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Apple v. European Commission: Losing the War on Corporate International Transfer Pricing

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Abstract: For the last several years, Apple has been defending tax strategies utilized in Ireland before the European Union (EU) General Court. The European Commission, using Article 107 of the Treaty on the Functioning of the European Union, argues that Ireland provides state aid

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to Apple regarding several tax rulings, and that Apple owes a substantial tax liability. Although Apple was able to secure a favorable ruling before the EU General Court, the European Commission has appealed the General Court's decision, and the final resolution to this case could be several years away.

The outcome of this case has the potential to cause changes to the corporate tax structure within the EU and could either strengthen or weaken the Commission's success in challenging the lack of arm's length principles in transfer pricing methods through state aid concerns. If the European Commission is unsuccessful in this case, there may be a push for the EU to harmonize the corporate tax system in the hopes of limiting corporations' ability to reduce tax liabilities by shifting profits between countries in the EU. Additionally, harmonizing the corporate tax laws would allow for the European Commission to challenge these transfer pricing methods under a different theory of law, and would not allow certain countries to offer very favorable corporate tax treatment. Further, there is the possibility the Internal Revenue Service (IRS) may look into similar transactions made by other countries based on the tax strategies used by Apple in Ireland.

I. INTRODUCTION

In *Apple Sales International & Apple Operations Europe v. European Commission*, the European Commission challenged Apple's tax activities in Ireland, arguing that many of Apple's transactions lacked arm's length principles.[1] However, the EU General Court held that although using arm's length principles in state aid cases is appropriate, the European Commission failed to apply the principles correctly and failed to provide supporting evidence for the Commission's position regarding Apple's branches' activities in Ireland.[2] This highly publicized *Apple* case stems from a recent line of EU cases in which the European Commission argued that a handful of member states are providing or have provided state aid and preferential treatment to certain corporations over others. If the Commission is successful in its argument that state aid has indeed been provided, then the member state providing said aid must attempt to collect the tax that the corporation would have otherwise had to pay. Considering the enormous financial stakes for Apple, it is no wonder this case is so closely watched. Currently, the *Apple* case is pending appeal. In that appeal, the Commission is expected to address the

1. Joined Cases T-778/16 & T-892/16, Apple Sales Int'l v. Eur. Comm'n, ECLI:EU:T:2020:338 ¶¶ 2, 23 (July 15, 2020).

2. *Id.* ¶¶ 247, 249, 295, 309, 351, 373.

shortcomings in its arguments and evidence noted by the EU General Court. The complexity of this pending appeal means the final outcome of the *Apple* case may still be several years away.

In Part II of this article, we provide an overview of tax structures within the EU and how tax policies work between individual member states and the EU. This Part will provide a brief introduction of the general principles of state aid and the provisions which the European Commission uses to establish a state aid case. Part III will provide a detailed look into the *Apple* case itself and examine the arguments set forth by both sides. Additionally, this Part will cover the general reasoning and holdings of the Court and provide an overview of the main issues which may be spotlighted on appeal. Part IV of this article will examine several of the other state aid cases and how these cases relate to the *Apple* case. These cases may also offer some insight into how the *Apple* case might conclude. Part V will discuss the application of this case's arguments and several policy arguments for and against the principles set forth in this case. This Part also covers some possible solutions in addressing concerns with the arm's length principle in corporate taxation in the EU. Part VI will examine the *Apple* case with respect to the United States, and how these decisions intersect between the EU and the United States. Finally, Part VII provides a summary of the key conclusions of this article.

II. OVERVIEW OF TAX STRUCTURES IN THE EU

A. Overall Tax Policy

To better understand the *Apple* case issue, a brief overview of the European Union authorities and tax policies is helpful, especially considering the different level of authorities within the EU as compared with the United States. However, the goal of this article is not to provide a comprehensive guide or background of corporate taxation within the EU. Rather, the purpose of this article is to provide an overview of the issues involved in the *Apple* case and to analyze how these issues may be viewed moving forward.

Generally, corporations in the EU are subject to corporate tax in the jurisdictions in which the corporations operate.[3] However, compliance for corporations within the EU can be complicated because corporate tax laws vary by EU country.[4] In the EU, corporate tax law and policy are shaped by the *OECD Model Convention with respect to Taxes on Income*

3. Stefano Micossi & Paola Parascandolo, *The Taxation of Multinational Enterprises in the European Union,* CTR. FOR EUR. POL'Y STUD. POL'Y BRIEF, 1, No. 203 (Feb. 4, 2010).

