURE

- (1) By letter of 19 June 2013, the Commission sent an information request to the Grand Duchy of Luxembourg requesting detailed information about its tax ruling practice, including a request to provide a list of the tax rulings issued in 2010, 2011 and 2012.¹
- (2) By letter of 17 July 2013, Luxembourg replied in general terms to that letter and submitted part of the requested information.

¹ That letter was sent under reference HT.4020 - Pratiques en matière de ruling fiscal.

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- (3) On 22 December 2014, Luxembourg submitted a list of beneficiaries of tax rulings to comply with the Commission’s request for information of 19 June 2013. That document lists the rulings issued by the Luxembourg tax administration (*Administration des contributions directes*) during the years 2010 to 2012.
- (4) By letter of 23 March 2015, the Commission sent an additional request for information to Luxembourg.² In particular, the Commission requested Luxembourg to provide information about a number of companies, including the GDF Suez Group. The information requested included, *inter alia*, all tax rulings granted to any entity of that group from 2004 until the date of the letter, addressed to that group or to any entity of that group which was in place at that time or which had been in place in the previous 10 years, as well as annual accounts of that group and the legal entities of that group for 2011, 2012 and 2013 and copies of tax declarations.
- (5) On 25 June 2015, Luxembourg replied to that request by submitting detailed information about the tax rulings issued by the Luxembourg tax administration in favour of several companies of the GDF Suez Group, including GDF Suez Treasury Management S.à.r.l. (hereinafter “GSTM”) and LNG Supply S.A. (hereinafter “LNG Supply”). In particular, Luxembourg provided two tax ruling requests and their respective approvals that concerned two almost identical intra-group financing instruments – interest-free mandatorily convertible loans denominated as “ZORA”³ in the tax rulings – issued by both companies (hereinafter: the “GSTM ZORA” and the “LNG ZORA”, respectively; collectively referred to as the “ZORAs”).
- (6) By letter of 1 April 2016, the Commission indicated that, based on the information submitted by Luxembourg, it could not exclude that the tax rulings issued in favour of those GDF Suez group companies regarding the ZORAs constituted incompatible State aid and it requested Luxembourg to provide reasons why those measures would not be selective or why they could be justified. In the same letter, the Commission requested Luxembourg to provide information concerning all companies related to the ZORAs, in particular (i) the financial accounts of the relevant group companies, (ii) the “*advance pricing agreements of [tax advisor]*”^{*} of 11 July 2012 and 1 November 2013”⁴, and (iii) a specific “*APA Letter*”⁵ and “*transfer pricing report*” which were mentioned in the ruling requests of 15 June 2012.
- (7) By letter of 3 May 2016, the Commission reminded Luxembourg to provide the information referred to in recital (6).

² That letter was sent under reference SA 37.267 (2013/CP) - Pratiques en matière de ruling fiscal.

³ Although the precise meaning of the acronym ZORA is not specified in the file, the Commission presumes it to stand for “*Zero-intérêts Obligation Remboursable en Actions*”.

^{*} Parts of this text have been hidden so as not to divulge confidential information; those parts are enclosed in square brackets [...].

⁴ Mentioned in Annex 3 of the *Déclaration pour l’impôt sur le revenu des collectivités et pour l’impôt commercial communal de l’année 2012* of GDF SUEZ Treasury Management S.à.r.l. (“*accords préalable en matière de prix de transfert de [tax advisor] du 11 juillet 2012 et du 11 novembre 2013 (les APAs)*”).

⁵ “APA” stands for Advance Pricing Agreement.

- (8) On 23 May 2016, Luxembourg replied to the Commission’s request for information of 1 April 2016 and submitted the financial accounts requested. In its response, Luxembourg indicated that the letters of 11 July 2012 and 11 November 2013⁶ are not advance pricing agreements, but requests for tax rulings (*demandes de décisions anticipatives*),⁷ which had not been approved by the Luxembourg tax administration. Luxembourg further indicated that what the Commission referred to as the “APA Letter” and the “transfer pricing report” was part of the ruling requests of 11 July 2012 and 11 November 2013. Luxembourg did not submit the “APA Letter” or the “transfer pricing report” to the Commission.

2. FACTUAL AND LEGAL BACKGROUND

- (9) The present Decision concerns two sets of tax rulings issued by the Luxembourg tax administration in favour of GDF Suez group companies.
- (10) On 9 February 2010, the Luxembourg tax administration issued a tax ruling in favour of the GDF Suez group company GSTM regarding the tax treatment of the GSTM ZORA (hereinafter: the “GSTM ZORA tax ruling”). That ruling was partly amended by a ruling issued on 15 June 2012 concerning an increase in the amount to be issued under the GSTM ZORA.
- (11) On 9 September 2008, the Luxembourg tax administration issued a tax ruling in favour of the GDF Suez group company LNG Supply regarding the tax treatment of the LNG ZORA (hereinafter: the “LNG ZORA tax ruling”). Additional ruling requests concerning the LNG ZORA were submitted on 30 September 2008, 3 March 2009, 9 March 2012 and 20 September 2013.⁸ The purpose of the last request, which was accepted by the Luxembourg tax administration by letter of 13 March 2014, was to clarify the tax treatment of a partial conversion of the LNG ZORA (hereinafter: the “partial conversion ruling request”).
- (12) The GSTM ZORA tax ruling and the LNG ZORA tax ruling are collectively referred to as the “contested tax rulings” in this Decision.

2.1. Beneficiary of the contested tax rulings: the GDF Suez Group

- (13) The GDF Suez Group is the result of a merger in 2008 between GDF and the French group Suez (formerly, Lyonnaise des Eaux). GDF was created in 1946 through the nationalisation by France of the assets of private gas and power companies.⁹ The GDF

⁶ Luxembourg clarified that the relevant date was 11 and not 1 November.

⁷ Luxembourg also clarified that the letter of 11 November 2013 replaced the one of 11 July 2012.

⁸ The ruling request of 30 September 2008, approved by a confirmation of the Luxembourg tax administration of the same day, concerns the transfer of LNG Trading to the Netherlands. The ruling request of 3 March 2009, approved by a confirmation of the Luxembourg tax administration of the same day, concerns some changes in the implementation of the LNG ZORA structure (see footnote 64 below). The ruling request of 9 March 2012, approved by letter of the Luxembourg tax administration of the same date, concerns a clarification on the calculation of the margin described in the 2008 LNG ZORA tax ruling request (see footnote 66).

⁹ See the website of ENGIE (<http://www.engie.com/en/group/history-engie-group/>).

Suez Group is headquartered in France. In 2015, the group was renamed Engie.¹⁰ Engie is the largest shareholder of the Belgian group Electrabel, holding a stake of more than 95 % of the share capital of Electrabel.¹¹ Engie is listed on the Paris, Brussels and Luxembourg stock exchanges.¹²

- (14) The GDF Suez Group is present in four main sectors: independent power production, liquefied natural gas, renewable energy and energy efficiency services. The GDF Suez Group is mainly active in the production and supply of energy¹³ and energy trading, exploration, production, supply, transportation and distribution of natural gas, energy efficiency services, and energy infrastructure. The GDF Suez Group also carries out public services entrusted to it under French law and regulations.¹⁴
- (15) The GDF Suez Group currently employs 152 900 people worldwide. In 2014, the revenues of the GDF Suez Group amounted to EUR 74.7 billion.¹⁵ Of the total revenues recorded by the Group, EUR 58.7 billion were generated in Europe, EUR 5.4 billion in Asia, EUR 4.3 billion in Latin America, EUR 3.8 billion in North America and EUR 2.4 billion in the rest of the world.¹⁶ In 2014, 33 % of the group's earnings before interest, tax, depreciation and amortization (EBITDA) was generated in France, 7 % in Belgium, 5 % in the Netherlands, 3 % in Germany, 3 % in the UK, 2 % in Italy, 16 % in other European countries, 12 % in Latin America, 8 % in North America and 11 % in the rest of the world. By business lines, 16 % of the Group's EBITDA is generated by the European Energy division of the group, 30 % by Energy International, 26 % by Infrastructures, 18 % by Global Gas & LNG and 9 % by Energy Services.¹⁷
- (16) GSTM conducts treasury management and financing activities for the GDF Suez Group from Luxembourg. Those activities were originally carried out by two GDF Suez branches operating in Luxembourg: Electrabel Finance and Treasury Management Services (hereinafter: "EFTM") and Tractebel Cash Management Services (hereinafter: "TCMS").¹⁸ According to the tax ruling request of 15 June 2012, "*in general, GSTM*

¹⁰ See the website of ENGIE (<http://www.engie.com/en/group/history-engie-group/>). Although the group is now called Engie, in order to ensure coherence with the tax rulings described below, the decision will refer to it as the GDF Suez Group.

¹¹ See the websites of ENGIE (<http://www.engie.com/en/group/history-engie-group/>) and Electrabel (<https://www.electrabel.com/en/corporate/company/history>).

¹² See the website of ENGIE (<http://www.engie.com/en/journalists/press-releases/gdf-suez-becomes-engie/>).

¹³ In 2014, it operated close to 650 power plants globally (ENGIE, Key Figures, http://library.engie.com/uid_3b0d9abd-abf7-404d-913f-0c30f10eb8d0/beevirtua/beevirtua.html#app=3d20&9557-source=xmlConfs/init.xml&adf3-lang=en&ccb3-pageId=0).

¹⁴ GDF SUEZ 2014 Registration Document, page 378.

¹⁵ ENGIE, Key Figures (<http://www.engie.com/en/investors/key-figures/>).

¹⁶ ENGIE, Key Figures, http://library.engie.com/uid_3b0d9abd-abf7-404d-913f-0c30f10eb8d0/beevirtua/beevirtua.html#app=3d20&9557-source=xmlConfs/init.xml&adf3-lang=en&ccb3-pageId=0.

¹⁷ ENGIE, Key Figures (<http://www.engie.com/en/investors/key-figures/>).

¹⁸ In order to centralise the financing and treasury activity of the then Tractebel Group, several Belgian companies of the group created in 1999 an *association en participation* ("AP") in Luxembourg. Initially, TCMS was set up to manage the business of the AP. Later, TCMS was divided into a finance branch for the Tractebel Group (operating under the same name), and a finance branch for the part of the group controlled by Electrabel S.A., EFTM (see ruling request of 30 of November 1999). TCMS and EFTM

grants loans in various denominations (notably EUR and USD) to related companies and carries out a cash pooling activity and will consequently not only be financed by the ZORA but also by borrowings from group or third parties. The cash pooling activity of GSTM generally varies between EUR [2-7] and EUR [7-12] billion".¹⁹ According to the same ruling request, GSTM had a full time equivalent staff of [0-8] at that time.

- (17) LNG Supply is active in the purchase, sale and trading of LNG, gas and gas derivative products, having a significant number of contracts in place with international energy companies.²⁰

2.2. The contested tax rulings

2.2.1. The GSTM ZORA tax ruling

2.2.1.1. General description of the GSTM ZORA tax ruling

- (18) The GSTM ZORA tax ruling is based on a ruling request dated 9 February 2010 (hereinafter "2010 GSTM ZORA tax ruling request"), submitted by the tax advisors of GDF Suez, [...] (hereinafter: the "tax advisor"). The 2010 GSTM ZORA tax ruling request follows a transfer of assets and liabilities between the companies GSTM and Compagnie Européenne de Financement C.E.F. S.A. (hereinafter: "CEF")²¹, a company belonging to the GDF Suez Group which wholly-owns GSTM. In the context of that transfer, a financing instrument in the form of an interest-free mandatorily convertible loan was issued by GSTM (the GSTM ZORA) to a third GDF Suez group company, Electrabel Invest Luxembourg SA (hereinafter: "EIL"), a Luxembourg-based company also owned by CEF.
- (19) That request consists of a description of the facts, a tax analysis and a tax position on the GSTM ZORA, which the Luxembourg tax administration was asked to confirm.
- (20) According to the 2010 GSTM ZORA tax ruling request, CEF will transfer assets and liabilities to GSTM against a promissory note from GSTM.²² CEF will sell the promissory note to EIL, which will give it back to GSTM in exchange for the ZORA.²³ As a consequence, the promissory note will be cancelled out.
- (21) The GSTM ZORA, as an interest-free mandatorily convertible loan, will upon conversion confer the shares of GSTM on its receiver, EIL. In exchange for the

operated as Luxembourg treasury departments of the Belgian companies Tractebel S.A. and Electrabel S.A. respectively, also performing intra-group financing activities (see ruling request of 4 April 2005).

¹⁹ See ruling request of 15 June 2012, page 2.

²⁰ According to the tax ruling request of 9 September 2008, LNG Trading's main assets at the time were: an LNG terminal capacity agreement and a swap agreement with respect to this terminal, as well as several capacity agreements.

²¹ Later renamed as GDF SUEZ Invest International SA.

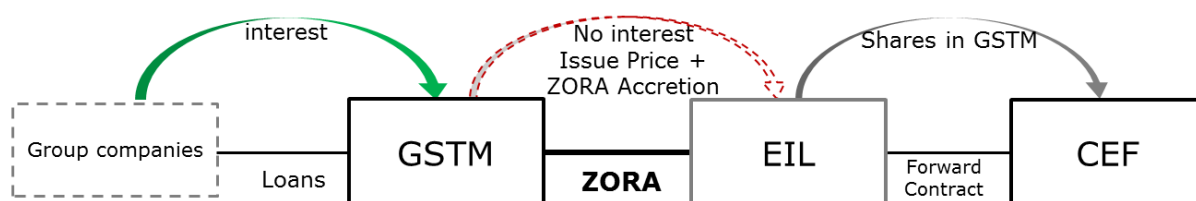
²² The 2010 GSTM ZORA tax ruling request does not explain the need for a promissory note and does not expressly indicate its amount either. According to footnote 1 of the 2010 GSTM ZORA tax ruling request "We have intentionally not mentioned certain preliminary steps as these are for the moment not clearly determined. These steps include the closing of EFTM and TCMS."

²³ According to the 2010 GSTM ZORA tax ruling request, "GSTM will issue an interest-free mandatorily convertible loan ('ZORA') to EIL in an amount equal" to the above mentioned promissory note. The 2010 GSTM ZORA tax ruling request explains that "EIL pays for the ZORA by way of compensation" with the above mentioned promissory note. See 2010 GSTM ZORA tax ruling request, Section I, para. 3.

promissory note, EIL and CEF will enter into a Prepaid Forward Sale Contract (hereinafter: the “Forward Contract”), under which EIL will agree to transfer to CEF the shares that GSTM will issue in favour of EIL upon the mandatory conversion of the ZORA (hereinafter: the “GSTM Shares”).

- (22) Figure 1 below summarises the transactions described in the 2010 GSTM ZORA tax ruling request. GSTM receives assets and liabilities from CEF and the cancellation of the promissory note. In return, GSTM issues the ZORA in favour of EIL. Upon conversion of the ZORA, EIL will receive the GSTM Shares, which it will pass on to CEF under the Forward Contract.

Figure 1 – Illustration of the structure set up in the GSTM ZORA tax ruling



- (23) The 2010 GSTM ZORA tax ruling request concerns the tax treatment of the ZORA. The ruling request seeks the confirmation that:
- (i) GSTM shall be taxed on a fixed margin identified in the ruling request;
 - (ii) the difference between the profit generated by GSTM and the fixed margin can be deducted from GSTM’s taxable profit as an expense linked to the ZORA, with the result that GSTM will only be taxed on that fixed margin; and
 - (iii) the expense linked to the ZORA, which will be incorporated into the value of the shares upon the conversion of the ZORA, will not be taxed as a profit at the level of EIL, in application of Article 22bis of the Luxembourg Income Tax Code (*loi modifiée du 4.12.1967 concernant l’impôt sur le revenu*, hereinafter “LIR”), which allows for the tax neutrality of profits arising from the conversion of debt into equity.
- (24) Since EIL will immediately transfer the GSTM Shares to CEF, the latter will receive the shares plus all the profits accumulated (as represented in the increased value of those shares) free of tax, since any capital gains arising from those shares will be covered by the participation exemption provided under Luxembourg tax law.²⁴
- (25) By letter dated 9 February 2010 (the same date as the 2010 GSTM ZORA ruling request), the Luxembourg tax administration confirmed by way of the GSTM ZORA tax ruling that the content of the 2010 GSTM ZORA tax ruling request was in conformity with Luxembourg tax law.
- (26) A subsequent ruling request dated 15 June 2012 (hereinafter “2012 GSTM ZORA tax ruling request”) contains a tax position on the same ZORA which is almost identical to

²⁴ The participation exemption regime in Luxembourg is laid down in Article 166 LIR.

that of the ruling request of 9 February 2010, except that the amount to be issued under the GSTM ZORA is increased. By letter of the same date, the Luxembourg tax administration confirmed the content of that request was in conformity with Luxembourg tax law

- (27) In addition to those confirmatory rulings, the tax advisor requested a tax ruling by letters of 11 July 2012 and 11 November 2013 concerning the establishment under transfer pricing rules of a fixed margin on which GSTM would be taxed.²⁵ According to GSTM's 2011 annual accounts, such a ruling was necessary because, from 1 January 2012 onwards, the company had to determine a margin on which GSTM would be taxed in accordance with the *Circulaire du directeur des contributions* LIR n° 164/2 of 28 January 2011, concerning intra-group financing activities (hereinafter: the "Circulaire 164/2").²⁶ However, according to Luxembourg, those requests did not result in the issuance of tax rulings by its tax administration.

2.2.1.2. *The GSTM ZORA sample agreement*

- (28) The 2012 GSTM ZORA tax ruling request refers to a "sample of the ZORA agreement", contained in the Annex to that request. That agreement is an unsigned draft agreement between EIL, as the "the Lender", and GSTM, as "the Borrower", concerning a mandatory convertible loan agreement. The terms of "Loan and Interest" are defined in Article 2 of that agreement as follows:

"2.1 Subject to the terms and conditions of this Agreement, the Lender grants the Borrower a Loan in an amount equal to the Principal Amount discounted to the Issue Price.

2.2. The Loan shall not carry interest.

2.3 Any positive difference between the Issue Price and the Principal Amount represents an accretion in value of the Issue Price."

- (29) In Article 1.2.1 of the sample agreement, the following definitions are provided:

*"[...] **Annual Accretion Amount** means the Net Operational Income of Borrower during a relevant Determination Period minus (ii) the corresponding Annual Gross Margin calculated for the relevant Determination Period";*

*"**Margin** means the percentage spread to be generated as agreed from time to time for Luxembourg tax purposes and determined in a transfer pricing report";*

*"**Issue Price** means EUR [...]";*

*"**Principal Amount** shall be determined on each relevant Determination Date using the following formula: Issue Price plus the Total Accretion Amount [...]";*

²⁵ Annex 3 of the *Déclaration pour l'impôt sur le revenu des collectivités et pour l'impôt commercial communal de l'année 2012*.

²⁶ See *Notes explicatives au bilan au 31 décembre 2011*, included as Annex 3 of the *Déclaration pour l'impôt sur le revenu des collectivités et pour l'impôt commercial communal de l'année 2011*.

“Conversion Price means EUR 1,000 of Principal amount per Conversion Share”;

“Conversion Shares means the number of shares to be issued by the Borrower upon conversion, such amount to be determined by way of using the following formula: Principal amount to be divided by EUR 1,000 rounded down to the nearest whole number”.

- (30) According to Article 4 of the sample agreement, the loan has a maximum term of 15 years. At the end of that period, it shall be converted into shares, unless it is terminated and converted into shares earlier by any party with the written consent of the other party.
- (31) According to Article 5 of the sample agreement, the *“Borrower shall repay the Loan by the Issuance of the Conversion Share to the Lender on the Conversion Date or on such earlier date [...]”*

2.2.1.3. Tax treatment of the GSTM ZORA from the perspective of GSTM

- (32) According to the 2010 GSTM ZORA tax ruling request, GSTM’s yearly taxable profit shall be equal to a margin agreed with the Luxembourg tax administration. GSTM will be taxed on that margin and the difference between the profit actually generated by GSTM and the margin on which it is taxed will be considered an expense which GSTM may deduct every year from its taxable income. That expense is described in the GSTM ZORA sample agreement as an increase in the value of the issue price of the ZORA²⁷ and is referred to in the 2010 GSTM ZORA ruling request as *“Accrétion sur ZORA”* or *“ZORA Accretion”* (hereinafter: *“ZORA Accretion”*).
- (33) On this point, the 2010 GSTM ZORA tax ruling request states that *“the ZORA will accrue expenses to the extent of the pre-tax profits of GSTM minus a net margin [...] The increase in value of the obligation under the ZORA will lead to a corresponding deductible expense for GSTM”*.²⁸ According to the 2010 GSTM ZORA tax ruling request, *“[t]he ZORA is structured in such a way that effectively, GSTM will derive, as per its commercial accounts, an overall net spread of [1/(50-100)%] on the principal value of all its assets, including those assets financed with normal borrowings (‘Margin’)”*.²⁹ According to the 2010 GSTM ZORA tax ruling request, *“the margin that GSTM will earn on its assets (financed with the ZORA and normal liabilities) will qualify as arm’s length”*.³⁰ The margin seems to have been changed in 2012. In fact, according to GSTM’s 2011 annual accounts, from 1 January 2012 onwards the company was supposed to set the margin in accordance with Circulaire 164/2.³¹ In

²⁷ See recital (28).

²⁸ 2010 GSTM ZORA tax ruling request, page 2 (emphasis added by the Commission).

²⁹ 2010 GSTM ZORA tax ruling request, page 2.

³⁰ See 2010 GSTM ZORA tax ruling request, page 5, para. 5.

³¹ See *Notes explicatives au bilan au 31 décembre 2011*, included as Annex 3 of the *Déclaration pour l’impôt sur le revenu des collectivités et pour l’impôt commercial communal de l’année 2011*.

GSTM's 2012 tax return, the margin is calculated by applying a percentage of 0.042 % on the value of the debts financing the assets.³²

- (34) The 2010 GSTM ZORA tax ruling request further explains that “GSTM will have income derived from its assets, but it will have expenses equalling the aforementioned income minus the Margin due to the accretion of the ZORA”.³³ Consequently, as the margin is based on a fixed percentage over the value of assets, “the ZORA Accretion will always match the interest income less the interest (and any foreign currency exchange difference) on the borrowings less the Margin”.³⁴ The 2010 GSTM ZORA tax ruling request also indicates that “in the unlikely event that the accounting treatment would not be totally in line with the obligations under the ZORA agreement, the resulting profit or loss reflected in the annual accounts will not affect the tax position set out above”.³⁵
- (35) A pro-forma balance sheet of GSTM was provided in the 2010 GSTM ZORA tax ruling request and is represented in Figure 2.

Figure 2 – Illustration of the recording of the ZORA financing instrument in the balance sheet of GSTM according to the GSTM ZORA 2010 ruling request

GSTM	
Assets	Liabilities
Receivables	Share Capital ZORA
Receivables	Liabilities
Total Assets	Total Liabilities

2.2.1.4. Tax treatment of GSTM ZORA from the perspective of EIL

- (36) According to the 2010 GSTM ZORA tax ruling request, EIL will book the value of the ZORA in its accounts at the Issue Price. At conversion, EIL will receive the GSTM Shares which will reflect the Principal Amount, i.e. the Issue Price, plus all the ZORA Accretions accumulated until the date of the conversion. The 2010 GSTM ZORA tax ruling request asks for a confirmation that, in application of Article 22bis LIR, EIL will not recognise any taxable profit arising out of this conversion, as that provision provides that the conversion of a loan into the share capital of the debtor will not lead to the realisation of any capital gains for tax purposes.

³² Annex 3 of the *Déclaration pour l'impôt sur le revenu des collectivités et pour l'impôt commercial communal de l'année 2012*.

³³ 2010 GSTM ZORA tax ruling request, page 2.

³⁴ 2010 GSTM ZORA tax ruling request, page 2.

³⁵ 2010 GSTM ZORA tax ruling request, page 2. In the same line, the 2012 GSTM ZORA tax ruling request states: “to the extent the accounting treatment would differ from the annual accretion under the ZORA agreement, GSTM will for tax purposes still only report the Margin.”

- (37) According to the 2010 GSTM ZORA tax ruling request, “*EIL will continue to value the ZORA in its commercial accounts at book value^[.] or, alternatively, will accrete the ZORA from cost price to the expected redemption price over the term of the ZORA^[.]*”.³⁶
- (38) The first option (i.e. maintaining the value of the ZORA at book value) would be based on the “*Umgekehrte Massgeblichkeit*” (i.e. reverse alignment) rule, which is – according to the 2010 GSTM ZORA tax ruling request – provided for in Articles 55.1.c.dd and 61.1.e of the Code on the Commercial Registry and the Financial Statements of Companies dated 19 December 2002.³⁷ According to the reverse alignment rule, “*it is possible to derogate from normally applicable accounting rules if such derogation is necessary in order to avoid adverse tax implications; the assumption is that tax laws allow for certain valuation methods which due to mandatory accounting rules could not be fully used (‘exceptional value adjustments for taxation purposes only...’). In such cases, the normal accounting treatment may not be applied*”. In order to avoid adverse tax implications, the ZORA should be booked in accordance with the *Umgekehrte Massgeblichkeit*. The 2010 GSTM ZORA tax ruling request further explains that “*based on the principle of prudence, the fact that as a result of the mandatory conversion, the ZORA has elements that justify the same treatment as shares and the fact that the facility of Article 22bis LIR³⁸ could otherwise not be used, the ZORA should be booked at the lower of the historical cost price or the actual value*”.³⁹
- (39) The second option (i.e. accrete the value of the ZORA from its acquisition price to the expected redemption price) is not further pursued. The GSTM ZORA tax ruling request acknowledges in a footnote⁴⁰ that, “*in absence of any specific requirements under Luxembourg law and to reflect the substance of the remuneration of the ZORA, it may be recommended for EIL to accrue for the income over the life of ZORA. This would result in an increase on the value of ZORA in EIL’s accounts, unless the actual value of ZORA is lower.*”⁴¹
- (40) The tax records and accounts of EIL provided to the Commission show that the value of the ZORA in EIL’s accounting books has been maintained at book value (EUR 1 036 912 507).⁴² The amounts of the ZORA Accretion do not seem to have been recorded in EIL’s accounts as an increase in the value of EIL’s assets or as an income related to the ZORA.

³⁶ 2010 GSTM ZORA tax ruling request, page 3.

³⁷ 2010 GSTM ZORA tax ruling request, footnote 3.

³⁸ Article 22bis(2), reads as follows: “*Par dérogation à l’article 22, alinéa 5, les opérations d’échange visées aux numéros 1 à 4 ci-dessous ne conduisent pas à la réalisation des plus-values inhérentes aux biens échangés, à moins que, dans les cas visés aux numéros 1, 3 et 4, soit le créancier, soit l’associé ne renoncent à l’application de la présente disposition : 1. lors de la conversion d’un emprunt : l’attribution au créancier de titres représentatifs du capital social du débiteur. En cas de conversion d’un emprunt capitalisant convertible, l’intérêt capitalisé se rapportant à la période de l’exercice d’exploitation en cours précédant la conversion est imposable au moment de l’échange*”.

³⁹ 2010 GSTM ZORA tax ruling request, para. 3, page 5 (emphasis added by the Commission).

⁴⁰ 2010 GSTM ZORA tax ruling request, footnote 4.

⁴¹ 2010 GSTM ZORA tax ruling request, footnote 4.

⁴² See Bilan au 31 décembre 2012, included as Annex 1 to the *Déclaration pour l’impôt sur le revenu des collectivités et pour l’impôt commercial communal de l’année 2012*.

- (41) According to the 2010 GSTM ZORA tax ruling request, “*at maturity, the mandatory conversion of the ZORA into GSTM shares will, unless the holder chooses not to, be governed by Article 22bis of LIR [...]; for Luxembourg tax purposes, the original cost (if and to the extent maintained until the conversion date) and the acquisition date of the ZORA can be rolled-over to the shares acquired in return. Under this scenario, upon the mandatory conversion of ZORA, EIL should not recognise any income*”.⁴³
- (42) Therefore, “*as a result of [...] article 22bis LIR, no corporate income tax will be due on the conversion and the historical acquisition price [...] as well as the historical acquisition date of the ZORA will be used for the shares that are issued at that time*”.⁴⁴ No further explanation is provided in the tax ruling request as to the application of Article 22bis LIR.

2.2.1.5. Tax treatment of the Forward Contract from the perspective of EIL and of CEF

- (43) According to the 2010 GSTM ZORA tax ruling request, under the Forward Contract EIL undertakes to sell to CEF the GSTM Shares received upon conversion of the ZORA against immediate payment of the price. The delivery of the GSTM Shares will therefore take place at the moment of the conversion of the ZORA (i.e. at the date of the ZORA’s maturity or sooner in the case of an earlier conversion).
- (44) The 2010 GSTM ZORA tax ruling request indicates that the forward obligation of EIL under the Forward Contract is to be considered “debt” for Luxembourg tax purposes. In fact, that obligation has been recorded in EIL’s balance sheet as non-subordinated debt.⁴⁵ According to the 2010 GSTM ZORA tax ruling request, EIL will value the obligations under the Forward Contract at the same value as the ZORA⁴⁶ and EIL will “*not incur in any foreign exchange or bad debt risk. Consequently, in relation to the holding of the ZORA and the obligation under the Forward Contract, EIL will not have any Luxembourg tax liability apart from the legal minimum annual net wealth tax*”.⁴⁷
- (45) The 2010 GSTM ZORA tax ruling request concludes that CEF is the owner of the GSTM Shares as from the moment that it enters into the Forward Contract, even though those shares have not yet been issued.⁴⁸ In addition, CEF will record the payment under the Forward Contract in its commercial accounts as “Financial Fixed Assets”.⁴⁹ According to the ruling request, those assets “*will be and will continue to be valued at cost price*”.⁵⁰

2.2.1.6. The tax position sought in the 2010 GSTM ZORA tax ruling request

⁴³ 2010 GSTM ZORA tax ruling request, page 3.

⁴⁴ 2010 GSTM ZORA 2010 tax ruling request, para. 6, page 6.

⁴⁵ See Note 3 to EIL’s unaudited annual accounts for 2012 (the amount of the Forward Contract coincides with the initial amount of the ZORA).

⁴⁶ 2010 GSTM ZORA tax ruling request, page 5, para. 4.

⁴⁷ 2010 GSTM ZORA tax ruling request, page 3.

⁴⁸ 2010 GSTM ZORA tax ruling request, page 4.

⁴⁹ CEF’s 2013 annual accounts indicate, in Note 5 to the balance sheet, that “*a loan [...] was granted under a prepaid forward sale contract entered into by GDF Suez Invest International S.A. and Electrabel Invest Luxembourg S.A. GDF Suez Invest International S.A. is the beneficiary of GDF Suez Treasury Management S.à r.l. shares to be issued by the latter.*”

⁵⁰ 2010 GSTM ZORA tax ruling request, page 3.

(46) In the 2010 GSTM ZORA tax ruling request, the tax advisor states a tax position and requests the Luxembourg tax administration's confirmation of the following:

- *“In order to avoid adverse tax consequences for EIL, the ZORA should be booked in accordance with the ‘Umgekehrte Massgeblichkeit’ rule. Based on the principle of prudence, the fact that as a result of the mandatory conversion the ZORA has elements that justify the same treatment as shares and the fact that the facility of article 22bis LIR could otherwise not be used, the ZORA should be booked at the lower of the historical cost price or the actual value. The commercial accounts will follow this tax treatment”*.⁵¹
- *“The obligations of EIL under the Forward Contract qualify, in accordance with EIL’s commercial accounts, as debt for income and net-wealth tax purposes. For tax purposes, the valuation of this debt, as well as the valuation of the ZORA in the hands of EIL will be kept at the same amount. As a result, EIL will not realise any profit”*.⁵²
- *“The Margin that GSTM will earn on its assets (financed with the ZORA and normal liabilities) will qualify as arm’s length and will be included in taxable income on the income tax return of GSTM (together with the return on undistributed after tax profits). To the extent the accounting treatment would differ from the annual accretion under the ZORA agreement, GSTM will for tax purposes still only report the Margin (plus the return on undistributed profits)”*.⁵³
- *“The conversion of the ZORA into shares will be governed by article 22bis LIR. As a result of the Umgekehrte Massgeblichkeit rule and article 22bis LIR, no corporate income tax will be due on the conversion and the historical acquisition price (if and to the extent maintained until the conversion date) as well as the historical acquisition date of the ZORA will be used for the shares that are issued at that time”*.⁵⁴

(47) Figure 3 below summarises the tax treatment of the income and expenses derived from the ZORA by GSTM and by EIL:

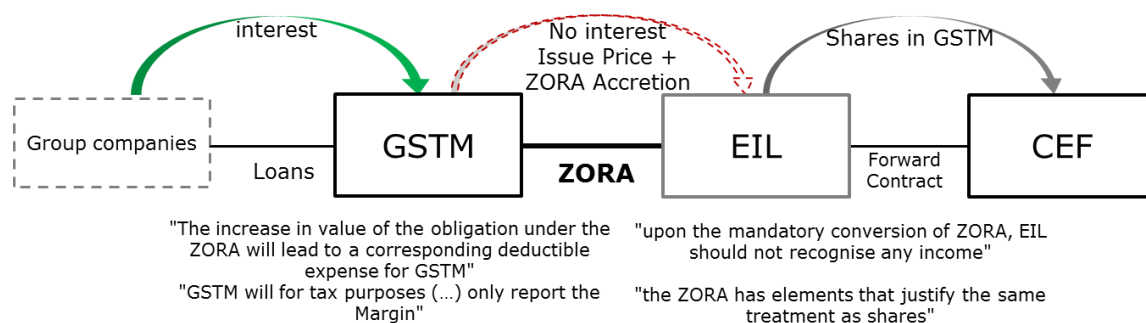
⁵¹ 2010 GSTM ZORA tax ruling request, page 5, section 3.

⁵² 2010 GSTM ZORA tax ruling request, page 5, section 4.

⁵³ 2010 GSTM ZORA tax ruling request, page 5, section 5. The language of the 2012 GSTM ZORA tax ruling request is slightly different.

⁵⁴ 2010 GSTM ZORA tax ruling request, page 6, section 6.

Figure 3 –Tax treatment described in the GSTM ZORA 2010 tax ruling request



2.2.1.7. Implementation of the GSTM ZORA ruling

- (48) According to the accounts provided to the Commission⁵⁵, EIL “granted a mandatory convertible loan amount of EUR 1 036 912 506.84 to [GSTM] with a maturity of 15 years from June, 17 2011”.⁵⁶ For each year, an amount equal to the yearly ZORA Accretion has been recorded as a financial liability of GSTM against the corresponding expense in the profit and loss account.⁵⁷
- (49) The implementation of the GSTM ZORA tax ruling in GSTM’s tax return is illustrated in Figure 4 and Figure 5 below, which present extracts from the tax returns of the company for the period 2011 and 2012 respectively. In 2011, the “net earnings before tax and ZORA Accretion” amounted to EUR [45 000 000 - 50 000 000]. GSTM’s taxable base is calculated as $[1/(50-100\%)]$ of the total average assets of the company for the 2011 period, which amounted to EUR 3.7 billion. The taxable profit retained for GSTM on this basis amounts to EUR [550 000 - 600 000] (to which an amount designated as “remuneration of capital” is added for an amount of EUR 8 326). The difference between the calculated profit and the actual profit in the amount of EUR 44 931 567 was recorded in the tax return as the tax deductible ZORA Accretion.

⁵⁵ GSTM and EIL’s accounts and tax returns have been provided for years 2011 and 2012. In addition, Luxembourg has provided in its letter of 23 May 2016 the annual accounts of GSTM, EIL and CEF for 2013, 2014 and 2015.