4. *Id.* at 1, 3.

and on Capital, which traces back to League of Nations policies from the 1920s.[5] In addition to differing corporate tax structures and rates[6] within the EU, "in all member states the tax base is reduced by a variety of tax incentives (provisions that provide special treatment to qualified investment projects not available to investment projects in general) primarily to promote entrepreneurship and stimulate innovation."[7]

The European Parliament has also set forth several objectives for taxation within the EU.[8] As mentioned above, each member state has the power to create tax policy within its own jurisdiction.[9] As long as the member state follows the overarching rules set forth by the EU, "each member state is free to choose the tax system it deems most appropriate."[10] According to the European Parliament, the objectives of EU tax policy are "the elimination of tax obstacles to cross-border economic activity, the fight against harmful tax competition and tax evasion, and the promotion of greater cooperation between tax administrations in ensuring control and combating fraud."[11]

B. State Aid Concerns

Though member states may create their own tax structures and policies, the European Commission enforces overarching rules which affect economic competition within the European Union.[12] Article 107 of the Treaty on the Functioning of the European Union (TFEU) provides:

Save as otherwise provided in the Treaties, any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favoring certain

5. Sijbren Cnossen, *Corporation Taxes in the European Union: Slowly Moving Toward Comprehensive Business Income Taxation?*, 25 INT'L TAX & PUB. FIN. 808, 810 (2017).

6. *Id.* at 816.

7. *Id.* at 815.

8. Dirk Verbeken, *Fact Sheets on the European Union: General Tax Policy*, EUR. PARL. 1-2 (last updated May 2021).

9. *Id.*

10. *Id.*

11. *Id.*

12. David G. Chamberlain, *Apple, State Aid, and Arm's Length: EU General Court's Failure of Imagination*, TAX NOTES TODAY FED., 1179, 1180 (Sept. 16, 2020), https://www.taxnotes.com/tax-notes-todayfederal/competition-and-state-aid/apple-state-aid-and-arms-length-eu-general-courts-failureimagination/2020/09/16/2cwm8. The European Commission is the executive wing of the European Union, and, among other things, is in charge of enforcing the European Union's laws. *European Commission*, EUR. UNION, https://www.europa.eu/european-union/about-eu/institutions-bodies/european-commission_en (last updated July 5, 2020).

undertakings or the production of certain goods shall, in so far as it affects trade between Member States, be incompatible with the internal market.[13]

The European Commission can decide to intervene when it deems a member state is providing a subsidy to a corporation to promote that corporation above others.[14] Although Article 107 does not directly discuss taxation, "the collection of tax that a local enterprise would otherwise owe is the economic equivalent of providing a subsidy," thus pulling certain tax provisions into the state aid realm.[15] In order for the European Commission to bring forth a state aid case, four elements must be present: (i) "an intervention using state resources; (ii) that is liable to affect trade between member states; (iii) confers an advantage on a particular beneficiary; and (iv) threatens to distort competition."[16]

III. THE APPLE CASE

A. Facts

To fully understand the different entities in this case, we shall provide a brief overview of the Apple hierarchy. Apple Inc. (the main entity when consumers think of Apple) owns the subsidiary Apple Operations International (AOI).[17] Apple Operations Europe (AOE) is a fully owned subsidiary of AOI, and AOE fully owns the subsidiary Apple Sales International (ASI).[18] Both AOE and ASI are incorporated in Ireland, however neither company is a tax resident in Ireland.[19]

Ireland and Apple Group have a history of entering into advanced tax rulings "concerning the chargeable profits of ASI and AEO in Ireland."[20] These contested tax rulings were from 1991 and 2007.[21] In the 2007 tax ruling, the Irish Government agreed with proposals set forth by

13. Consolidated Version of the Treaty on the Functioning of the European Union art. 107, May 9, 2008, 2008 O.J. (C 115) 47, 91 [hereinafter TFEU].

14. Chamberlain, *supra* note 12, at 1184.

15. *Id.*

16. *Id.*

17. Joined Cases T-778/16 & T-892/16, Apple Sales Int'l v. Eur. Comm'n, ECLI:EU:T:2020:338, ¶¶ 1–3 (July 15, 2020).

18. *Id.*

19. *Id.* ASI is responsible for "carrying out procurement, sales and distribution activities associated with the sale of Apple-branded products to related parties and third-party customers in the regions covering Europe, the Middle East, India, and Africa (EMEIA) and the Asia-Pacific region (APAC)." *Id.* ¶ 9. AOE "is responsible for the manufacture and assembly of a specialized range of computer products in Ireland . . .which it supplies to related parties for the EMEIA region." *Id.* ¶ 10.

20. Joined Cases T-778/16 & T-892/16, Apple Sales Int'l v. Eur. Comm'n, ECLI:EU:T:2020:338, ¶ 11 (July 15, 2020).

21. *Id.*

Apple, setting out, in part, for ASI's "chargeable profit to be allocated to that branch corresponding[sic] to [*confidential*] of its operating costs, excluding costs such as sums invoiced from affiliated companies within the Apple Group and material costs."[22] In regards to AOE, the tax ruling set forth:

> the chargeable profit was to correspond to . . . an amount corresponding to [*confidential*] of the branch's operating costs, excluding costs such as the sums invoiced from affiliated companies within the Apple Group and material costs, and, on the other, an amount corresponding to the IP return for the manufacturing process technology developed by that branch . . . .[23]

The Commission contested these tax rulings, arguing Ireland had provided an advantage to Apple through these tax rulings, and because Ireland lost tax revenue, "Ireland had renounced tax revenue, which had given rise to a loss of State resources."[24]

B. Arguments From Apple and Ireland

Many of the arguments against the European Commission were set forth by Apple and Ireland. The main goal of Apple and Ireland was to have the Commissions contested decision, in which the Commission argued that the tax rulings had provided state aid under Article 107(1) TFEU, set aside.[25] In arguing to set aside the contested decision, Apple and Ireland reasoned that, "the Commission carried out a joint assessment of the concept of an advantage and the concept of selectivity."[26] Further, they argued that the Commission (1) applied the incorrect reference framework under Irish law; (2) misapplied arm's length principles and the OECD guidelines; (3) incorrectly assessed the activities of the Apple subsidiaries; and (4) "contest[ed] the assessments relating to the selective nature of the contested tax rulings."[27]

Before ultimately arguing that state aid had not occurred in this case, Apple and Ireland first argued that the Commission should not be interfering with the tax rulings of individual member states.[28] They argued that the contested decision violated the "fundamental constitutional principles of the EU legal order" which governs the "division of

22. *Id.* ¶ 18.
23. *Id.* ¶ 19.
24. *Id.* ¶ 27.
25. *Id.* ¶ 88.
26. Joined Cases T-778/16 & T-892/16, Apple Sales Int'l v. Eur. Comm'n, ECLI:EU:T:2020:338, ¶ 91 (July 15, 2020).
27. *Id.*
28. *Id.* ¶ 103.

competences" between the EU and Member States.[29] Under this argument, Apple and Ireland argued that "the field of direct taxation falls within the competence of the Member States."[30]

Further, Apple and Ireland argued the Commission used the incorrect reference framework in considering relevant Irish tax law, and erred in applying the correct arm's length principles.[31] In addressing the correct reference framework, Apple and Ireland "contest that definition of the reference framework and claim, in essence, that the relevant reference framework in the present instance is section 25 of the TCA 97, a separate charging provision applicable specifically to non-resident companies which are not in a situation comparable to that of resident companies."[32]

Additionally, Apple and Ireland argued for the application of certain other applicable Irish tax provisions regarding the normal taxation of profits of corporations by Ireland.[33] Apple and Ireland contended: (1) "the Irish tax authorities had not required all of ASI and AOE's profits to be allocated to their Irish branches;" (2) that Article 107(1) TFEU provides for an arm's length principle, which is not applicable in Ireland; and (3) the OECD approach to the arm's length principle does arise under Irish law and should not apply in Ireland, and even if it could apply, "the Commission was wrong to conclude, on the basis of that approach, that the profits relating to the Apple Group IP licenses held by ASI and AOE should have been allocated to their Irish branches."[34]

To further support their arguments concerning the normal taxation of profits in Ireland, Apple and Ireland brought forth an expert in Irish law to provide the Court with an overview of the relevant laws at issue in this case.[35] In the expert's opinion, "when determining the chargeable profits of non-resident companies" conducting business in Ireland through branches, "the relevant analysis for the application of section 25 of the TCA 97 must cover the actual activities of those Irish branches and the value of the activities actually carried out by the branches themselves."[36] Apple and Ireland further reasoned that the arm's length principle as set forth by the European Commission was not a part of Irish law and thus Ireland should not have to apply the principle arising under

29. *Id.*
30. *Id.*
31. *Id.* ¶ 129.
32. Joined Cases T-778/16 & T-892/16, Apple Sales Int'l v. Eur. Comm'n, ECLI:EU:T:2020:338, ¶ 143 (July 15, 2020).
33. *Id.* ¶¶ 169–71.
34. *Id.*
35. *Id.* ¶ 179.
36. *Id.*

Article 107(1) TFEU.[37] Additionally, Apple and Ireland put forth that "the Commission misapplied that approach inasmuch as it failed to examine the functions actually performed within the Irish branches of ASI and AOE."[38]

C. European Commission's Arguments

In August of 2016, the European Commission set forth its decision regarding its investigation of the tax rulings between Apple and Ireland.[39] It is this decision that is being contested before the General Court of the European Union.[40] Within the contested decision, the Commission set forth some of its arguments supporting its claims that Ireland had conferred tax advantages to Apple which were not made available to other corporations, and that the agreed-upon transfer pricing methodologies violated arm's length principles.[41]