⁵⁶ See Note 3 to EIL’s unaudited annual accounts for 2012. See also explanatory notes to GSTM’s balance sheet at 31 December 2011, in Annex 3 of the *Déclaration pour l’impôt sur le revenu des collectivités et pour l’impôt commercial communal de l’année 2011* of GSTM.

⁵⁷ Recorded in the profit and loss account under: “other interest payable and similar charges”. See GSTM’s profit and loss accounts for 2011 and 2012.

Figure 4 – The calculation of the tax base of GSTM for the year 2011 as detailed in Annex 3 to the 2011 tax return of GSTM

Total actif	De	à	Nombre de jours	Moyenne*
8.691.871.776	2/05/2011	31/12/2011	244	3.729.884.433

* calculé sur une base mensuelle

Total des dettes finançant les actifs	3.729.202.241
Revenu net avant impôt et avant accréation du Zora	[45.000.000-50.000.000]
Revenu net avant impôt et avant accréation du Zora relatif au capital	8.326
Revenu net avant impôt et avant accréation du Zora relatif à la dette finançant les actifs	[45.000.000-50.000.000]
Total	<u>[45.000.000-50.000.000]</u>
Marge de [1/(50-100)%]	[550.000-600.000]
Rémunération sur le capital	8.326
Rémunération sur la dette finançant les actifs (marge de [1/(50-100)%])	[550.000-600.000]
Marge nette totale	<u>[550.000-600.000]</u>

La marge a déjà été comptabilisée dans les comptes annuels, aucun ajustement n'est à opérer.

Calcul du montant imposable

	<u>Euro</u>
Résultat de l'exercice	420.802
Ajouter: impôts	<u>[150.000-200.000]</u>
Montant imposable	<u>[550.000-600.000]</u>
Impôt sur le revenu des collectivités	<u>[100.000-150.000]</u>

Figure 5 – The calculation of the tax base of GSTM in reference to the ruling requests of 2010 and 2012 in Annex 3 to the 2012 GSTM tax return (the figure does not present Annex 3 in full)

Annexes à la déclaration pour l'impôt sur le revenu des collectivités et pour l'impôt commercial communal de l'année 2012 et la déclaration de la fortune au 1er janvier 2013 au nom de:
GDF SUEZ Treasury Management S.à r.l., numéro fiscal 2011 2416 545

Annexe 3

STAW/NGOK

Notes explicatives

Généralités

Référence est faite aux lettres de Loyens & Loeff du 9 février 2010 et 15 juin 2012.

Marge sur activité de financement

Référence est faite aux accords préalables en matière de prix de transfert de Loyens & Loeff du 11 juillet 2012 et du 11 novembre 2013 (les APAs).

La marge sur activité de financement est calculée comme suit:

Montant moyen des dettes finançant les actifs*	du	au	jours	%**	marge
[9.000.000.000-10.000.000.000]	4,2 bps	1/01/2012	31/12/2012	366	4,2 bps [3.000.000-4.000.000]
Total			366		

*Calculé sur une base mensuelle

**Nous nous référons à l'étude de prix de transfert comme prévu dans les APAs.

Rémunération du capital à risque

Capital moyen*	du	au	jours	rémunération du capital à risque
[2.000.000-3.000.000]	1/01/2012	31/12/2012	366	[20.000-30.000]
Total			366	

*Calculé sur une base mensuelle

Calcul de l'accrétion sur Zora

Revenu net avant impôt et avant accrétion du Zora	[100.000.000-150.000.000]
Moins: rémunération en capital	[20.000-30.000]
Moins: marge minimum	[3.000.000-4.000.000]
Accrétion sur Zora	[100.000.000-150.000.000]

Le montant de l'accrétion sur le Zora tel qu'indiqué dans les comptes annuels n'est pas conforme aux APAs (pas suffisant). Par conséquent, un ajustement de EUR[40K-50K] a été opéré dans le bilan fiscal et le compte de profits et pertes fiscal et cet ajustement sera reflété dans les comptes commerciaux de l'année 2013.

- (50) In GSTM’s annual statutory accounts, the amount corresponding to the ZORA Accretion for the periods 2011 and 2012 is reported in the accounting category “Non Subordinated Debts” under the designation “Amounts owed to affiliated undertakings becoming due and payable after less than one year” in “Annual accretion”. The amounts reported in this accounting category over the period 2011 to 2015 in GSTM’s statutory accounts⁵⁸ are presented below.

Table 1 – Accumulated Accretion recorded in the financial accounts of GSTM

EUR million	2011	2012	2013	2014	2015
‘Accumulated Accretion’	44.9	[100-150]	[300 – 350]	[450 – 500]	[600 – 650]

- (51) The nominal amount of the ZORA financing instrument of EUR 1 036 912 506 is reported under the same category designation “Amounts owed to affiliated undertakings becoming due and payable after less than one year” in “Financial debt”. That amount did not vary over the period 2011 to 2015.

Assets	2011	Liabilities	2011
Goodwill	14 683 885	Subscribed capital	2 000 000
Receivables from related companies	4 249 889 106	Profit of financial year	420 802
Investments	1 735 037 565	Total own funds	2 420 802
Treasury bills	159 462 864	ZORA	1 036 912 507
Deposits	1 831 461 057	ZORA Accretion	44 931 567
Bank account	685 086 826	Other debt	7 604 517 303
Other	16 250 473	Other	2 083 687
TOTAL ASSETS	8 691 871 776	TOTAL EQUITY AND LIABILITIES	8 691 871 776

2.2.1.8. Increase of the GSTM ZORA

- (52) According to the 2012 GSTM ZORA tax ruling request, GDF Suez was planning to increase the ZORA “*in the near future*” following the reimbursement of a previous profit participating loan that CEF held in the past. As a consequence, the total amount to be used under the ZORA was expected to increase in the years following 2012 from the initial amount of ca. EUR [0.8 – 1.2] billion to a sum between EUR [7-12] and [37-42] billion.⁵⁹ According to that ruling request, each new tranche of the ZORA would be implemented “*as a restatement of the existing ZORA as a result of which always one*”

⁵⁸ In 2015, the company was according to the accounts renamed ENGIE Treasury Management S.à.r.l.

⁵⁹ According to this ruling, the cash pooling activity of GSTM would generally remain in the range of EUR [2-7]-[7-12] billion.

agreement is in place".⁶⁰ That increase was also subject to the confirmation of the GSTM ZORA tax ruling.

2.2.2. The LNG ZORA tax ruling

2.2.2.1. General description of the LNG ZORA tax ruling

- (53) On 9 September 2008, the tax advisor submitted a tax ruling request (hereinafter "2008 LNG ZORA tax ruling request") to the Luxembourg tax administration concerning the tax treatment of the LNG ZORA on behalf of Suez LNG Trading S.A. (hereinafter: "LNG Trading",⁶¹ later replaced by GDF Suez LNG Holding S.à.r.l., hereinafter: "LNG Holding") and two companies to be incorporated in Luxembourg, referred to at the time as "LuxCo2" and "LuxCo3". That ruling request was accepted by a confirmation of the Luxembourg tax administration of the same date.⁶²
- (54) The set-up of the LNG ZORA, as described in the 2008 LNG ZORA tax ruling request, follows the same structure as the GSTM ZORA.
- (55) According to the 2008 LNG ZORA tax ruling request, LNG Trading incorporated two new taxable Luxembourg companies: LuxCo2, which was later renamed "GDF Suez LNG (Luxembourg) S.à.r.l." (hereinafter: "LNG Luxembourg") and LuxCo3, later renamed LNG Supply. Subsequently, LNG Trading transferred its whole enterprise (its LNG business activity) to LNG Luxembourg, for an estimated price of approximately USD 750 million. LNG Luxembourg then sold the enterprise to LNG Supply, which financed the purchase price by issuing to LNG Luxembourg an USD denominated interest-free mandatorily convertible loan (the LNG ZORA).⁶³
- (56) According to the 2008 LNG ZORA tax ruling request, LNG Luxembourg financed the investment in the LNG ZORA by entering into a Prepaid Forward Sale Contract (hereinafter: the "LNG Forward Contract") with LNG Trading. Under that contract, LNG Luxembourg agreed to transfer to LNG Trading the shares that LNG Supply would issue upon the mandatory conversion of the ZORA (hereinafter: the "LNG Supply Shares"). Under the Forward Contract, the amount due as consideration for the transfer of the LNG Supply Shares (estimated at the time of the ruling to amount to USD 750 million) would be offset against LNG Luxembourg's debt towards LNG Trading, resulting from the original sale of the enterprise by LNG Trading.⁶⁴

⁶⁰ Consequently, the maturity date of 17 June 2026 remains in place for all the amounts covered by the ZORA agreement.

⁶¹ As it will be explained below, LNG Trading's business was later transferred to another company of the GDF Suez Group. LNG Trading was liquidated on 1 October 2012.

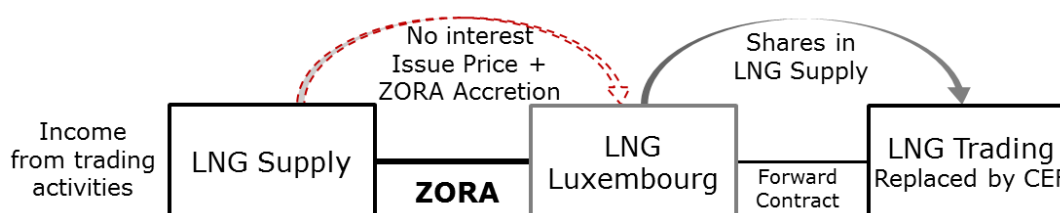
⁶² A stamp of the Luxembourg tax administration on the last page of the 2008 LNG ZORA tax ruling request indicates that it was approved by that administration ("for approval").

⁶³ The Swiss branch of LNG Trading would no longer manage the business after the transfer of the activity to LNG Supply and would be liquidated. LNG Supply would employ at least [5-10] persons in Luxembourg.

⁶⁴ This structure was later modified, as explained in the tax ruling request of 3 March 2009. According to this ruling request, LNG Trading's shares were transferred to CEF, one of the Luxembourg financing companies of the Tractebel/Electrabel Group. CEF would then incorporate three new Luxembourg companies: LNG Holding, LNG Luxembourg and LNG Supply. The LNG ZORA structure is implemented between these three companies.

- (57) Figure 6 below summarises the transactions in the 2008 LNG ZORA tax ruling request. LNG Supply receives the assets and liabilities previously belonging to LNG Trading. LNG Supply issues the LNG ZORA in favour of LNG Luxembourg. Through the ZORA, it receives financing from LNG Luxembourg to pay for the acquisition of the aforementioned assets and liabilities. Upon redemption of the LNG ZORA, LNG Luxembourg will receive the LNG Supply Shares and pass them on to LNG Holding under the LNG Forward Contract. As described in the tax ruling request of 3 March 2009, LNG Holding takes the position of LNG Trading under the 2008 LNG ZORA tax ruling request.

Figure 6 – Illustration of the structure set up in the LNG ZORA 2008 tax ruling



2.2.2.2. Tax treatment of LNG ZORA from the perspective of LNG Supply

- (58) According to the 2008 LNG ZORA tax ruling request, the yearly profit that LNG Supply generates will be reduced to a margin agreed with the Luxembourg tax administration and LNG Supply will be taxed on that margin. The difference between the profit actually generated by LNG Supply and the margin on which it is taxed is considered an expense linked to the LNG ZORA, which LNG Supply deducts every year from its taxable income.
- (59) In particular, the 2008 LNG ZORA tax ruling states that *“the ZORA will accrue to the extent of the pre-tax profits of [LNG Supply] minus the net margin [...]. The increase in value of the obligation under the ZORA will lead to a corresponding deduction for [LNG Supply]”*.⁶⁵ This increase in the obligation is referred in the 2008 LNG ZORA tax ruling request as “accrue on the ZORA” or “expense on the ZORA”.
- (60) According to the 2008 LNG ZORA tax ruling request, the LNG ZORA is structured in such a way *“that effectively, [LNG Supply] will derive, as per its commercial accounts, an overall net spread of [1/(50-100)%] of the value of the gross amount of assets as shown in its balance sheet, such net spread however not being lower than [0.0-0.50%] of the annual gross turn-over derived from the Enterprise (hereinafter: the ‘Margin’)*”.⁶⁶ According to the 2008 LNG ZORA tax ruling request, *“the margin will qualify as arm’s length”* because LNG Supply will not *“incur foreign exchange and/or*

⁶⁵ 2008 LNG ZORA tax ruling request, page 2.

⁶⁶ The tax ruling request of 9 March 2012 later clarifies that the *“net spread of [1/(50-100)%] of the value of the gross assets”* should be considered as referring to the average value of the assets financed by the ZORA, whereas “gross turnover” should be considered the total income of LNG Supply as per its commercial accounts, including income and expenses resulting from interest expenses incurred and foreign exchange differences relating to the different activities of LNG Supply.

bad debt risk on its trade".⁶⁷ The 2008 LNG ZORA tax ruling request further explains that *"in other words, the [LNG Supply] gross income [from its activities (the LNG business)], minus all operational expenses incurred and minus the expense on the ZORA is approximately the Margin"*.⁶⁸

2.2.2.3. Tax treatment of LNG ZORA from the perspective of LNG Luxembourg

- (61) According to the 2008 LNG ZORA tax ruling request, LNG Luxembourg will book the value of the ZORA in its accounts at its issue price. At conversion, LNG Luxembourg will receive the LNG Supply Shares, the value of which will incorporate the ZORA Accretions accumulated until the date of the conversion. The 2008 LNG ZORA tax ruling request asks confirmation that, in application of Article 22bis LIR, LNG Luxembourg will not recognise any taxable profit arising out of that conversion, as that provision stipulates that the conversion of a loan into the share capital of the debtor will not lead to the realisation of any capital gains for tax purposes.
- (62) LNG Luxembourg's tax records and accounts provided to the Commission show that the value of LNG ZORA in LNG Luxembourg's accounting books has been maintained at book value (EUR 646 000 000)⁶⁹ until 2013, when a partial conversion of the ZORA took place (described in section 2.2.2.7 below).

2.2.2.4. Tax treatment of the Forward Contract from the perspective of LNG Luxembourg and for LNG Holding

- (63) As explained above, LNG Luxembourg financed its investment in the LNG ZORA by its obligation under the LNG Forward Contract entered into with LNG Holding. The tax consequences of this Forward Contract between LNG Luxembourg and LNG Holding are identical to those described in the 2010 GSTM ZORA ruling request.

2.2.2.5. Tax position sought in the LNG ZORA 2008 tax ruling request

- (64) In the 2008 LNG ZORA tax ruling request, the tax advisor states a tax position and requests the Luxembourg tax administration to confirm the following:
- *"In order to avoid adverse tax consequences for [LNG Luxembourg], the ZORA should be booked in accordance with the Umgekehrte Massgeblichkeit rule. Based on the principle of prudence, the fact that as a result of the mandatory conversion the ZORA has elements that justify the same treatment as shares and the fact that the facility of article 22bis LIR could otherwise not be used, the ZORA should be booked at the lower of the historical cost price or the actual value. The commercial accounts will follow this tax treatment."*⁵⁷⁰
 - *"The obligations of [LNG Luxembourg] under the Forward Contract qualify, in accordance with [LNG Luxembourg]'s commercial accounts, as debt for income and net-wealth tax purposes. For tax purposes, the valuation of this debt, as well*

⁶⁷ 2008 LNG ZORA tax ruling request, page 5, para. 6 and for the explanation page 3.

⁶⁸ 2008 LNG ZORA tax ruling request, page 2.

⁶⁹ See *Bilan au 31 décembre 2011*, included as Annex 1 to the *Déclaration pour l'impôt sur le revenu des collectivités et pour l'impôt commercial communal de l'année 2011*.

⁷⁰ 2008 LNG ZORA tax ruling request, page 5, section 4.

*as the valuation of the ZORA in the hands of [LNG Luxembourg] will be kept at the same amount. As a result, [LNG Luxembourg] will not realise any profit.*⁷¹

- *“The Margin that LNG Supply will earn on the ZORA funded Enterprise as per its commercial accounts will qualify as arm’s length.”*⁷²
- *“The conversion of the ZORA into shares will be governed by article 22bis LIR. As a result of the Umgekehrte Massgeblichkeit rule and article 22bis LIR, no corporate income tax will be due on the conversion and the historical acquisition price (if and to the extent maintained until the conversion date) as well as the historical acquisition date of the ZORA will be used for the shares that are issued at that time.”*⁷³

2.2.2.6. Implementation of the LNG Zora tax ruling

- (65) LNG Supply’s 2010 accounts⁷⁴ show that a “loan agreement mandatorily exchangeable into shares between LNG Luxemburg and LNG Supply” was entered into in 2009 for an Issue Price of USD 646 000 000. The maturity of the loan is 15 years from 30 October 2009 (i.e. it expires on 30 October 2024).⁷⁵ For each year, an amount equal to the yearly ZORA Accretion is recorded as a financial liability of LNG Supply against the corresponding expense in the profit and loss account.⁷⁶
- (66) The implementation of the tax ruling in the tax return of LNG Supply is illustrated in Figure 7 below which presents extracts from the tax returns of the company for the period 2011.

⁷¹ 2008 LNG ZORA tax ruling request, page 5, section 5.

⁷² 2008 LNG ZORA tax ruling request, page 5, section 6.

⁷³ 2008 LNG ZORA tax ruling request, page 5, section 7.

⁷⁴ LNG Supply's accounts and tax returns have been provided for years 2011 and 2012 (the accounts are also available for 2010). LNG Luxembourg’s accounts and tax returns have been provided for years 2011, 2012 and 2013. In addition, Luxembourg has provided in its letter of 23 May 2016 the annual accounts of LNG Supply's, LNG Luxembourg's and LNG Holding's for 2013 and 2014.

⁷⁵ Note 9 to the Annual accounts of LNG Supply of 31 December 2010.

⁷⁶ Recorded in the profit and loss account under “*other interest payable and similar charges*”.