In order to show Apple received a selective advantage in this case, the European Commission used a three part analysis developed from case law. Specifically, the Commission: (1) "identified the reference framework and provided grounds for applying the arm's length principle in that case;" (2) "examined whether there was a selective advantage arising from a derogation from the reference framework;" and (3) "stated that neither Ireland nor Apple Inc. had put forward arguments to justify that selective advantage."[42] For the reference framework used, the Commission looked to Irish tax rules in regards to corporations and also considered "integrated companies" and "stand-alone companies" as "a comparable factual and legal situation."[43] In state aid cases, the Commission argues that under Article 107(1) TFEU, profit allocations must follow arm's length principles even if the member state had not adopted arm's length principles into its own tax rules.[44]

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37. *Id.* ¶ 189.

38. Joined Cases T-778/16 & T-892/16, Apple Sales Int'l v. Eur. Comm'n, ECLI:EU:T:2020:338, ¶ 231 (July 15, 2020).

39. *Id.* ¶ 26.

40. *Id.* ¶¶ 26–27.

41. *Id.* ¶¶ 32–47.

42. *Id.* ¶ 32 (The reference system in State aid cases refers to "the baseline against which the illegal subsidy (or the 'tax advantage' in EU parlance) can be measured."); *see also* Stephen Daly & Ruth Mason, *State Aid: The General Court Decision in Apple*, 99 TAX NOTES INT'L 1317 (2020), https://www.taxnotes.com/tax-notes-federal/corporate-taxation/state-aid-general-court-decision-apple/2020/09/07/2cw9y (explaining that the reference system in state aid cases refers to "the baseline against which the illegal subsidy (or the 'tax advantage' in EU parlance) can be measured").

43. Joined Cases T-778/16 & T-892/16, Apple Sales Int'l v. Eur. Comm'n, ECLI:EU:T:2020:338, ¶ 33 (July 15, 2020).

44. *Id.* ¶ 34 (According to the Commission, the reasoning behind the arm's length principle is described as, "principle was intended to ensure that intra-group transactions be treated, for tax

One of the main arguments set forth by the Commission in its contested decision was "that the Apple Group IP licenses held by ASI and AOE had to be allocated outside Ireland had led to ASI and AOE's annual chargeable profits in Ireland departing from a reliable approximation of a market-based outcome in line with the arm's length principle."[45] Additionally, the Commission argued that Ireland incorrectly allocated assets and activities to the ASI and AOE head offices, as neither of these offices had employees nor a physical presence.[46] Instead of allocating the profits resulting from Apple Group's IP licenses to the head offices, the Commission argued "those profits should have been allocated to ASI and AOE's branches, which alone would have been in a position effectively to perform functions related to the Apple Group's IP that were crucial to ASI and AOE's trading activity."[47] Further, the Commission stated that the profit allocation methods set forth in the tax rulings were not based on realistic market outcomes, and thus did not follow arm's length principles.[48] As a result, the Commission concluded by finding Ireland needed to recover the taxes that Apple should have paid if the proper tax rules been followed.[49]

D. Reasoning

The General Court issued a lengthy opinion in which it addressed the specifics regarding Apple's activities in Ireland, the mechanics of the transfer pricing, and the methodology used to determine if arm's length principles were followed.[50] At the outset of the opinion, the Court recognized the European Commission's responsibility to prove the existence of state aid and demonstrate "the existence of a selective advantage resulting from the issuing of the contested tax rulings."[51] In addressing Apple and Ireland's arguments on the division of competences, the Court noted that, while member states are responsible for creating their own tax policies, they must exercise that responsibility in a way that conforms and

purposes, in the same way as those carried out between non-integrated stand-alone companies, so as to avoid unequal treatment of companies in a similar factual and legal situation, having regard to the objective of such a system, which was to tax the profits of all companies falling within its fiscal jurisdiction.").

45. *Id.* ¶ 37.

46. *Id.* ¶ 39.

47. *Id.*

48. *Id.* ¶ 41.

49. Joined Cases T-778/16 & T-892/16, Apple Sales Int'l v. Eur. Comm'n, ECLI:EU:T:2020:338, ¶ 45 (July 15, 2020).

50. *See generally id.*

51. *Id.* ¶ 101.

complies with EU law.[52] Further, the Court stated that "the Commission may classify a tax measure as State aid so long as the conditions for such a classification are satisfied."[53] The Court found that the issue in this case, if successfully set forth by the European Commission, could constitute state aid under Article 107(1) TFEU.[54] The Court noted that if a member state provides favorable tax treatment for some corporations but declines to extend the same treatment to other similarly situated corporations, this disparate treatment can constitute state aid because it elevates the financial situation of one corporation over another.[55]

In determining whether an advantage exists, the Court noted "the very existence of an advantage may be established only when compared with 'normal' taxation."[56] Additionally, in determining whether an advantage exists, the Court must compare the position of the corporation receiving the "preferential" tax treatment with and without the tax policy in question.[57] Regarding Apple and Ireland's arguments concerning the Commission's competence to analyze whether state aid occurred, the Court said, "it is necessary to set aside as ineffective the complaints relied on by Ireland and by ASI and AOE relating to the Commission having exceeded its competences by considering ASI and AOE to be stateless for tax residency purposes."[58] In discussing the proper reference framework, the Court noted "the purpose of the measures at issue and the legal framework of which they form part must be taken into consideration when determining the reference framework."[59] Ultimately, after looking at relevant Irish law and the reference framework arguments set forth by both sides, the Court held that "the Commission did not err when it concluded that the reference framework in the present instance was the ordinary rules of taxation of corporate profit in Ireland, the intrinsic objective of which was the taxation of profit of all companies subject to tax in that Member State . . . ."[60] The Court also addressed Irish tax law under several of the different arguments in this case, including trying to discern the normal taxation of corporate profits in Ireland.[61] The Court noted that for

52. *Id.* ¶ 105.
53. *Id.* ¶ 106.
54. *Id.* ¶ 108.
55. Joined Cases T-778/16 & T-892/16, Apple Sales Int'l v. Eur. Comm'n, ECLI:EU:T:2020:338, ¶ 108 (July 15, 2020).
56. *Id.* ¶ 110.
57. *Id.* ¶ 111.
58. *Id.* ¶ 122.
59. *Id.* ¶ 150.
60. *Id.* ¶¶ 152–63.
61. Joined Cases T-778/16 & T-892/16, Apple Sales Int'l v. Eur. Comm'n, ECLI:EU:T:2020:338, ¶ 175 (July 15, 2020).

non-resident corporations operating in Ireland through a branch, "only the profits derived from trade directly or indirectly attributable to that Irish branch, on the one hand, and all income from property or rights used by, or held by or for, the branch, on the other, are taxable."[62]

Through careful analysis of relevant Irish case law and after hearing arguments set forth by Apple and Ireland's expert, the Court found that, under the normal taxation of profits under Irish law, "the profits derived from property that is controlled by a non-resident company cannot be regarded as such as being profits attributable to the Irish branch of that company even if that property has been made available to that branch."[63] Further, the Court noted, "that property belonging to a company that is not resident in Ireland and controlled by the executives of that company, who are also not resident in Ireland, cannot be allocated to that company's Irish branch, even if that property is made available to that branch."[64] From this reading of Irish law, the Court found that "the question that is relevant when determining the profits of the branch is whether the Irish branch has control of that property."[65] The property of a non-resident corporation "cannot be allocated to the Irish branch" unless the European Commission can prove "that property is actually controlled by that branch."[66]

In applying the relevant Irish law to the facts of this case, the Court found that the European Commission's "exclusion" approach was inconsistent under Irish law.[67] Further, the Court found "the Commission did not attempt to show that the Irish branches of ASI and AOE had in fact controlled the Apple Group's IP licenses when it concluded that the Irish tax authorities should have allocated Apple Group's IP licensed to those branches;" and under relevant Irish law "all of ASI and AOE's trading income should have been regarded as arising from the activities of those branches."[68] Thus, the Commission incorrectly assessed Irish law in determining the taxation of non-resident corporations which operate a branch in Ireland.[69]

In regards to the arm's length principle application in this case, the Court specifically noted that the Commission did not directly apply the

62. *Id.*
63. *Id.* ¶ 180.
64. *Id.* ¶ 181.
65. *Id.* ¶ 182.
66. *Id.* ¶ 184.
67. Joined Cases T-778/16 & T-892/16, Apple Sales Int'l v. Eur. Comm'n, ECLI:EU:T:2020:338, ¶ 186 (July 15, 2020).
68. *Id.*
69. *Id.* ¶ 187.

guidance provided by the OECD.[70] Additionally, the Court stated the Commission was correct in asserting that arm's length principles serve as a "benchmark" in determining profit for a corporation using transfer pricing methods and for a corporation whose profits were earned at arm's length in the marketplace.[71] Thus, the Court found that using arm's length principles as a tool in determining the correct level of profit in State aid cases is appropriate.[72]

However, just because the arm's length principle is a proper tool to be used does not mean that these principles were applied correctly.[73] The Court found it was appropriate to look to OECD guidance in applying arm's length principles.[74] Although it was appropriate to rely on the OECD guidance, the Commission deviated from the OECD guidance when applying arm's length principles in this case.[75] The Court found:

It is true that the analysis in that first step cannot be carried out in an abstract manner that ignores the activities and functions performed within the company as a whole. However, the fact that the Authorised OECD Approach requires an analysis of the functions actually performed within the permanent establishment is at odds with the approach adopted by the Commission consisting, first, in identifying the functions performed by the company as a whole without conducting a more detailed analysis of the functions actually performed by the branches and, second, in presuming that the functions had been performed by the permanent establishment when those functions could not be allocated to the head office of the company itself.[76]

Thus, the Court sided with Apple and Ireland regarding the application of the arm's length standard under the OECD approach.[77] The Court concluded that "it is appropriate to conclude that the Commission's primary line of reasoning was based on erroneous assessments of normal taxation under the Irish tax law applicable in the present instance."[78]

Next, the Court looked at the functions performed by the Irish branches.[79] The Court ultimately found that the European Commission

70. *Id.* ¶ 196.
71. *Id.* ¶ 215.
72. *Id.* ¶ 225.
73. Joined Cases T-778/16 & T-892/16, Apple Sales Int'l v. Eur. Comm'n, ECLI:EU:T:2020:338, ¶ 229 (July 15, 2020).
74. *Id.* ¶ 240.
75. *Id.* ¶ 242.
76. *Id.*
77. *Id.* ¶ 245.
78. *Id.* ¶ 249.
79. Joined Cases T-778/16 & T-892/16, Apple Sales Int'l v. Eur. Comm'n, ECLI:EU:T:2020:338, ¶¶ 251–311 (July 15, 2020).

did not make a showing of the actual functions performed by the Irish branches as well as "the strategic decisions taken and implemented outside of those branches . . . ."[80] Thus, the Commission was not successful in arguing "the Apple Group's IP licenses should have been allocated to those Irish branches when determining the annual chargeable profits of ASI and AOE in Ireland."[81] Further, the Court later found "the Commission did not put forward evidence to prove that the choice of ASI and AOE's Irish branches as tested parties had led to a reduction in the chargeable profit of those companies."[82] The Court ultimately sided with Apple and Ireland, finding that the Commission failed to show that Ireland conferred an advantage to Apple through the contested tax rulings under Article 107(1) TFEU.[83]

E. Appeal

Given the complicated circumstances involved in the *Apple* case, as well as the amount

of tax at stake, the European Commission has decided to appeal the decision of the EU General Court.[84] On appeal, the European Commission is focusing on the General Court's reasoning regarding the separate entity approach and the arm's length principle set forth in the case.[85] Because the European Commission is appealing the decision, a final resolution to this case may still be several years away.[86]

Commentators on the *Apple* case have set forth several of the key principles that may be the focus of the appeal.[87] The General Court noted that the European Commission failed to carry its burden of proof "on the issue of profit attribution to the Irish branches of Apple Sales International (ASI) and Apple Operations Europe (AOE) . . . ."[88] Despite the Commission not carrying its burden of proof on this issue, the best way forward may be to focus on the tax policy at issue concerning the arm's

80. *Id.* ¶ 310.
81. *Id.*
82. *Id.* ¶ 333.
83. *Id.* ¶ 505.
84. Leonie Carter, *Commission Lays Out Arguments in Appeal of Apple Tax Case*, POLITICO (Feb. 1, 2021, 2:28 PM).
85. *Id.*
86. *Id.*
87. *See* Robert Goulder, *Why the European Commission Must Appeal the* Apple *Decision*, 99 TAX NOTES INT'L 973 (Aug. 17, 2020), https://www.taxnotes.com/featured-analysis/why-european-commission-must-appeal-apple-decision/2020/08/14/2ctv8; *see also* Chamberlain, *supra* note 12.
88. Goulder, *supra* note 87, at 973.

length standard.[89] In deciding the *Apple* case, the General Court found that the OECD approach to finding the arm's length standard was appropriate over the Commission's novel exclusionary model of profit attribution.[90] Under the Commission's approach, "The exclusionary model—to the extent that one can understand it—takes stateless income off the table by ensuring that profits are attributed somewhere."[91] However, though the General Court decided to follow the OECD model, it did not fully explain the reasoning for selecting one method over the other.[92] Thus, the Commission may once again argue the exclusionary approach should apply over the OECD approach in this case.[93] Additionally, the General Court turned to Irish law for a portion of the decision which the Commission may be able to differentiate on appeal.[94]

From a policy perspective, although the Court of Justice of the European Union (CJEU) may overturn the decision on appeal, the transfer pricing landscape in the EU has shifted since the beginning of the *Apple* case litigation.[95] Irish law has since changed, and one of the tax loopholes utilized by Apple is now closed.[96] Ireland also passed new transfer pricing laws.[97] Additionally, corporations are more hesitant to participate in such aggressive tax planning because of the widespread repercussions to brand image.[98] One proposed solution for the CJEU is to apply the Commission's arguments moving forward and rule that "member states are only under an obligation to apply international best practices after they have been formally articulated."[99]