Figure 7 – Calculation of the tax base of LNG Supply, as presented in annex 3 to the tax return of 2011

Accrétion du Zora

Le montant de l'accrétion sur le Zora tel que indiqué dans les comptes annuels n'est pas conforme à aux accords préalables signé par les autorités fiscales le 9 septembre 2008 et 9 mars 2012.

Par conséquent, un bilan fiscal a été dressé afin de tenir compte du montant correct. En effet, suivant cet accord préalable, la société n'est imposable que sur la marge (voir ci-dessous).

Calcul de la marge

Marge nette de $\frac{1}{50-100}\%$ sur la valeur des actifs bruts (càd la valeur moyenne des actifs finançant le Zora), avec un minimum de $\frac{100-0.5}{100}\%$ du chiffre d'affaires brut dérivant des actifs qui ont été transférés à la Société (càd le revenu total de la Société).

Marge minimum

	Produit total	Taux	Date début	Date fin	Marge minimum (USD)
	1.573.579.569	$\frac{100-0.5}{100}\%$	01/01/11	31/12/11	<u><u>[3.500.000-4.000.000]</u></u>

Marge nette de $\frac{1}{50-100}\%$ sur la valeur moyenne des actifs finançant le Zora

Date	Zora				Marge $\frac{1}{50-100}\%$ (USD)
01/01/11	692.817.329	(Voir déclaration fiscale 2010)			
31/12/11	812.590.069				
Total	<u><u>1.505.407.398</u></u>				
Moyenne	<u><u>752.703.699</u></u>				
	Zora	Taux	Date début	Date fin	Marge $\frac{1}{50-100}\%$ (USD)
	752.703.699	$\frac{1}{50-100}\%$	01/01/11	31/12/11	<u><u>[100.000-150.000]</u></u>

(67) In LNG Supply's annual statutory accounts, the amounts corresponding to the ZORA Accretion are reported in the accounting category "Non subordinated debts",⁷⁷ under the designation "Amounts owed to affiliated undertakings becoming due and payable after more than one year" in "Accumulated Accretion".⁷⁸ The amounts reported in that accounting category over the period 2009 to 2014 in LNG Supply's statutory accounts are presented in Table 2.

Table 2 – Accumulated Accretion in the financial accounts of LNG Supply

USD million	2009	2010	2011	2012	2013	2014
-------------	------	------	------	------	------	------

⁷⁷ Under the category 'Creditors' in 2010 annual accounts.

⁷⁸ Under the category 'Financial debt GS LNG Lux Annual Accretion' in 2010 annual accounts.

'Accumulated Accretion'	10.8	46.2	165.8	[350 – 400]	[650 – 700]	[450 – 500]
-------------------------	------	------	-------	----------------	----------------	----------------

(68) The nominal amount of the LNG ZORA of USD 646 000 000 is reported under the same category “Amounts owed to affiliated undertakings becoming due and payable after less than one year” in “Financial debt”. That amount does not vary over the period 2009 to 2013. In 2014, it was reduced to USD 452 200 000 following a partial conversion carried out that year.

2.2.2.7. The LNG ZORA 2008 partial conversion ruling request

(69) A tax ruling request of 20 September 2013 concerns the tax implications of the partial conversion of the LNG ZORA.

(70) According to that ruling request, [...]. For that purpose, it would execute a first partial conversion into shares for an amount estimated at that date of USD [300-400] million. If executed, the conversion would, according to the ruling request, take place by the end of 2013 or the beginning of 2014. On the day of the conversion, a decision would be adopted to reduce the nominal capital of LNG Supply to an amount equal to the conversion amount. According to the ruling request, “[f]or [LNG Luxembourg] the Partial Conversion of the ZORA has no tax consequences”.⁷⁹ “Due to the capital reduction by [LNG Supply], [LNG Holding] will recognise a profit equal to the difference between the nominal amount of shares converted and the conversion amount. This profit will be visible in the books of [LNG Holding] and is covered by the participation exemption.”⁸⁰

(71) LNG Supply’s 2014 annual accounts provided by Luxembourg to the Commission in its letter of 23 May 2016 show that a partial conversion took place that year. According to the accounts, the conversion was split “between a part of the nominal amount and a part of accretion.”⁸¹ Accordingly, in September 2014, LNG Supply increased its capital by USD 699.9 million to partially refund the LNG ZORA. Shares were issued at nominal value and were subsequently cancelled through a capital decrease at their nominal amount.⁸² According to the accounts of LNG Holding, this operation generated a capital gain of USD 506.1 million⁸³ for LNG Holding.

2.3. Description of the relevant national legal framework

(72) In Luxembourg, corporate income tax is payable on the business profits realised during the year minus business losses and deductible expenses.⁸⁴ According to Article 163(1) corporate income tax is levied on the taxable income of the corporate taxpayer during the calendar year.⁸⁵

⁷⁹ 2008 LNG ZORA partial conversion ruling request, page 2, section 3.1.

⁸⁰ 2008 LNG ZORA partial conversion ruling request, page 2, section 3.1.

⁸¹ 2014 LNG Supply accounts, note 8.

⁸² 2014 LNG Supply accounts, note 7.

⁸³ 2014 LNG Holding accounts, note 3.

⁸⁴ See Articles 6(1), 7, 14, 45, 109, 163, 167 LIR.

⁸⁵ Article 163(1) LIR provides: “L’impôt sur le revenu des collectivités frappe le revenu imposable réalisé par le contribuable pendant l’année du calendrier.”

- (73) According to Article 159 LIR, domestic companies and foreign companies resident in Luxembourg are taxed on the totality of their income.⁸⁶ A company is deemed resident in Luxembourg if it has its corporate address or its central management in Luxembourg. Domestic companies and foreign companies resident in Luxembourg are therefore liable to corporation tax on their worldwide profits, unless a tax treaty applies. For the permanent establishments of non-resident companies, Article 160 LIR. provides that those entities are only subject to source taxation.⁸⁷
- (74) The Luxembourg corporate income tax rate consists of a corporate income tax on profits (“*impôt sur le revenu des collectivités*” or “*IRC*”), taxed at a rate of 21 %, and, for companies established in the city of Luxembourg, a municipal business tax on profits (“*impôt commercial communal*”), taxed at a rate of 6.75 %. In addition, there is a 5 % surcharge on the 21 % tax rate for an employment fund calculated on the IRC.⁸⁸ Since 1 January 2011, all companies subject to tax in Luxembourg are taxed on their taxable profit at the standard tax rate of 28.80 %.⁸⁹ With the changes introduced for tax year 2013, the aggregate income tax rate increased from 28.80 % to 29.22 % for Luxembourg City.⁹⁰
- (75) Article 7(1) LIR provides that the taxable income is obtained through the deduction of the special expenses provided in Article 109 LIR from the total net income.⁹¹ Other special deductions are laid down in Article 167 LIR. As regards the tax treatment of interest on debts, according to Article 109 LIR, interest payments on loans, bonds, debentures and other debts of the company are deductible as normal business expenses at the level of the company making the payment.⁹² At the level of the beneficiary,

⁸⁶ Article 159(1) LIR provides: “*Sont considérés comme contribuables résidents passibles de l’impôt sur le revenu des collectivités, les organismes à caractère collectif énumérés ci-après, pour autant que leur siège statutaire ou leur administration centrale se trouve sur le territoire du Grand-Duché.*” Article 159(2) LIR provides: “*L’impôt sur le revenu des collectivités porte sur l’ensemble des revenus du contribuable.*”

⁸⁷ Article 160 L.I.R.: “*Sont passibles de l’impôt sur le revenu des collectivités pour leur revenu indigène au sens de l’article 156, les organismes à caractère collectif de l’article 159 qui n’ont ni leur siège statutaire, ni leur administration centrale sur le territoire du Grand-Duché.*” Article 156 LIR defines source income as follows: “*Sont considérés comme revenus indigènes des contribuables non résidents : 1. le bénéfice commercial au sens des articles 14 et 15: a) lorsqu’il est réalisé directement ou indirectement par un établissement stable ou un représentant permanent au Grand-Duché, excepté toutefois lorsque le représentant permanent est négociant en gros, commissionnaire ou représentant de commerce indépendant;*”

⁸⁸ In 2012, the solidarity surcharge was increased from 5 % to 7 % with effect from tax year 2013.

⁸⁹ The Luxembourg corporate income tax consists of a corporate income tax on profits (“*impôt sur le revenu des collectivités*” or “*IRC*”), taxed at a rate of 21 %, and, for companies established in Luxembourg City, a municipal business tax on profits (“*impôt commercial communal*”), taxed at a rate of 6.75 %. In addition, there is a 5 % surcharge on the 21 % tax rate for an employment fund calculated on the IRC. In 2012, the solidarity surcharge was increased from 5 % to 7 % with effect from tax year 2013. With the changes introduced for tax year 2013, the aggregate income tax rate increases from 28.80 % to 29.22 % for Luxembourg City. In addition, Luxembourg companies are subject to an annual net wealth tax, which is levied at a rate of 0.5 % on the company’s worldwide net worth on 1 January of each year.

⁹⁰ In addition, Luxembourg companies are subject to an annual net wealth tax, which is levied at a rate of 0.5 % on the company’s worldwide net worth on 1 January of each year.

⁹¹ Article 7(1) LIR reads as follows: “*Le revenu imposable est obtenu par la déduction des dépenses spéciales visées à l’article 109 du total des revenus nets.*”

⁹² Art. 109(1) provides the following: “*Sont déductibles du total des revenus nets, dans la mesure où elles ne sont à considérer ni comme dépenses d’exploitation ni comme frais d’obtention, les charges et*

interest income received is subject to corporate income tax in accordance with Articles 97(1)(3) or (1)(5) LIR.⁹³

- (76) As regards the distribution of profits, Article 164(1) and (2) LIR states that those are not deductible and therefore must be included in the taxable income, regardless of whether they are effectively distributed or not.⁹⁴ Under Article 164(3) LIR, taxable income must also include the so-called “hidden profit distributions” (“*distribution cachée de bénéfices*”). A hidden profit distribution arises in particular when a shareholder, a stockholder or an interested party receives either directly or indirectly benefits from a company or an association which he normally would not have received if he had not been a shareholder, a stockholder or an interested party.⁹⁵
- (77) The Circulaire 164/2, although applicable to financing companies, explains the scope of Article 164(3) LIR. According to this Circulaire, Article 164(3) LIR “*provides that [a hidden profit] distribution is to be included in the taxable base of the company or association and establishes the arm’s length principle in domestic law. An intra-group service (including an intra-group financing transaction) has been rendered if, in comparable circumstances, an independent enterprise had been willing to pay another independent enterprise to carry out that activity, or if it had carried out that activity itself. Where an intra-group service has been rendered, as with other types of intra-group transfers, one should ascertain whether an arm’s length price is charged for such service, i.e. a price corresponding to the price which would have been charged and agreed to by independent enterprises in comparable circumstances.*”⁹⁶ Consequently,

dépenses suivantes, qualifiées de dépenses spéciales: 1a. les intérêts débiteurs, dans la mesure où ces intérêts ne sont pas en rapport économique avec des revenus exemptés.”

⁹³ Luxembourg tax law defines various categories of interest subject to income tax and corporate income tax in Articles 97(1)(3)-(1)(5) LIR, which include: interest on bonds and similar values including profit shares and repayment premiums (97(1)(3)), interest on debt claims secured by registration in the mortgage register (97(1)(4)), and interest on debt-claims such as loans, funds, contributions, deposits, and current accounts (97(1)(5)).

⁹⁴ Article 164(1) LIR reads as follows: “*Pour déterminer le revenu imposable, il est indifférent que le revenu soit distribué ou non aux ayants droit*”. Article 164(2) establishes that the remunerations on certain financial instruments, such as instruments giving right to a participation in the annual profit or in the liquidation proceeds, qualify as profit distributions and must therefore be included in the taxable base of the company generating the income (i.e. they cannot be deducted). (“*Sont à considérer comme distribution dans le sens de l’alinéa qui précède, les distributions de quelque nature qu’elles soient, faites à des porteurs d’actions, de parts bénéficiaires ou de fondateurs, de parts de jouissance ou de tous autres titres, y compris les obligations à revenu variable donnant droit à une participation au bénéfice annuel ou au bénéfice de liquidation.*”)

⁹⁵ Article 164(3) LIR provides: “*Les distributions cachées de bénéfices sont à comprendre dans le revenu imposable. Il y a distribution cachée de bénéfices notamment si un associé, sociétaire ou intéressé reçoit directement ou indirectement des avantages d’une société ou d’une association dont normalement il n’aurait pas bénéficié s’il n’avait pas eu cette qualité.*”

⁹⁶ Circular 164/2, Section 2. See also the Commission Decision of 21 October 2015 in case SA.38375, Luxembourg – *Alleged aid to FFT*, under appeal, paragraph 75. See also Luxembourg case law applying this provision: judgments of the Tribunal Administratif du Grand-Duché de Luxembourg of 27 Novembre 2006 (rôle n°21033) (“*Les distributions cachées de bénéfices visées par l’article 164 (3) LIR existent si un associé ou un actionnaire reçoit directement ou indirectement d’une société des avantages qu’il n’aurait pu obtenir en l’absence de ce lien. La situation concernée est celle où un gestionnaire prudent et avisé n’aurait pas accordé un avantage similaire à un tiers*”) and of 4 October 2012 (rôle n°28782) (“*Les distributions cachées de bénéfices visées par l’alinéa 3 de l’article 164 LIR existent si un associé, sociétaire ou un intéressé reçoit, ne serait-ce qu’indirectement, d’une société un avantage qu’il n’aurait*

Article 164(3) LIR imposes the application of the arm's length principle to intra-group transactions.

- (78) In addition, any Luxembourg company receiving a distribution of dividends must include such distribution (including hidden distributions) in its taxable income,⁹⁷ unless the distribution is received in connection with shares for which the participation exemption pursuant to Article 166 LIR applies.⁹⁸
- (79) Finally, as regards the conversion of a loan into shares, according to the general evaluation principles laid down in Article 22(5) LIR, an exchange of assets should be considered as the sale of the given asset, followed by the acquisition of the asset acquired in return at a price corresponding to its estimated disposal value, thus potentially giving rise to a taxable capital gain. As an exception to this general rule, Article 22bis(2) number 1 LIR stipulates that the conversion of a loan into the share capital of the debtor will not lead to the realisation of a capital gains for tax purposes. However, that same provision provides that such an exception does not cover the interest accrued on the loan up until the date of the exchange.⁹⁹

3. POSITION OF LUXEMBOURG

- (80) In its letter of 23 May 2016, Luxembourg submits that the ZORAs described in both the 2010 GSTM ZORA tax ruling request and in the 2008 LNG ZORA tax ruling request are debt instruments and claim that the tax treatment granted under the contested tax rulings is in conformity with the Luxembourg tax rules.
- (81) Luxembourg explains that the ZORA constitutes debt at the level of the issuing companies and argues that, from an accounting perspective under the Luxembourg

pas pu obtenir en l'absence de son lien spécial, c'est-à-dire que ladite disposition légale vise la situation où un gestionnaire prudent et avisé n'aurait pas accordé un avantage similaire à un tiers."

⁹⁷ Article 97(1) LIR.

⁹⁸ Luxembourg's participation exemption regime provides for an exemption from income, withholding and net wealth tax for qualifying investments held by qualifying entities. In particular, Article 166 LIR provides, in line with Council Directive 2011/96/EU of 30 November 2011 on the common system of taxation applicable in the case of parent companies and subsidiaries of different Member States, OJ L 345, 29.12.2011, p. 8–16 (hereinafter, the "Parent – Subsidiary Directive"), that dividends or capital gains received by a Luxembourg entity from a shareholding will be fully exempt from Luxembourg corporate income tax if the entity deriving such income holds or commits itself to hold this shareholding for an uninterrupted period of at least 12 months, and the shareholding does not fall below either a 10% participation or a EUR 1.2 million acquisition price. In addition, according to Article 147 LIR, no withholding tax on dividend distributions will apply if the conditions for the participation exemption are met.

⁹⁹ Article 22bis(2), number 1 reads as follows: "*Par dérogation à l'article 22, alinéa 5, les opérations d'échange visées aux numéros 1 à 4 ci-dessous ne conduisent pas à la réalisation des plus-values inhérentes aux biens échangés, à moins que, dans les cas visés aux numéros 1, 3 et 4, soit le créancier, soit l'associé ne renoncent à l'application de la présente disposition : 1. lors de la conversion d'un emprunt : l'attribution au créancier de titres représentatifs du capital social du débiteur. En cas de conversion d'un emprunt capitalisant convertible, l'intérêt capitalisé se rapportant à la période de l'exercice d'exploitation en cours précédant la conversion est imposable au moment de l'échange."* Additionally, Article 22bis(4) provides the following: "*Dans le chef de l'associé, le prix et la date d'acquisition des titres reçus en échange correspondent au prix et à la date d'acquisition des titres donnés en échange. En cas de paiement d'une soulte à l'associé, le prix d'acquisition des titres reçus en échange est à diminuer du montant de ladite soulte."*

accounting rules (hereinafter: the “Lux GAAP”), the issuing companies are obliged to record the ZORA Accretion as a cost in the annual accounts.¹⁰⁰ In line with this accounting qualification, the provisions on the ZORAs should be considered a cost/expense for the issuing companies. Luxembourg submits that, according to Article 40 LIR, the tax balance sheet must follow the commercial balance sheet.¹⁰¹ The contested tax rulings do not deviate from the principle of Article 40 LIR, since the accounting treatment determines the tax treatment of the ZORAs. Therefore, from a tax perspective, the expenses linked to the annual ZORA Accretion are deductible at the level of the issuing companies, since they are not linked with any exempted income.