89. *Id.*
90. *Id.*
91. *Id.*
92. *Id.*
93. Robert Goulder, *Why the European Commission Must Appeal the* Apple *Decision*, 99 TAX NOTES INT'L 973 (Aug. 17, 2020), https://www.taxnotes.com/featured-analysis/why-european-commission-must-appeal-apple-decision/2020/08/14/2ctv8.
94. *Id.*
95. Chamberlain, *supra* note 12, at 1180.
96. *Id.* at 1189.
97. *Id.* at 1180.
98. Mark Beasley et al., *Make Tax Planning a Part of Your Company's Risk Management Strategy*, HARV. BUS. REV. (Nov. 13, 2020), https://www.hbr.org/2020/11/make-tax-planning-a-part-of-your-companys-risk-management-strategy.
99. Chamberlain, *supra* note 12, at 1189.

IV. SIMILAR CASES

A. The Fiat Case

In *Fiat*, Fiat Chrysler Finance Europe sought a ruling from the Luxembourg tax authorities stating that intra-group financing activities within the company followed arm's length principles.[100] However, the Commission found that this tax ruling conferred a selective advantage under Article 107(1) of the TFEU and violated arm's length principles.[101] In this case, the General Court confirmed the reasoning set forth by the Commission and found that a selective advantage existed.[102]

B. The Starbucks Case

In the Starbucks case before the EU's General Court, the arm's length principle was also at issue.[103] The European Commission challenged a Dutch tax ruling reducing Starbucks' tax liability.[104] In this case, Starbucks Manufacturing, the Starbucks entity responsible for the sale and distribution of products in Europe, Africa, and the Middle East, received a favorable tax ruling from the Netherlands.[105] However, the European Commission challenged the tax rulings because the agreed-upon royalty rate for transfer pricing considerations was excessive.[106] Thus, because "the transfer methodology determining such excessive remuneration was covered by a tax ruling, a selective advantage in the meaning of State aid rules was granted."[107]

100. Joined Cases T-755/15 & T-759/15, Grand Duchy of Luxembourg v. Comm'n, ECLI:EU:T:2019:670, ¶ 1 (Sept. 24, 2019).

101. *Id.*

102. *The Fiat & Starbucks State Aid Cases: The Arm's Length Principle, a New Tool to Challenge (But Also Defend) Transfer Pricing Rulings in Illegal State Aid Investigations?*, EVERSHEDS SUTHERLAND (Oct. 14, 2019), https://www.eversheds-sutherland.com/global/en/what/articles/index.page?ArticleID=en/State_aid/Fiat-Starbucks-general-court-judgements [hereinafter *Fiat & Starbucks*].

103. *Id.*

104. Sara White, *Starbucks Wins €30m Case Over Disputed Tax Bill*, ACCOUNTANCY DAILY (Sept. 24, 2019), https://www.accountancydaily.co/starbucks-wins-eu30m-case-over-disputed-dutch-tax-bill.

105. *Fiat & Starbucks*, *supra* note 102.

106. *Id.*

107. *Id.*

V. POSSIBLE RESPONSES TO THE APPLE CASE

One possible EU response to the *Apple* case would be to harmonize corporate tax laws and policies among member states.[108] If corporate tax laws were consistent between member states, it would disincentivize corporations from shifting profits from one member state to another and reduce the need for the Commission to challenge tax rulings as state aid.[109] Under the EU's current tax environment, "[t]he combination of the principle of legal certainty, in which a tax is only due when there is a clear legal prescription, and the member states' freedom to determine their national tax rates inevitably results in profit shifts by multinationals founded on both tax motives and sound economic considerations."[110] However, there has been push back in the past with similar proposals because of arguments that the corporate tax revenues would be split among member states, and member states showed reluctance to give up the ability to create their own tax laws and policies.[111] On the other hand, a unified tax structure would serve as a better means to combat tax abuse in the EU because "state aid is an instrument for maintaining free and fair competition, not an instrument to fight tax shifting within the EU."[112]

After losing several significant state aid cases, another response by the Commission would be to adapt its state aid arguments and approach in order to have a better chance of challenging taxpayer conduct.[113] In the *Apple* case and the more recent *Amazon* case, the Commission has argued it has the power under Article 107 to challenge issues of direct taxation, which some commentators note "arguably was never intended [to include] obedience to an idealized version of the arm's length standard."[114] Other commentators have explained the Commission may be using the wrong methodology to challenge taxpayers in these state aid cases.[115] Instead of using transfer pricing to challenge local tax rates used to

108. Frans Vanistendael, *Apple: Why the EU Needs a Common Corporate Income Tax*, 99 TAX NOTES INT'L 451 (July 27, 2020), https://www.taxnotes.com/tax-notes-international/competition-and-state-aid/apple-why-eu-needs-common-corporate-income-tax/2020/07/27/2crc2.