- (82) At the level of the companies holding the ZORAs, Luxembourg invokes the principle of prudence which is “*one of the pillars of the Luxembourg accounting and tax laws.*” According to that principle, an income should not be accounted for until the moment at which it is realised, whereas costs must be recorded from the moment at which their realisation is likely or possible. Following that principle, latent capital losses at the end of an exercise must be recorded. By contrast, capital gains not yet realised should not be recorded in the accounts. To avoid taxation of income which has not been realised, Article 23 LIR states that the assets other than amortisable assets must be valued at the acquisition price or at cost. According to the principle of prudence, a profit cannot be taxed until it is realised. According to Luxembourg, the principle of prudence therefore implies that for a same contract (financial instrument), a cost can be recorded at the level of the issuer, whereas no corresponding revenue is recorded (and therefore taxed) at the level of the lender.
- (83) As to the valuation of the ZORA at the level of the lender, according to the Lux GAAP, it must be valued at its acquisition cost (rather than at its market value). The applicable law concerning annual accounting does not provide for any derogation to this principle concerning instruments such as a ZORA. Accordingly, the ZORA does not imply any taxable income for the lender before conversion. As the final amount of the market value of the ZORA will not be known until the moment of its conversion into shares, no sums must be recorded annually by the companies holding that instrument and therefore there can be no taxation. According to Luxembourg, the contested tax rulings apply the principle of prudence in conformity with Luxembourg accounting and tax law.
- (84) Luxembourg submits that Article 22(5) LIR provides that the exchange of assets can in principle give rise to a taxable capital gain. It further submits that Article 22bis(2), number 1, LIR concerns the lender, who exchanges, within the framework of the conversion of the loan, its credit for a participation in the share capital of the borrower.

¹⁰⁰ Luxembourg's generally accepted accounting principles (Lux GAAP) are contained in Chapter 2 of Title 2 of the *loi du 19 décembre 2002 concernant le registre de commerce et des sociétés ainsi que la comptabilité et les comptes annuels des entreprises*, as amended by the *Loi du 18 décembre 2015 modifiant, en vue de la transposition de la directive 2013/34/UE du Parlement européen et du Conseil du 26 juin 2013 relative aux états financiers annuels, aux états financiers consolidés et aux rapports y afférents de certaines formes d'entreprises, modifiant la directive 2006/43/CE du Parlement européen et du Conseil et abrogeant les directives 78/660/CEE et 83/349/CEE du Conseil.*

¹⁰¹ Article 40 LIR reads as follows: “*Lorsque les prescriptions régissant l'évaluation au point de vue fiscal n'exigent pas une évaluation à un montant déterminé, les valeurs à retenir au bilan fiscal doivent être celles du bilan commercial ou s'en rapprocher le plus possible dans le cadre des prescriptions prévues, suivant que les valeurs du bilan commercial répondent ou ne répondent pas aux mêmes prescriptions.*”

To avoid a realisation of the capital gain inherent to the ZORA, the value of the shares received in exchange must correspond to the initial value of the ZORA. The initial date of acquisition of the ZORA is also maintained.¹⁰²

- (85) Luxembourg further argues that, in this case, the shares received by the lenders are considered as a replacement of the ZORA, since they are convertible into shares. The exchange is therefore made in a tax neutral manner on the basis of Article 22bis LIR. In such a case, the historic acquisition cost, as well as the historic acquisition date, is taken into account for the shares received upon conversion.¹⁰³
- (86) According to Luxembourg, the contested tax rulings therefore merely confirm the right which Article 22bis LIR confers on the lender. They do not confer a selective advantage, since that provision is applicable to all taxpayers in Luxembourg without restriction – be they multinationals or not – and has commonly been applied for many years. The possibility to convert loans into shares is present in the Luxembourg laws since 1967 and constitutes a well-known principle in other Member States.

4. ASSESSMENT OF THE CONTESTED MEASURES

4.1. Existence of aid

- (87) According to Article 107(1) TFEU, any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the provision of certain goods is incompatible with the internal market, in so far as it affects trade between Member States. For a measure to be categorised as aid within the meaning of Article 107(1) TFEU, all the conditions set out in that provision must be fulfilled.¹⁰⁴ It is thus well-established that, for a measure to be categorised as State aid, there must, first, be an intervention by the State or through State resources; second, the intervention must be liable to affect trade between Member States; third, it must confer a selective advantage on an undertaking and, fourth, it must distort or threaten to distort competition.¹⁰⁵
- (88) As regards the first condition for a finding of aid, the contested tax rulings were issued by the Luxembourg tax administration, which is an organ of the Luxembourg State. Those rulings were used by the GDF Suez Group companies GSTM, EIL, LNG Supply, LNG Luxembourg and, indirectly, by CEF and LNG Holding, to calculate their yearly corporate income tax liability in Luxembourg. The Luxembourg tax administration accepted those calculations and, on that basis, accepted that the tax paid by those GDF Suez Group companies corresponds to their corporate income tax liability in Luxembourg. The contested tax rulings are therefore imputable to Luxembourg. As regards the financing of the measures through State resources, the Court of Justice has consistently held that a measure by which the public authorities grant certain undertakings a tax exemption which, although not involving a positive transfer of State

¹⁰² Page 5 of the submission of 23 May.

¹⁰³ Page 5 of the submission of 23 May.

¹⁰⁴ See Case C-399/08 P *Commission v Deutsche Post* EU:C:2010:481, paragraph 38 and the case-law cited therein.

¹⁰⁵ See Case C-399/08 P *Commission v Deutsche Post* EU:C:2010:481, paragraph 39 and the case-law cited therein.

resources, places the persons to whom it applies in a more favourable financial situation than other taxpayers constitutes State aid.¹⁰⁶ The rulings confirm that the ZORA Accretions are deductible expenses for GSTM and LNG Supply, whereas the corresponding income, once realised, would be exempt in the hand of EIL and LNG Luxembourg. As a consequence, the ZORA Accretions remain untaxed in Luxembourg, so that the contested tax rulings can be said, at this stage, to reduce the corporate income tax liability in Luxembourg of those companies and the GDF Suez Group as a whole and therefore give rise to a loss of State resources. That is because any expenses of GDF Suez Group companies declared tax deductible in Luxembourg, as well as any revenues of GDF Suez Group companies declared tax-exempt in Luxembourg, result in a loss of tax revenue that would have otherwise been available to Luxembourg.¹⁰⁷

- (89) As regards the second condition for a finding of aid, the companies benefitting from the contested tax rulings are part of the GDF Suez Group, a globally active multinational group operating on various energy markets in all Member States, so that any aid in their favour is liable to affect intra-Union trade. Similarly, a measure granted by the State is considered to distort or threaten to distort competition when it is liable to improve the competitive position of its recipient as compared to other undertakings with which it competes.¹⁰⁸ To the extent the contested tax rulings relieve the GDF Suez Group companies of a tax liability they would otherwise have been obliged to pay, the aid granted under those rulings constitutes operating aid, in that it relieves those undertakings from a charge that they would normally have had to bear in their day-to-day management or normal activities. The Court of Justice has consistently held that operating aid in principle distorts competition,¹⁰⁹ so that any aid granted to those undertakings should be considered to distort or threaten to distort competition by strengthening the financial position of those companies and the GDF Suez group as a whole on the markets on which they operate. In particular, by relieving those undertakings of a tax liability they would otherwise have had to bear and which competing undertakings have to carry, the contested tax rulings free up resources for those undertakings and the group to which they belong to invest in their business operations, thereby distorting competition on the market, so that the fourth condition for a finding of aid is also fulfilled in this case.
- (90) As regards the third condition for a finding of aid, an advantage for the purposes of Article 107(1) TFEU is any economic benefit that an undertaking would not have obtained under normal market conditions, that is to say, in the absence of the State intervention.¹¹⁰ Thus, whenever the financial situation of an undertaking is improved as

¹⁰⁶ See Joined Cases C-106/09 P and C-107/09 P *Commission v. Government of Gibraltar and United Kingdom* EU:C:2011:732, paragraph 72 and the case-law cited therein.

¹⁰⁷ See Joined Cases C-106/09 P and C-107/09 P *Commission v. Government of Gibraltar and United Kingdom*, ECLI:EU:C:2011:732, paragraph 72 and the case-law cited.

¹⁰⁸ See Case 730/79 *Phillip Morris* EU:C:1980:209, paragraph 11 and Joined Cases T-298/97, T-312/97 etc. *Alzetta* EU:T:2000:151, paragraph 80.

¹⁰⁹ Case C-172/03 *Heiser* EU:C:2005:130, paragraph 55 (emphasis added). See also Case C-494/06 P *Commission v. Italy and Wam* EU:C:2009:272, paragraph 54 and the case-law cited and C-271/13 P *Rousse Industry v Commission* EU:C:2014:175, paragraph 44. Joined Cases C-71/09 P, C-73/09 P and C-76/09 P *Comitato "Venezia vuole vivere" and Others v Commission* EU:C:2011:368, paragraph 136. See also Case C-156/98 *Germany v Commission* EU:C:2000:467, paragraph 30, and the case-law cited.

¹¹⁰ Case C-39/94 *SFEI and Others* EU:C:1996:285, paragraph 60; Case C-342/96 *Spain v Commission* EU:C:1999:210, paragraph 41.

a result of a State intervention, an advantage is present. Such an improvement is shown by comparing the financial situation of the undertaking as a result of the contested measure with the financial situation of that undertaking had the measure not been granted.¹¹¹ An advantage can consist both in the granting of positive economic advantages as well as in the mitigation of charges normally included in the budget of an undertaking.¹¹² As regards fiscal measures, an advantage may be granted through different types of reduction in an undertaking's tax burden and, in particular, through a reduction in the taxable base or in the amount of tax due.¹¹³ As the Commission will demonstrate in Section 4.2, the contested tax rulings result in a lowering of GSTM's and LNG Supply's annual corporate tax liability by allowing those companies to deduct the ZORA Accretions from their taxable profit. They also result in a lowering of EIL and LNG Luxembourg's corporate income tax liability by exempting the corresponding income from those companies' taxable profit. The contested tax rulings therefore confer an economic advantage on those companies and the GDF Suez Group as a whole through a reduction in their taxable bases.

- (91) As regards the selective nature of that advantage, the Court of Justice has previously held that in the case of an individual aid measure, as opposed to a scheme, “*the identification of the economic advantage is, in principle, sufficient to support the presumption that it is selective*”,¹¹⁴ without it being necessary to analyse the selectivity of the measure according to the three-step analysis devised by the Court of Justice for fiscal State aid schemes.¹¹⁵ Since the contested tax rulings are individual aid measures granted only to certain undertakings of the GDF Suez Group, a finding that those measures grant an advantage to those undertakings already suffices to conclude that that advantage is selective in nature.
- (92) Nevertheless, for the sake of completeness, in Section 4.2 the Commission will examine those measures according to the three-step analysis devised by the Court of Justice for fiscal aid schemes to demonstrate that they are also selective under that analysis. However, in so doing, the Commission's assessment of whether the contested tax rulings constitute a derogation from the reference system (the second step of the selectivity analysis) will coincide with its assessment of whether those measures confer an advantage on the beneficiaries of those rulings. That is because the identification of the advantage flowing from a tax measure requires a comparison of the economic position of the beneficiary of that measure with the economic position of that undertaking had the measure not been granted, while the identification of the derogation from the reference system requires a comparison of the economic position of the beneficiary of that measure with the economic position of operators who are in a comparable factual and legal situation to the beneficiary in the light of the objectives of that reference system and who do not benefit from the tax measure in question. In other

¹¹¹ See Case 173/73 *Italy v Commission* EU:C:1974:71, paragraph 13.

¹¹² See, for instance, Case C-387/92 *Banco Exterior de España* EU:C:1994:100.

¹¹³ See Case C-66/02 *Italy v Commission* EU:C:2005:768, paragraph 78; Case C-222/04 *Cassa di Risparmio di Firenze and Others* EU:C:2006:8, paragraph 132; Case C-522/13 *Ministerio de Defensa and Navantia* EU:C:2014:2262, paragraphs 21 to 31. See also point 9 of the Commission notice on the application of the State aid rules to measures relating to direct business taxation OJ C 384, of 10.12.98, p. 3.

¹¹⁴ See Case C-270/15 P *Belgium v Commission* EU:C:2016:489, paragraph 49 and Case C-15/14 P *Commission v MOL* EU:C:2015:362, paragraph 60.

¹¹⁵ See Case T-385/12 *Orange v Commission* EU:T:2015:117, paragraph 53.

words, where a tax measure results in an unjustified reduction of the tax liability of a beneficiary that would otherwise be subject to a higher level of tax under the applicable reference system, that reduction constitutes both the advantage granted by the tax measure and the derogation from the reference system.

4.2. Existence of a selective advantage

- (93) The function of a tax ruling is to establish in advance the application of the ordinary tax system to a particular case in view of its specific facts and circumstances. However, like any other fiscal measure, the granting of a tax ruling must respect the State aid rules. Where a tax ruling endorses a result that does not reflect in a reliable manner what would result from a normal application of the ordinary tax system, without justification, that ruling may confer a selective advantage upon the addressee, in so far as that selective treatment results in a lowering of that taxpayer's tax liability in the Member State as compared to companies in a similar factual and legal situation.
- (94) First and foremost, the Commission considers, at this stage, that the contested tax rulings derogate from the normal application of Articles 109(1) and 164 LIR by allowing GSTM and LNG Supply to deduct the ZORA Accretions from their taxable profit. At this stage, the Commission considers that the Luxembourg tax administration should not have considered the ZORA Accretions to constitute a deductible expense within the meaning of Article 109(1) LIR and that it should have considered those payments to constitute a taxable distribution of profits within the meaning of Article 164 LIR. The Commission therefore takes the preliminary view that the contested tax rulings confer a selective advantage on GSTM and LNG Supply, and on the GDF Suez Group as a whole, in the form of a reduction of their taxable base and thus their corporate income tax liability in Luxembourg.¹¹⁶
- (95) By an alternative line of reasoning, the Commission considers that, if the contested tax rulings correctly apply Article 109(1) LIR, which the Commission contests by its primary line of reasoning, they nevertheless derogate (i) from Article 22bis, number 1, and Article 97(1)(3) or 97(1)(5) LIR by leaving untaxed the corresponding income from the ZORA Accretions, once realised, at the level of EIL and LNG Luxembourg, respectively,¹¹⁷ and (ii) from the ordinary rules of taxation of corporate profit in Luxembourg, or from Article 164(3) LIR, by allowing GSTM and LNG Supply to determine their taxable profit in a manner that deviates from a reliable approximation of a market-based outcome in line with the arm's length principle, namely on the basis of a fixed margin whereby the taxable profit of GSTM is determined as [1/(50-100)%] of its assets and the taxable profit of LNG Supply is determined as [1/(50-100)%] of its assets or [0.0-0.50%] of its turnover.¹¹⁸
- (96) As explained in recital (92), the Commission will examine the contested tax rulings following the three-step analysis devised by the Court of Justice for determining whether a particular fiscal measure is selective.¹¹⁹

¹¹⁶ Section 4.2.1

¹¹⁷ Section 4.2.2

¹¹⁸ Section 4.2.2.2

¹¹⁹ See Joined Cases C-78/08 to C-80/08 *Paint Graphos* ECLI:EU:C:2009:417.

- (97) As a first step, the common or normal tax regime applicable in the Member State is identified: “the reference system”. As a general rule, for the purposes of determining whether a particular fiscal measure gives rise to a selective advantage, a reference system must be identified which is composed of a consistent set of rules that apply on the basis of objective criteria to all undertakings falling within its scope as defined by its objective. The identification of the reference system therefore depends on elements such as the taxable persons, the taxable base, the taxable events and the applicable tax rates.
- (98) As a second step, it is determined whether the tax measure in question constitutes a derogation from that system, in so far as it differentiates between economic operators who, in light of the objectives intrinsic to the system, are in a comparable factual and legal situation. As explained in recital (92), where a tax measure results in an unjustified reduction of the tax liability of a beneficiary that would otherwise be subject to a higher level of tax under the applicable reference system, that reduction constitutes both the advantage granted by the tax measure and the derogation from the reference system.
- (99) As a third step, if the measure constitutes a derogation from the reference system, it is then established whether that measure is justified by the nature or the general scheme of the reference system. A tax measure which constitutes a derogation to the application of the reference system may be justified if the Member State concerned can show that that measure results directly from the basic or guiding principles of that tax system.¹²⁰ If that is the case, the tax measure is not selective. The burden of proof in that third step lies with the Member State.

4.2.1. Selective advantage arising from a misapplication of Articles 109(1) and 164 LIR

4.2.1.1. Determination of the reference system

- (100) By the contested tax rulings, the Luxembourg tax administration endorsed an interpretation of Article 109(1) LIR whereby the ZORA Accretions are considered to constitute tax deductible expenses for GSTM and LNG Supply within the meaning of that provision.¹²¹ As regards that interpretation, the Commission considers the reference system to be Articles 109(1) and 164 LIR, which are general provisions of the LIR that apply to all corporate taxpayers subject to tax in Luxembourg.
- (101) According to Article 163 LIR, corporate taxpayers are liable to corporate income tax in Luxembourg on the basis of their taxable income. A taxpayer’s income is its business profits realised during the tax year minus business losses and deductible expenses.¹²² As regards deductible expenses, the LIR draws a distinction between payments on debt (interest), which are tax deductible, and remuneration of equity (distribution of profits), which are not.
- (102) Article 109(1) LIR provides that interest payments on loans, bonds, debentures and other debts of a company are deductible as normal business expenses at the level of the

¹²⁰ See Joined Cases C-78/08 to C-80/08 *Paint Graphos* ECLI:EU:C:2009:417, paragraph 65.

¹²¹ “*The increase in value in the obligation under the ZORA will lead to a corresponding deduction*” for the operating company (see page 2 of the 2008 LNG ZORA tax ruling request and page 2 of the 2010 GSTM ZORA tax ruling request).

¹²² See Articles 6(1), 7, 14, 45, 109, 163, 167.

company making the payment.¹²³ Article 97(1)(3) and 97(1)(5) LIR provide that that income is subject to corporate income tax at the level of the company receiving interest income.¹²⁴

- (103) By contrast, Article 164(1) LIR establishes that a distribution of profits must be included in the taxable income of the taxpayer (regardless of their effective payment) and, therefore, cannot be deducted. Article 164(2) LIR requires the inclusion in the taxable income of payments related to instruments if they give their holders a right to a participation in the annual profit or in the liquidation proceeds (“*donnant droit à une participation au bénéfice annuel ou au bénéfice de liquidation*”). Finally, Article 164(3) LIR requires the taxpayer to include in its taxable income so-called “hidden profit distributions” (“*distribution cachée de bénéfices*”), which is understood as any situation in which a shareholder, a stockholder or an interested party receives either “*directly or indirectly*” advantages from a company or an association “*which he normally would not have received if he had not been a shareholder, a stockholder or an interested party*”.
- (104) In light of the intrinsic objective of those provisions, which is to tax the taxable profit of all undertakings subject to corporate income tax in Luxembourg, all corporate taxpayers should be considered to be in a comparable factual and legal situation for the purposes of Articles 109(1) and 164 LIR.
- 4.2.1.2. Derogation from the reference system giving rise to an advantage in the form of a reduction of the taxable base
- (105) Article 109(1) LIR provides that “debt interest” is deductible from a corporate taxpayer’s taxable base. However, since from a contractual, accounting or economic point of view the ZORAs do not seem to generate any interest payments or equivalent expenses, either at present or in the future, the Commission considers, at this stage, that the Luxembourg tax administration was wrong to consider the ZORA Accretions as deductible debt interest within the meaning of Article 109(1) LIR.
- (106) From a contractual point of view, both the contested tax rulings and the ZORA sample agreement state at several occasions that the ZORA is “interest-free”. Accordingly, no charge should be recorded in the accounts of GSTM or LNG Supply in respect of a payment obligation arising in the respective financial years under the ZORAs. Moreover, the ZORA sample agreement stipulates that the borrower shall repay the loan underlying the ZORA by issuing new shares.¹²⁵ An issuance of new shares does not, in principle, generate a tax deductible accounting expense. Rather, the issuance of new shares results in the dilution of existing shareholders. If no new funds are provided by investors in new shares, the level of a company’s equity remains the same, but that equity would be attributed to an increased number of shares. As such, there are no indications that the future repayment in the form of shares would generate a future charge for loss or obligation.
- (107) From an accounting point of view, first, LNG Supply’s 2014 annual accounts do not show any expense or charge for the ZORA Accretion which was paid out at the moment

¹²³ See footnotes 91 and 92.

¹²⁴ See footnote 93.

¹²⁵ See recital (31).

of the partial conversion. The amount of the capital decrease recorded in the accounts corresponds to the total of the ZORA Accretion amount repaid and the issue price repaid. The same accounting treatment was applied to both the repayment of the issue price and the repayment of the ZORA Accretion through issuance of shares.¹²⁶

- (108) Second, a potential future payment in the form of shares of any amount beyond the issue price is contingent on profits realised in future periods. Accordingly, if GSTM and LNG Supply do not make any profits or in fact record losses, any such future payments would be reduced or fully annulled. This is, in principle, not the case for interest payments or other forms of remuneration of a debt instrument. The yearly deductions for contingent future payments of the ZORA Accretion would seem even more unjustified if the accumulated ZORA Accretion at conversion is lower than the sum of the past deductions, because losses would have been recorded by GSTM and LNG Supply over the lifetime of the instrument. Recording losses cannot be excluded in the case of activities with a certain business risk and since GSTM and LNG Supply engage in activities which are associated with a certain business risk, namely financing activities and energy trading activities respectively, recording losses in this particular case cannot be ruled out. In fact, as the obligation to pay relates to the accumulated income net of cumulated losses at the moment of conversion, it seems that an obligation to pay cannot be triggered by a yearly profit recording.
- (109) Third, a debt instrument can be remunerated even if it does not bear a periodic interest through a reimbursement amount exceeding the amount of the loan initially provided. In this case, a yearly expense corresponding to the amortisation of the difference between the reimbursement price and the initial amount of the loan can be recorded in the yearly accounts. It would represent an implicit interest rate which is paid each year and would sum up over time to this difference. However, the deduction of such interest from the yearly taxable profit would require an effective future obligation to pay a higher amount at the maturity of the loan. Such an effective obligation does not seem to exist in the case of the ZORAs. In fact, the ZORA sample agreement states that “*the Lender grants the Borrower a Loan in an amount equal to the Principal Amount discounted to the Issue Price.*”¹²⁷ The issue price of the ZORAs is set in the sample agreement as an amount. However, the principal amount is not determined in the agreement in absolute amounts, but rather defined as the sum of the issue price and the ZORA Accretion, and thus could only be established in the future. Accordingly, even if the ZORAs were considered to carry an implicit interest rate,¹²⁸ that implicit interest rate would not however be certain, but solely based on the profitability of the company as a whole.
- (110) Luxembourg invokes Article 40 LIR in favour of allowing a deduction for the ZORA Accretion in the present case,¹²⁹ according to which the tax balance sheet must follow the commercial balance sheet and the expenses linked to the annual accretion in the

¹²⁶ See recital (71).

¹²⁷ See recital (28).

¹²⁸ This rate would be found to vary over the years independently of the ZORA financing transaction. In fact, the implicit interest rate of the GSTM ZORA for the period 2 May 2011 to end 2012 based on the ZORA Accretion for that period would amount to [5 – 10%]. If the amount recorded at end 2015 as 'accumulated Accretion' of EUR [600-650] million corresponds fully to the ZORA Accretion, then the implicit interest rate would be of [5 – 10%].

¹²⁹ See recital (81).

accounts are deductible.¹³⁰ At this stage, the Commission cannot follow that line of reasoning, since Article 40 LIR lays down the principle that the values to be considered in the tax balance sheet must be the same as those of the commercial balance sheet, unless the tax rules impose an adjustment.¹³¹ The fact that the net tax assessment does not need to follow the commercial balance sheet where the tax rules impose an adjustment is confirmed by the *Circulaire du directeur des contributions L.I.R. - n° 174/1* of 1 August 2013, “*Impôt minimum en matière de l’impôt sur le revenu des collectivités*”, according to which:

*“Conformément au principe de l’accrochement du bilan fiscal au bilan commercial de l’article 40 L.I.R., le total du bilan est en principe celui de la clôture du bilan commercial, à moins que ce bilan nécessite d’être retraité afin d’être compatible avec les principes et les règles d’évaluation valables en matière des impôts directs.”*¹³²

- (111) Therefore, and notwithstanding the accounting treatment of the ZORA Accretions (i.e. even if the ZORA Accretions had been rightfully recorded in the accounts of GSTM and LNG Supply), no taxable deduction should have been granted in the tax returns of GSTM and LNG Supply. The Commission does not understand how the rule according to which the tax treatment must follow the accounting treatment could justify a derogation from the general rule on tax deductible expenses laid down in Article 109(1) LIR, which only allows for the deduction of debt interest. As explained, although the ZORA Accretions are qualified as the “remuneration” of the loan in the ruling request,¹³³ the ZORAs do not correspond to a loan bearing a tax deductible remuneration.
- (112) In any event, the Commission does not understand why the accounting treatment of the ZORA Accretions would prescribe a deduction from an accounting perspective, as claimed by Luxembourg. Article 44 Lux GAAP provides that provisions for risks and charges need to cover losses or debt which are clearly identified as to their nature, but at the balance sheet date, they are either likely or certain but undefined as to their amount or as to the date of their occurrence.¹³⁴ However, the ZORAs do not seem to give rise to any future charges to cover losses or debt in the future, which are likely or certain but undefined as to their amount within the meaning of Article 44 Lux GAAP.

¹³⁰ Article 40 LIR: “*Lorsque les prescriptions régissant l’évaluation au point de vue fiscal n’exigent pas une évaluation à un montant déterminé, les valeurs à retenir au bilan fiscal doivent être celles du bilan commercial ou s’en rapprocher le plus possible dans le cadre des prescriptions prévues, suivant que les valeurs du bilan commercial répondent ou ne répondent pas aux mêmes prescriptions.*”

¹³¹ “*Lorsque les prescriptions régissant l’évaluation au point de vue fiscal n’exigent pas une évaluation à un montant déterminé.*”

¹³² Emphasis added by the Commission.

¹³³ 2010 GSTM ZORA tax ruling request, footnote 4 and 2008 LNG ZORA tax ruling request, footnote 3.

¹³⁴ Article 44 of *Loi comptable du 19 décembre 2002* reads as follows: “(1) *Les provisions pour risques et charges ont pour objet de couvrir des pertes ou dettes qui sont nettement circonscrites quant à leur nature mais, à la date de clôture du bilan, sont ou probables ou certaines mais indéterminées quant à leur montant ou quant à la date de leur survenance. (2) Est également autorisée la constitution de provisions ayant pour objet de couvrir des charges qui trouvent leur origine dans l’exercice ou en exercice antérieur et qui sont nettement circonscrites quant à leur nature mais qui, à la date de clôture du bilan, sont ou probables ou certaines mais indéterminées quant à leur montant ou quant à la date de leur survenance. (3) Les provisions pour risques et charges ne peuvent pas avoir pour objet de corriger les valeurs des éléments de l’actif.*”

- (113) In addition, the Commission has doubts whether qualifying the ZORA Accretions as an expense – when it is not established that those instruments would give rise to any future expenses at the moment of the issuance of new shares – can be considered compatible with the principle of prudence which, as Luxembourg confirms in its letter of 23 May 2016, is applicable under Luxembourg tax and accounting laws. In fact, the accounting principles take as a reference a prudent businessman who would not take decisions which are not in the interest of the company, such as decisions to decrease the profits of the company in the absence of any obligation to do so.
- (114) The Commission also observes that the ruling requests seek confirmation that “*in the unlikely event that the accounting treatment would not be totally in line with the obligations under the ZORA agreement, the resulting profit or loss reflected in the annual accounts will not affect the tax position set out above.*”¹³⁵ This seems to anticipate that the accounting treatment might not recognise the existence of an expense and requests that, in that case, the tax deductibility is maintained. It is not clear on which grounds that request is made, since it has been established that the deduction is in any event contrary to the wording of Article 109(1) LIR.
- (115) Finally, from an economic point of view, the qualification of the ZORA Accretions as “interest” does not seem to reflect economic reality. Indeed, it might be argued that in Luxembourg, under the “substance over form principle”,¹³⁶ economic considerations should override contractual arrangements. However, even an economic or substance perspective does not seem to explain why the ZORA Accretions should be considered debt interest under Article 109(1) LIR and, therefore, tax deductible for GSTM and LNG Supply.
- (116) First, the amounts of the ZORA Accretions which are deducted yearly do not take into account the factors which are typically considered by a credit institution when granting a loan, such as the creditworthiness of the borrower, the maturity and the subordination. Rather, the amounts deducted depend exclusively and entirely on the future profitability of GSTM and LNG Supply.
- (117) Second, the fact that CEF, which is the shareholder of GSTM, would receive the GSTM Shares at conversion through the Forward Contract¹³⁷ seems to suggest that the underlying arrangement is an equity contribution and not a debt instrument. As described in recital (20), CEF transferred assets and liabilities to GSTM against a promissory note. However, the reason a promissory note was issued to CEF at that point in time – instead of CEF directly receiving an equity stake in GSTM and not indirectly via EIL – is not explained in the ruling requests. In fact, the assets and liabilities transferred by CEF were previously held by two companies of the GDF Suez group (TCMS and EFTM)¹³⁸ and, in principle, the assets and liabilities of each company equalled the equity of each company. This seems to be confirmed by the fact that in the pro-forma balance sheet provided in the 2010 GSTM ZORA ruling request, the ZORA is associated with share capital rather than with liabilities.¹³⁹ The same considerations

¹³⁵ See, for example, recital (34).

¹³⁶ See for instance the judgment of the Court Administrative, 26 June 2008 (rôle n°24061 C).

¹³⁷ See recital (21).

¹³⁸ See recital (16).

¹³⁹ See Figure 2.

apply to the LNG ZORA, where LNG Supply, through the ZORA, receives financing from LNG Luxembourg to pay for the acquisition of the assets and liabilities received, instead of LNG Supply directly issuing shares to the entity transferring the assets and liabilities.

- (118) Third, the partial redemption of the LNG ZORA described in recital (70) proceeded at terms that were at odds with a debt treatment. In fact, USD [300-400] million of the issue price was redeemed in the partial conversion, as well as around USD [300-400] million of the ZORA Accretion.¹⁴⁰ There seems to be no reason for the conversion of the ZORA Accretion of an amount equivalent to the issue price redeemed. In fact, the ZORA Accretion which seems to have remained in the accounts of LNG Supply after the conversion would constitute less than 100 % of the outstanding amount of the issue price. There also appears to be no reason why, if the ZORAs were treated as debt, one portion of that debt should effectively carry a higher remuneration (100 %) than the non-converted portion of the same financing instrument.¹⁴¹
- (119) In light of the reasons given in recitals (106) to (118), the ZORA Accretions do not seem to reflect the remuneration for a loan and thus deductible debt interest for the purpose of Article 109(1) LIR. For those reasons, the Commission has doubts as to the recognition of tax deductible provisions in the yearly financial accounts and tax returns of GSTM and LNG Supply. Rather, the ZORA Accretions appear to represent an (expected) distribution of profits. In that regard, the acceptance by the Luxembourg tax administration of the deduction of the ZORA Accretions under Article 109(1) LIR appears to contravene Article 164 LIR.
- (120) Article 164(1) LIR provides that a distribution of profits must be included in the taxable base of the taxpayer (regardless of their effective payment) and, therefore, cannot be deducted. In addition, Article 164(2) LIR provides that payments related to instruments that give their holders the right to a participation in the annual profit or in the liquidation proceeds (“*donnant droit à une participation au bénéfice annuel ou au bénéfice de liquidation*”) should be included in the taxable base of the company issuing the instrument. Accordingly, since the ZORA Accretions appear to constitute “a participation in the annual profit” of GSTM and LNG Supply, the Commission has doubts as to whether the acceptance by the Luxembourg tax administration of the deduction under Article 109(1) LIR complies with Article 164(2) LIR.
- (121) In light of the foregoing considerations, the deduction of the ZORA Accretions from GSTM’s and LNG Supply’s taxable income should not have been accepted by the Luxembourg tax administration. Consequently, at this stage, the Commission considers that by endorsing an application of Article 109(1) LIR whereby the ZORA Accretions are considered to constitute deductible expenses for GSTM and LNG Supply within the meaning of that provision, the Luxembourg tax administration derogated from the general rules laid down in Articles 109(1) and 164(1) and (2) LIR that apply to all corporate taxpayers on the deductibility of interest payments and the non-deductibility

¹⁴⁰ USD [600-700] million minus USD [300-400] million, see recitals (70) and (71).

¹⁴¹ The capital gain which would have been reported by LNG Holding at conversion, but which would be exempted does not seem to correspond to the ZORA Accretion in respect of the redeemed issue price, see recital (71).

of profit distributions, respectively. As a result of that derogation, the Commission considers, at this stage, that Luxembourg conferred an economic advantage on GSTM, LNG Supply and the GDF Suez Group as a whole in the form of an unjustified reduction of their taxable base, which is selective in nature since it is not available to all other corporate taxpayers.

- (122) In any event, even if Article 164(1) and (2) LIR were not applicable to the ZORA Accretions, Article 164(3) LIR should have in principle required the inclusion of the ZORA Accretions in the taxable base of GSTM and LNG Supply, since that provision requires a corporate taxpayer to include the so-called “hidden profit distributions” (*“distribution cachée de bénéfices”*) in its taxable income. Such distributions are understood as any benefit which a shareholder, a stockholder or an interested party receives, either *“directly or indirectly”*, from a company or an association *“which he normally would not have received if he had not been a shareholder, a stockholder or an interested party”*. As explained in recital (77), compliance with Article 164(3) LIR requires assessing whether the remuneration of the ZORAs can be considered to be at arm’s length.
- (123) At this stage, the Commission doubts that any independent company negotiating under comparable circumstances at arm’s length would have granted a loan to GSTM in 2011 for an amount of more than EUR 1 billion. First, if Luxembourg were correct to consider the ZORA as constituting debt, which the Commission contests, GSTM’s equity at end 2011 amounted to only EUR 2.4 million and GSTM’s leverage would have stood at 0.02 % (EUR 2.4 million of equity compared to a balance sheet total of EUR 9 billion). The Commission doubts that such a level would have been accepted by an independent financial institution or any other third party loan provider in the position of EIL (i.e. as lender). Second, the granting of a loan to an entity which is as overleveraged as GSTM would have implied an extreme credit risk, as the financing entity would risk losing all or most of the funds provided in case of bankruptcy of the borrower, without having any possibility to control that risk. If these doubts are well-founded, excluding the ZORA Accretions from the taxable base of GSTM would have produced an outcome that departs from a reliable approximation of a market-based outcome, contrary to the arm’s length principle and Article 164(3) LIR.

4.2.2. Alternative lines of reasoning: Selective advantage resulting from a misapplication of Article 22bis(2), number 1, and Article 97(1)(3) or 97(1)(5) LIR and from a misapplication of the arm’s length principle

- (124) As explained in recitals (105) to (123), the Commission takes the preliminary view that the ZORA Accretions should not be considered a deductible expense for GSTM and LNG Supply under Article 109(1) LIR and therefore should not have been deducted from those companies’ taxable profit. However, if Luxembourg’s position were accepted that the ZORA Accretion is a deductible expense within the meaning of that provision, which the Commission contests, then the Commission considers, at this stage, that those expenses should have necessarily led to the taxation of the corresponding income, if realised, at the level of EIL and LNG Luxembourg, respectively, or at the level of the holding companies CEF and LNG Holding, respectively, under Article 97(1)(3) or 97(1)(5) LIR. The Commission further considers, at this stage, that if Luxembourg was right to accept the ZORA Accretion as a deductible expense, the method for determining the taxable profit of GSTM and LNG

Supply endorsed in the contested tax rulings results in an outcome that departs from a market-based outcome in line with the arm's length principle.

4.2.2.1. Selective advantage resulting from a misapplication of Article 22bis(2), number 1, LIR and Article 97(1)(3) or 97(1)(5) LIR

(a) *Determination of the reference system*

- (125) The contested tax rulings endorses an interpretation of Article 22bis(2), number 1, LIR according to which no corporate income tax is due from EIL and LNG Luxembourg upon conversion of the GSTM and LNG Supply Shares on the income corresponding to the ZORA Accretions.
- (126) However, Article 97(1) LIR defines various categories of investment income subject to corporate income tax, including interest on bonds and similar values including profit shares and repayment premiums (Article 97(1)(3)) and interest on debt-claims such as loans, funds, contributions, deposits, and current accounts (Article 97(1)(5)). To the extent the ZORA Accretions are considered debt interest for GSTM and LNG Supply within the meaning of Article 109(1) LIR, which the Commission contests, the corresponding income for EIL and LNG Luxembourg, respectively, should be considered taxable debt income within the meaning of Article 97(1)(3) or 97(1)(5) LIR.
- (127) Given that Article 22bis(2), number 1, LIR and Article 97(1) are general provisions of the LIR that apply to all corporate taxpayers subject to tax in Luxembourg, the Commission considers those provisions to constitute the appropriate reference system as regards the aforementioned interpretations in the contested tax rulings.

(b) *Derogation from the reference system giving rise to an advantage in the form of a reduction of the taxable base*

- (128) As explained in recital (126), to the extent the ZORA Accretions are considered debt interest for GSTM and LNG Supply within the meaning of Article 109(1) LIR, which the Commission contests, the corresponding income for EIL and LNG Luxembourg, respectively, should be considered taxable income within the meaning of Article 97(1)(3) or 97(1)(5) LIR.
- (129) That is not, however, the consequence of the contested tax rulings. Instead, the ZORA Accretions, once incorporated into the value of the shares held by EIL and LNG Luxembourg, are not taxed as income realised by those companies or by their holding companies LNG Holding and CEF. Rather, Luxembourg argues that Article 22bis(2), number 1, LIR provides for the tax neutrality of capital gains and that the contested tax rulings confirm the application of that provision to the conversion of the ZORA loan into shares of the borrowers.
- (130) While Article 22bis(2), number 1, LIR provides for the tax neutrality of capital gains arising from the conversion of a loan into the share capital of the debtor,¹⁴² the same

¹⁴² However, it is worth recalling that, according to the *Circulaire du directeur des contributions* L.I.R. N. 22BIS/1 of 27 November 2002, issued by the Luxembourg tax administration (hereinafter: the "Circulaire 22bis"), the purpose of article 22bis is not to permanently exempt capital gains, but merely postponing

provision expressly provides that that tax neutrality mechanism does not cover the interest accrued on the loan up until the date of the exchange:

“1. lors de la conversion d’un emprunt: l’attribution au créancier de titres représentatifs du capital social du débiteur. En cas de conversion d’un emprunt capitalisant convertible, l’intérêt capitalisé se rapportant à la période de l’exercice d’exploitation en cours précédant la conversion est imposable au moment de l’échange.”¹⁴³

- (131) Article 22bis(2) LIR thus differentiates extraordinary income arising from the conversion (the capital gain) – the taxation of which is postponed – from “ordinary” income, such as interest payments, which cannot escape immediate taxation. Indeed, the taxation of interest at the level of the beneficiary under Article 97(1)(3) or 97(1)(5) LIR seems to be required in case of interest deducted under Article 109(1) LIR. Any different interpretation would allow the non-taxation of such financial flows. Thus, it appears that the objective of the last indent of Article 22bis(2), number 1, LIR is to avoid that the payment of interest remains tax-exempt. Consequently, if the ZORA Accretions are to be assimilated to a deductible interest payment, which is what the contested tax rulings accept, then those Accretions should have been taxed at the level of the creditor (i.e. the recipient of the interest) once they accrue.¹⁴⁴
- (132) Consequently, the Commission cannot, at this stage, accept Luxembourg’s interpretation of Article 22bis(2) LIR to the present case. In the present case, the contested tax rulings go beyond the tax neutrality mechanism laid down under that provision, since they allow for the non-taxation of payments, both at the level of the ZORA issuer and at the level of the lender and, ultimately, at the level of their respective holding companies. This does not result from a mere application of the LIR, which appears to seek the effective taxation of sums such as the ZORA Accretions, since they should have been included in the taxable base of the borrower through the application of Article 164 LIR. However, if the ZORA Accretions were correctly considered to constitute interest-like payments, and therefore to be deductible by the borrower under Article 109(1) LIR, then the last indent of Article 22bis(2), number 1, LIR seems to require the taxation of that income, once realised, at the level of the lender.
- (133) In light of the inconsistent application of Article 109(1) and Article 22bis(2), number 1, LIR in the present case, the argument of Luxembourg at recital (86) that the latter provision is applicable to all taxpayers in Luxembourg without restriction and has commonly been applied for many years must also be rejected at this stage. This applies equally to the alleged application of the reverse alignment rule which, according to the tax ruling request,¹⁴⁵ would allow, in conjunction with Article 22bis LIR, to maintain

this taxation until the moment in which the shares will be transferred to a third party (Section 3.1.6, page 18).

¹⁴³ Emphasis added by the Commission.

¹⁴⁴ The Circulaire 22bis confirms this interpretation: “*La deuxième phrase du numéro 1 de l’alinéa 2 de l’article 22bis LIR précise que l’intérêt capitalisé, se rapportant à la période de l’exercice d’exploitation en cours, antérieure à la conversion d’un emprunt capitalisant convertible, est imposable au cours de l’année de l’échange*” (see section 3.1.3.1, page 8).

¹⁴⁵ See Recital (38).

the GSTM ZORA at the level of EIL at book value. According to the 2010 GSTM ZORA tax ruling request, that outcome is based on Articles 55(1)c.dd and 61(1)e of the law of 19 December 2002, under which “*it is possible to derogate from normally applicable accounting rules if such derogation is necessary in order to avoid adverse tax implications.*” The alleged provisions allow for an exceptional adjustment on the value of the assets in the balance sheet “*due to the application of the tax legislation*”, in which case, such correction must be indicated in the annex to the financial statements (“*Si les éléments de l'actif circulant font l'objet de corrections de valeur exceptionnelles pour la seule application de la législation fiscale, il y a lieu d'indiquer dans l'annexe le montant dûment motivé de ces corrections*”). Apart from the Commission’s preliminary reservations on whether Article 22bis LIR was correctly applied in the contested tax rulings, the Commission further doubts that the Luxembourg tax administration correctly applied the reversed alignment rule in the contested tax rulings. At the level of EIL, the ZORA Accretion should have been reflected by an exceptional value adjustment in form of an impairment loss “*due to the application of the tax legislation*”, and not, as stated in the request for the tax ruling, “*to avoid adverse tax implications*”. In addition, EIL should have indicated and motivated the adjustment in the Annex to the financial statements. The Commission therefore considers, at this stage, that the interpretation of the reversed alignment rule contained in the ruling requests is not in compliance with the alleged provisions of the law.

- (134) In conclusion, it appears that once the Luxembourg tax administration qualified the ZORA Accretions as deductible interest within the meaning of Article 109(1) LIR, it should have acted consistently by taxing the corresponding profits at the level of the recipient once they accrue under Article 97(1)(3) or 97(1)(5) LIR. By allowing EIL and LNG Luxembourg to extend the tax neutrality mechanism provided under Article 22bis(2), number 1, LIR to such profits, the Luxembourg tax administration appears to have departed from the explicit wording of that provision. In so doing, it endorsed a result in the contested tax rulings – the non-taxation of loan-related expenses – that appears to be contrary to the objectives of Article 22bis(2), number 1 LIR. That result appears, at this stage, to confer a selective advantage on EIL and LNG Luxembourg and, ultimately, their respective holding companies CEF and LNG Holding, respectively, for the purposes of Article 107(1) TFEU, by extending the tax neutrality mechanism provided under Article 22bis(2), number 1, LIR to the ZORA Accretions instead of taxing these sums in line with Luxembourg tax law. Consequently, the Commission considers, at this stage, that Luxembourg conferred an economic advantage on those companies and the GDF Suez Group as a whole in the form of an unjustified reduction of their taxable base, which is selective in nature since it is not available to all other corporate taxpayers.

4.2.2.2. Selective advantage resulting from the method for determining the taxable profit of GSTM and LNG Supply endorsed in the contested tax rulings

- (135) In addition to endorsing an interpretation of Article 109 LIR, whereby the ZORA Accretions are considered tax deductible expenses, and of Article 22bis(2), number 1, LIR, allowing for the non-taxation of the corresponding income to EIL and LNG, the contested tax rulings also endorse a method for determining the taxable profit of GSTM and LNG Supply. That method is based on a fixed margin, whereby the taxable profit of GSTM is determined as $[1/(50-100)\%]$ of its assets and the taxable profit of LNG Supply is determined as $[1/(50-100)\%]$ of its assets or $[0.0-0.50\%]$ of its turnover.

- (136) The Commission observes that the use of transfer pricing for determining the taxable base of GSTM and LNG Supply is only necessary where the ZORA Accretions can be considered a tax deductible expense for those companies under Article 109(1) LIR. This is because, in the absence of such deductible expenses, there is no related transaction between GSTM and EIL, on the one hand, and LNG Supply and LNG Luxembourg, on the other, that needs to be priced. As explained in recitals (105) to (123), the ZORAs seem to have the characteristics of an equity and not a debt instrument. Consequently, GSTM and EIL, on the one hand, and LNG Supply and LNG Luxembourg, on the other, are not considered to engage in a debt financing transaction through the ZORAs. There is therefore, in principle, no reason to determine the price for an intra-group debt financing transaction between associated group companies and therefore no reason to resort to transfer pricing in the context of the ZORA transactions, since no such group transaction in need of transfer pricing could be said to exist.
- (137) Since the Commission has provisionally concluded that the contested tax rulings derogate from Article 109(1) LIR by allowing the deduction of the ZORA Accretions at the level of GSTM and LNG Supply, there is no need for it to examine the transfer pricing method agreed in those rulings under the State aid rules. The reasoning that follows in recitals (138) to (150) is therefore only pertinent if the Commission's primary provisional conclusion that the ZORA Accretions should not have been treated as debt interest within the meaning of Article 109(1) LIR is wrong.

(a) Determination of the reference system

- (138) As regards the transfer pricing method endorsed in the contested tax rulings, the Commission considers the reference system to be the ordinary rules of taxation of corporate profit under the Luxembourg corporate tax system, which have as their intrinsic objective the taxation of profit of all companies subject to tax in Luxembourg.¹⁴⁶ As explained in Section 2.3, corporate income tax in Luxembourg is payable on profits realised minus tax-deductible expenses and losses.¹⁴⁷ From the perspective of the aforementioned rules, all companies having an income are considered to be in a similar factual and legal situation, since the objective of those rules is the taxation of profit subject to tax in Luxembourg. Consequently, all companies subject to tax in Luxembourg are in a comparable factual and legal situation as regards the ordinary rules of taxation of corporate profit in Luxembourg.
- (139) That reference system includes both non-integrated companies that derive their profit from arm's length transactions carried out on the market and integrated companies that (partly) derive their profit from transactions carried out within the same company or corporate group. The Luxembourg corporate tax system does not distinguish between companies which derive their profit from market transactions only, such as non-integrated standalone companies, and companies which derive their profit through internal dealings between companies of the same corporate group or between parts of the same company, such as integrated companies. Both types of companies are subject to corporate income tax on their taxable profit at the standard corporate tax rate under

¹⁴⁶ See Joined Cases C-78/08 to C-80/08 *Paint Graphos* ECLI:EU:C:2009:417, paragraph 50. See Decision of 21 October 2015 in case SA.38375, Luxembourg – *alleged aid to FFT*, under appeal, paragraph 194 et seq.

¹⁴⁷ See recital (72).

the ordinary rules of taxation of corporate profit in Luxembourg. Thus, non-integrated and integrated companies subject to tax in Luxembourg should be considered to be in a comparable factual and legal situation as regards those rules.

- (140) The fact that the taxable profit of non-integrated and integrated companies is determined in a different manner does not alter this conclusion. In the case of a non-integrated company that transacts on the market, that company's taxable profit can, in principle, be directly observed and calculated on the basis of such market transactions, as it is based on the difference between income and costs in a competitive market. Consequently, a non-integrated company will take its accounting profit as the starting point for determining the taxable base to which Luxembourg corporate income tax applies, since that profit is determined on the basis of prices dictated by the market for the inputs acquired and the products and services sold by the company. By contrast, the determination of the taxable profit of an integrated company requires the use of estimates. That is because an integrated company is able to set the prices and conditions of its dealings with its associated group companies independently of other market participants, which, in turn, determine the taxable profit of the companies taking part in those transactions.¹⁴⁸ This difference in determining the taxable profit of non-integrated and integrated companies is therefore due to the fact that the profits of integrated companies cannot be observed in a reliable way from the statutory accounts, in contrast to non-integrated companies or companies which do not engage in any form of internal dealings and where the accounts therefore reflect prices negotiated at arm's length on the market. However, this difference in determining the taxable profits of non-integrated companies and integrated companies is merely the means by which to achieve the ultimate goal of determining the taxable base of both types of companies in a manner that ensures that integrated companies are taxed on an equal footing to non-integrated companies under the ordinary rules of taxation of corporate profit.

(b) Derogation from the reference system giving rise to an advantage in the form of a reduction of the taxable base

- (141) According to settled case-law, any fiscal measure a Member State adopts, including a tax ruling endorsing a method for determining a corporate taxpayer's taxable base, must comply with the State aid rules, which bind the Member States and enjoy primacy over their national legislation¹⁴⁹. The Court of Justice has already held that a reduction in the taxable base that results from a tax measure that enables a taxpayer to employ transfer prices in intra-group transactions that do not resemble prices which would be charged in conditions of free competition between independent undertakings negotiating under comparable circumstances at arm's length confers a selective advantage on that taxpayer for the purposes of Article 107(1) TFEU¹⁵⁰. This is because that taxpayer's tax

¹⁴⁸ This is the case for the contested tax rulings which also concern the fixing of a profit margin for GSTM and LNG Supply on the basis of which their taxable profit is calculated for Luxembourg corporate income tax purposes.

¹⁴⁹ See Joined Cases C-182/03 and C-217/03, *Belgium and Forum 187 ASBL v. Commission*, EU:C:2006:416, paragraph 81; Joined Cases C-106/09 P and C-107/09 P *Commission v Government of Gibraltar and United Kingdom*, EU:C:2011:732; Case C-417/10 *3M Italia* EU:C:2012:184, paragraph 25, and Order in Case C-529/10 *Safilo* EU:C:2012:188, paragraph 18; See also Case T-538/11 *Belgium v. Commission* EU:T:2015:188, paragraph 66.

¹⁵⁰ See Joined Cases C-182/03 and C-217/03 *Belgium and Forum 187 ASBL v. Commission* EU:C:2006:416.

liability, determined under the ordinary rules of taxation of corporate profit, is reduced as compared to independent undertakings whose taxable profit reflects prices determined on the market negotiated at arm's length.

- (142) In its judgment on the Belgian tax regime for coordination centres¹⁵¹, the Court accepted that a tax measure which results in an integrated group company charging transfer prices that do not reflect those which would be charged in conditions of free competition, that is prices negotiated by independent undertakings negotiating under comparable circumstances at arm's length, confers a selective advantage on that company, in so far as it results in a reduction of its taxable base and thus its tax liability as determined under the ordinary rules of taxation of corporate profit. The principle that transactions between integrated group companies should be remunerated as if they were agreed to by non-integrated standalone companies negotiating under comparable circumstances at arm's length is referred to as the "arm's length principle". In its judgment on the Belgian tax regime for coordination centres, the Court of Justice endorsed the arm's length principle as the benchmark for establishing whether an integrated group company receives a selective advantage for the purposes of Article 107(1) TFEU as a result of a tax measure that determines its transfer pricing and thus its taxable base.
- (143) The purpose of the arm's length principle is to ensure that transactions between integrated group companies are treated for tax purposes by reference to the amount of profit that would have arisen if the same transactions had been carried out by non-integrated standalone companies. Otherwise, integrated group companies would benefit from a favourable treatment under the ordinary rules of taxation of corporate profit when it comes to the determination of their taxable base which is not available to non-integrated standalone companies, leading to unequal treatment between companies that are factually and legally in a similar situation in light of the objective of those rules, which is to tax the profits of all companies falling under its scope of taxation, since both companies' taxable profit is taxed at the same corporate income tax rate.
- (144) In the contested tax rulings, the Luxembourg tax administration endorses a method for determining the taxable base of GSTM and LNG Supply. In previous decisions concerning the taxation of finance companies in Luxembourg, the Commission held that rulings allowing taxpayers to use improper transfer pricing methods for calculating taxable profits may involve State aid.¹⁵² That is the case, *a fortiori*, when the ruling endorses a method to establish the tax base of finance companies on the basis of margins which are set "*without checking whether [they correspond] to the economic reality of the underlying services*".¹⁵³
- (145) As regards GSTM, the arm's length assessment of the margin agreed in the 2010 GSTM ZORA tax ruling request of $[1/(50-100)\%]$ of its assets, applied in its 2011 tax return¹⁵⁴,

¹⁵¹ See Joined Cases C-182/03 and C-217/03 *Belgium and Forum 187 ASBL v. Commission* EU:C:2006:416.

¹⁵² See Commission Decision of 16 October 2002 in case C 50/2001, *Luxembourg Finance Companies*, OJ L 153, 20.6.2003, p. 40 and Commission Decision of 21 October 2015 in case SA.38375, *Luxembourg – Alleged aid to FFT*, under appeal, p. 219 et seq.

¹⁵³ See Commission Decision of 16 October 2002 in case C 50/2001, *Luxembourg Finance Companies*, OJ L 153, 20.6.2003, p. 40, recitals 43 and 44.

¹⁵⁴ See Figure 4.

is not substantiated by the tax advisor in any manner and seems, at this stage, not to be justified by any economic analysis in the tax ruling request. As regards the margin applied by GSTM in later accounting periods, the Commission observes that in its tax returns of 2012, GSTM seems to have used the margin proposed in the ruling requests of 11 July 2012 and 11 November 2013 to determine its taxable base, even if Luxembourg claims that that margin has not been formally approved in a ruling.¹⁵⁵ However, even if those requests were not approved in a tax ruling, there is no indication that Luxembourg contested GSTM's 2012 tax declaration so that, to the extent its declared corporate income tax liability was determined on the basis of the margin proposed in those requests, the Luxembourg tax administration has effectively accepted the margin proposed by GSTM to determine its taxable base.

- (146) As regards LNG Supply, the formula retained in the LGN ZORA tax ruling to calculate the tax base of $[1/(50-100)\%]$ of assets or $[0.0-0.50\%]$ of turnover¹⁵⁶ is not based on any economic analysis or a transfer pricing report. The consideration presented in the ruling request to justify the margin is that it “*will not incur foreign exchange and/or bad debt risk on its trade*”. This seems *prima facie* difficult to reconcile with LNG Supply's activity, which consists, *inter alia*, in the purchase, sale and trading of gas and gas derivative products, including transactions with companies not belonging to the GDF Suez Group, and the investment in companies in the gas sector.¹⁵⁷
- (147) Finally, considering the very different activities of GSTM and LNG Supply (intra-group financing and LNG trading, respectively), it also appears doubtful that both of those companies should be taxed – at least initially - on the basis of a taxable profit resulting from an identical margin.¹⁵⁸
- (148) In conclusion, the Commission considers, at this stage, that the method for determining the taxable profit of GSTM and LNG Supply endorsed in the contested tax rulings does not result in a reliable approximation of a market-based outcome in line with the arm's length principle. Consequently, the Commission considers, at this stage, that Luxembourg conferred an economic advantage on GSTM, LNG Supply and the GDF Suez Group as a whole by way of the contested tax rulings, in the form of an unjustified reduction of their taxable base, which is selective in nature since it is not available to all other corporate taxpayers.

(c) *Subsidiary line of reasoning: Derogation from Article 164(3) LIR*

- (149) As explained in recitals (138) to (140), the Commission considers that the reference system as regards the method for determining the taxable profit of GSTM and LNG Supply in the contested tax rulings is the ordinary rules of taxation of corporate profit in Luxembourg.
- (150) However, even if the reference system were composed of Article 164(3) LIR only, the Commission considers, at this stage and for the reasons given in recitals (141) to (148),

¹⁵⁵ See Figure 5.

¹⁵⁶ See Figure 7.

¹⁵⁷ See Note 1 to the 2010 annual accounts.

¹⁵⁸ It is true that GSTM's Margin was subsequently changed as from 2012. However, Luxembourg has not provided the transfer pricing report on which such new Margin is based.

that the contested tax rulings confer an economic advantage on GSTM and LNG Supply in the form of a reduction of their taxable base and thus their corporate income tax liability, since they endorse a method for determining the taxable profit of those companies which departs from a reliable approximation of a market-based outcome in line with the arm's length principle. That advantage is selective in nature since it is not available to other integrated group companies who must determine their taxable profit in accordance with Article 164(3) LIR, being the provision of the LIR which establishes the arm's length principle under Luxembourg tax law.

4.2.3. The combined effect of the derogations from Articles 109(1) and 22bis(2), number 1, LIR

(151) For the reasons given in Sections 4.2.1 and 4.2.2, the Commission considers, at this stage, that the contested tax rulings derogate from Articles 109(1) and Article 164 LIR as well as from Article 97(1)(3) or Article 97(1)(5) and Article 22bis(2), number 1, LIR.

(152) The Commission further considers that the endorsement by the Luxembourg tax administration of the combined application of Article 109(1) LIR, allowing for the deductibility of the ZORA Accretions by GSTM and LNG Supply, and of Article 22bis(2), number 1, LIR, allowing for the non-taxation of the corresponding income to EIL and LNG Luxembourg, respectively, departs from the objective of the Luxembourg corporate tax system, which is, according to Article 163(1) LIR, to tax the profit of all companies subject to tax in Luxembourg. For that reason, the contested tax rulings ultimately provide a selective advantage to the holding companies CEF and LNG Holding as well as the GDF Suez Group as a whole.

(153) The objective of the LIR, as laid down in Article 163(1) LIR, is the taxation of profit, including the sums corresponding to the remuneration of instruments or services between companies of the same group. In the case of the ZORA Accretions, those sums cannot be deducted under Article 109(1) LIR and should therefore be taxed at the level of GSTM and LNG Supply. However, if in the alternative the ZORA Accretions should be assimilated to interest and not to profit distribution, which the Commission contests, then they should be subject to taxation at the level of EIL and LNG Luxembourg under Article 97(1)(3) or 97(1)(5) LIR and, contrary to the claim by Luxembourg, should not be exempted under Article 22bis(2), number 1, LIR.

(154) Since it is the same event (the existence of accumulated profits at the moment of conversion) that triggers the obligation of GSTM to "pay" EIL in the form of shares of GSTM and LNG Supply and generates income at the level of EIL and LNG Luxembourg, the same tax administration cannot simultaneously consider the obligation as triggered and the income as not being generated, without endorsing inconsistent results. Since the event is contingent, the tax administration could have agreed to a certain treatment in case the event is triggered or to another treatment if the event does not materialise to address this contingency. Instead, it appears that in accepting both alternatives on two sides of the very same transaction, the tax authority is acting in an inconsistent manner.

(155) Consequently, the deductibility of the ZORA Accretions under Article 109(1) LIR and the non-taxation of the corresponding income under Article 22bis(2), number 1, LIR appear to be mutually excluding alternatives. By combining both alternatives into the

contested tax rulings, the Luxembourg tax administration has endorsed the effective non-taxation of a sizeable portion of the profits generated by the GSTM and LNG Supply in Luxembourg.

- (156) That result appears, at this stage, to also constitute a misapplication of the participation exemption rules by LNG Holding and CEF, as laid down in Article 166 LIR. The objective of that provision is to eliminate the double taxation of shareholders. In the absence of rules on participation exemption – or an equivalent form of tax relief – shareholders would pay taxes on the amount of dividend income received, which would result in double taxation, since such dividend income would have already been taxed as part of the profits of the distributing company. However, in this case, the participation exemption appears to be relied upon by CEF and LNG Holding to exempt profits which have not been taxed at the level of GSTM and LNG Supply.
- (157) The Commission observes in this regard that Circulaire 22bis expressly states that the purpose of Article 22bis LIR is not to permanently exempt capital gains that, in the absence of such provision, would have been taxed in the hand of the lender, but merely to postpone taxation of those gains. The contested tax rulings appear to endorse such an outcome, however, being the permanent exemption of the ZORA Accretions from taxation.¹⁵⁹
- (158) In light of that outcome, the Commission considers, at this stage, that the deductibility of the ZORA Accretions derogate not only from the provisions of the LIR, but might also derogate from Articles 5 and 6 of the Luxembourg Tax Adaptation Law (*Steueranpassungsgesetz*, hereinafter “StAnpG”).¹⁶⁰ The Commission recalls that those provisions prohibit that taxes are evaded or mitigated by abuse of forms or constructions which are legal under civil law. According to Article 6 StAnpG,¹⁶¹ if the legal form or the construction surrounding a transaction is not appropriate in terms of its substance, tax should be assessed in accordance with the substance of the transaction, as if it had been concluded in the appropriate legal form. Additionally, Article 5 StAnpG provides

¹⁵⁹ In the same vein, Article 166(7) LIR provides that the income arising from a participation received in exchange of another participation in application of Article 22bis LIR do not fall within the scope of the participation exemption where the funds distributed out of the participation given in exchange had not been exempted if the exchange had not taken place (“*Les revenus provenant d’une participation reçue en échange d’une autre participation en application de l’article 22bis ne tombent pas sous le présent article, au cas où les distributions provenant de la participation donnée en échange n’auraient pas été exonérées, si l’échange n’avait pas eu lieu*”). Under a formalistic interpretation, it could be argued that this provision is not applicable to the ZORA structures, as they do not entail the exchange of participations, but rather the conversion of a loan into shares. However, its underlying rationale, which is to avoid an abusive use of the participation exemption regime, is also applicable in the present case. If, indeed, Luxembourg considers that ZORA is a debt instrument, the income of which could not be exempted under the participation exemption regime, then the income of the converted shares should not benefit from such exemption either.

¹⁶⁰ In relation with the application of these provisions, see Section 1 in Biewer, S and Höfer, “Tax treaties and tax avoidance: application of anti-avoidance provisions – Luxembourg”, *Cahiers de Droit Fiscal International*, International Fiscal Association (IFA), Volume 95A, Sdu Fiscal & Financiële Uitgevers Amersfoort 2010, p. 487.

¹⁶¹ Article 6 StAnpG provides: “*Durch Missbrauch von Formen und Gestaltungsmöglichkeiten des bürgerlichen Rechts kann die Steuerpflicht nicht umgangen oder gemindert werden. Liegt ein Missbrauch vor, so sind die Steuern so zu erheben, wie sie bei einer den wirtschaftlichen Vorgängen, Tatsachen und Verhältnissen angemessenen rechtlichen Gestaltung zu erheben wären.*”

that a simulated transaction must be disregarded for Luxembourg tax purposes if the tax authorities are aware of the fact that the involved parties do not really intend to live up to the simulated transaction, but are rather using this transaction with the sole purpose to hide the real transaction.¹⁶²

4.2.4. Conclusion on the existence of a selective advantage

- (159) For all the foregoing reasons, the Commission considers at this stage that the contested tax rulings confer an economic advantage on several GDF Suez Group companies in the form of a reduction of their taxable base and thus their corporate income tax liability in Luxembourg. An economic operator in a factual and legal position similar to the GDF Suez Group companies should have been taxed on the expenses related to an instrument such as the ZORAs, either at the level of the borrower, in accordance with Articles 109(1) and 164 LIR, or at the level of the lender which receives the corresponding income, in accordance with Article 97(1)(3) or 97(1)(5) LIR. Since the GDF Suez Group companies are not taxed on those expenses, that advantage is selective in nature since it is only available to those companies to the exclusion of all other corporate taxpayers in a comparable factual and legal situation, who are taxed in accordance with the provisions of the LIR.
- (160) That advantage, which is grounded on three separate lines of reasoning, results in a single advantage for the GDF Suez Group as a whole, since the advantage deriving from the untaxed income at the level of LNG Luxembourg/EIL in the first alternative line of reasoning would not exist if it the corresponding amounts had been taxed at the level at GSTM/LNG Supply under the primary line of reasoning. Therefore, the direct beneficiaries of the aid measure would either be GSTM and LNG Supply or, alternatively, EIL and LNG Luxembourg. In any event, LNG Holding, CEF and the GDF Suez Group as a whole are the ultimate beneficiaries of the reduction of the taxable base granted under the contested tax rulings, since the untaxed profits remain untaxed at the source (GSTM/LNG Supply), and will not be taxed at the level of the receiver (LNG Luxembourg/EIL) either, and can, as such, be repatriated to LNG Holding and CEF without any tax ever having been paid on those profits.
- (161) Therefore, at this stage the Commission takes the view that, by allowing for the deduction of the ZORA Accretions by GSTM and LNG Supply and, at the same time, the non-taxation of the corresponding income, once realised, at the level of LNG Luxembourg and EIL, the contested tax rulings and the acceptance by the Luxembourg tax administration of their implementation in the yearly tax returns of those companies give rise to a selective advantage for the purposes of Article 107(1) TFEU, which ultimately leads to a favourable treatment of CEF and LNG Holding and thus to the entire GDF Suez Group compared to economic operators that are factually and legally in a similar situation.

¹⁶² Article 5 StAnpG provides: “*Scheingeschäfte und andere Scheinhandlungen (zum Beispiel die Begründung oder die Beibehaltung eines Scheinwohnsitzes) sind für die Besteuerung ohne Bedeutung. Wird durch ein Scheingeschäft ein anderes Rechtsgeschäft verdeckt, so ist das verdeckte Rechtsgeschäft für die Besteuerung massgebend.*”

4.3. Justification by the nature or general scheme of the tax system

(162) Luxembourg has not provided any possible justification for the selective advantage resulting from the contested tax rulings. The Commission recalls that the burden of establishing such a justification lies with the Member State.

(163) In any event, at this stage, the Commission has not been able to identify any possible ground for justifying the preferential treatment that could be said to derive directly from the intrinsic, basic or guiding principles of the reference system or that is the result of inherent mechanisms necessary for the functioning and effectiveness of that system.¹⁶³

4.4. Conclusion on the existence of aid

(164) For all the foregoing reasons, the Commission considers, at this stage, that the contested tax rulings constitute State aid within the meaning of Article 107(1) TFEU.

4.5. Compatibility with the internal market

(165) State aid is deemed compatible with the internal market if it falls within any of the grounds listed in Article 107(2) TFEU¹⁶⁴ and it may be deemed compatible with the internal market if it is found by the Commission to fall within any of the grounds listed in Article 107(3) TFEU.¹⁶⁵ It is the Member State granting the aid which bears the burden of proving that State aid granted by it is compatible with the internal market pursuant to Article 107(2) or (3) TFEU.¹⁶⁶

(166) At this stage, the Commission has no indication that the treatment afforded to the GDF Suez Group companies and the GDF Suez Group as a whole as a result of the contested tax rulings could be considered compatible with the internal market. In particular, the Commission considers the contested tax rulings appear to result in a reduction of charges that should normally be borne by the entities concerned in the course of their business, and that the exemption of those charges should therefore be considered to constitute operating aid. According to Commission practice, such aid cannot be considered compatible with the internal market in that it does not facilitate the development of certain activities or of certain economic areas, nor are the incentives in question limited in time, digressive or proportionate to what is necessary to remedy to a specific economic handicap of the areas concerned.¹⁶⁷

¹⁶³ See Joined Cases C-78/08 to C-80/08 *Paint Graphos and others* ECLI:EU:C:2009:417, paragraph 69.

¹⁶⁴ The exceptions provided for in Article 107(2) of the Treaty concern: (a) aid of a social character granted to individual consumers; (b) aid to make good the damage caused by natural disasters or exceptional occurrences; and (c) aid granted to certain areas of the Federal Republic of Germany.

¹⁶⁵ The exceptions provided for in Article 107(3) of the Treaty concern: (a) aid to promote the development of certain areas; (b) aid for certain important projects of common European interest or to remedy a serious disturbance in the economy of the Member State; (c) aid to develop certain economic activities or areas; (d) aid to promote culture and heritage conservation; and (e) aid specified by a Council decision.

¹⁶⁶ Case T-68/03 *Olympiaki Aeroporoi Ypiresies v Commission* EU:T:2007:253 paragraph 34.

¹⁶⁷ Decision of 21 October 2015 in case SA.38375, Luxembourg – *alleged aid to FFT*, under appeal, paragraph 347 et seq.

DECISION

In the light of the foregoing considerations, the Commission's preliminary view is that the tax rulings issued by the Luxembourg tax administration on 9 February 2010 in favour of the GDF Suez Group company GDF Suez Treasury Management S.à.r.l. regarding the tax treatment of the GSTM ZORA, partly amended on 15 June 2012, and on 9 September 2008 in favour of the GDF Suez Group company LNG Supply S.A. regarding the tax treatment of the LNG ZORA constitute State aid within the meaning of Article 107(1) TFEU granted to those companies, as well as to Electrabel Invest Luxembourg SA, GDF Suez LNG (Luxembourg) S.à.r.l., Compagnie Européenne de Financement C.E.F. S.A., (currently, GDF SUEZ Invest International SA), GDF Suez LNG Holding S.à r.l., and to the GDF Suez Group as a whole. That aid is granted annually when those companies used those rulings to calculate their annual corporate income tax liability in Luxembourg. The Commission has doubts as to the compatibility of that State aid with the internal market. The Commission has therefore decided to initiate the procedure laid down in Article 108(2) TFEU with respect to these tax rulings.

The Commission requests Luxembourg to submit its comments on this Decision and to provide all such information as may help to assess the contested tax rulings, within one month of the date of receipt of this letter. In particular, the Commission wishes to receive the following information:

- The ruling requests of 11 July 2012 and 11 November 2013 submitted with reference to the GSTM ZORA, comprising the *APA request* and the *transfer pricing report* mentioned in the ruling request of 15 June 2012, and requested by the Commission in its letter of 1 April 2016, which were confirmed as such by Luxembourg in its submission of 23 May 2016, but not submitted to the Commission (see recital (8)).
- All other exchanges between the GDF Suez Group and the tax administration regarding the ruling requests of 11 July 2012 and 11 November 2013.
- The yearly amounts of the ZORA Accretions both for the GSTM ZORA and the LNG ZORA for each year in which the ZORAs have been in place.
- Copies of the ZORA contracts signed between GSTM and EIL, on the one hand, and between LNG Supply and LNG Luxembourg, on the other.
- Copies of the two Forward Contracts associated to both ZORA structures, described in recitals (20) and (56).
- Copies of the corporate income tax returns (*Déclaration pour l'impôt sur le revenu des collectivités et pour l'impôt commercial communal*), including their annexes, for the following entities and years:
 - GSTM and EIL, for years 2013, 2014 and 2015.
 - CEF, for years 2011 to 2015 (included).
 - LNG Supply, for years 2009, 2010, 2013, 2014 and 2015.
 - LNG Luxembourg, for years 2009, 2010, 2014 and 2015.

- LNG Holding, for years 2009 to 2015 (included).

The Commission further requests Luxembourg to forward a copy of this letter to the potential beneficiaries of the aid identified herein immediately.

The Commission wishes to remind Luxembourg that Article 108(3) TFEU has suspensory effect, and would draw its attention to Article 16 of Council Regulation (EU) No 2015/1589,¹⁶⁸ which provides that all unlawful aid may be recovered from the recipient of that aid.

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

If this letter 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 this letter. Your request specifying the relevant information should be sent by registered letter or fax to:

European Commission
Directorate-General for Competition
State aid registry
1049 Brussels
Belgium
Fax : +322 296 12 42

Yours faithfully,
For the Commission

Margrethe VESTAGER
Member of the Commission

¹⁶⁸ OJ L 2015 L 248/9.