109. *See id.*

110. *Id.*

111. *See id.*

112. *Id.*

113. Robert Goulder, *Amazon and the State Aid Doctrine: Unchecked Mission Creep*, 102 TAX NOTES INT'L 1571 (June 14, 2021), https://www.taxnotes.com/tax-notes-international/litigation-and-appeals/amazon-and-state-aid-doctrine-unchecked-mission-creep/2021/06/14/76l71.

114. *Id.*

115. Ryan Finley & Kiarra M. Strocko, *Amazon and Engie Cast Doubt On State Aid Enforcement Approach*, 102 TAX NOTES INT'L 874, 874 (May 17, 2021), https://www.taxnotes.com/tax-notes-international/competition-and-state-aid/amazon-and-engie-cast-doubt-state-aid-enforcement-approach/2021/05/17/5s7tb.

incentivize business, the Commission should attempt to challenge on different grounds.[116] Additionally, the Commission has failed to carry its evidentiary burden in several recent state aid cases, and may need to adjust its approach moving forward.[117] One change the Commission may consider is utilizing expert witnesses in order to meet its evidentiary burden, which is common practice in U.S. transfer pricing cases.[118]

VI. EFFECT ON THE UNITED STATES

A. Possible U.S. Responses

Although Apple faces enormous tax repercussions in the EU, Apple's tax litigation in the EU originally stemmed from a May 2013 U.S. Senate report which critically detailed Apple's tax strategies and profit-shifting tools.[119] Following the Senate report, the European Commission began investigating Apple's profit shifting methods within the EU and concluded that Apple had underpaid Irish taxes by €13 billion between the years 2003 and 2014.[120] However, U.S. transfer pricing laws at the time did not allow for recovery of amounts shifted to other jurisdictions.[121] Several different methods of taxing Apple's income have been suggested, including a subpart F income approach or taxing the foreign entities as "income effectively connected with a U.S. trade or business."[122] In determining "income effectively connected with a U.S. trade or business," the IRS would need to determine if the Apple branches in Ireland had a U.S. trade or business and whether the income earned from these subsidiaries is "effectively connected" to the U.S. trade or business.[123] If the IRS could argue that Apple's activity fell into one of these categories, the 35% corporate tax rate would apply for the years at issue.[124]

Another possible response is the OECD proposing new corporate tax solutions, which the U.S. has argued could be detrimental to American multinationals.[125] Before the decision in the *Apple* case, the OECD

116. *Id.* at 875.
117. *Id.* at 875–76.
118. Goulder, *supra* note 113, at 1571.
119. Chamberlain, *supra* note 12, at 1179.
120. *Id.* at 1179–80.
121. *Id* at 1181.
122. *Id.* at 1182.
123. *Id.*
124. *Id.*
125. *See* Stephanie Soong Johnston, *Crunch Time: What the Apple Decision Means for Global Tax Reform*, TAX NOTES TODAY INT'L, 5 (July 28, 2020), https://www.taxnotes.com/tax-notes-

proposed a "two-pillar solution" to address issues in the international corporate taxation.[126] The first pillar "calls for the revision of profit allocation and nexus rules," and the second pillar proposes a minimum corporate tax rate.[127] When these pillars were proposed, the U.S. called for the first pillar to "be implemented on a safe harbor basis," which many countries in the OECD opposed.[128] The U.S. argues that the first pillar hurts American multinationals because the focus has been on taxing digital services.[129] With the *Apple* case being reversed and the Commission losing several state aid cases,[130] negotiations in the OECD about international corporate taxation may continue to shift in order to place greater burdens on U.S. multinationals.

VII. CONCLUSION

Though the European Commission's argument was unsuccessful before the EU General Court, there are several avenues the Commission may be able to successfully argue on appeal. As noted by the Court and commentators, the Commission needs to bring forth correct calculations and evidence of Apple's tax strategies in Ireland. Regardless of the outcome, this case still raises questions as to whether the EU should try to harmonize corporate tax laws rather than allow each country to create their own tax policies. Further, based on the holding of the EU General Court, the Commission secured several favorable holdings concerning arm's length transaction in state aid cases, but did not show that it applied the principles correctly in analyzing Apple's tax strategies. The final resolution of this case may still take a few years to sort out. During that time, both sides can, and likely will, challenge some of the aspects from the EU General Court's opinion.

today-international/digital-economy/crunch-time-what-apple-decision-means-global-tax-reform/2020/07/28/2crm9?highlight=state%20aid.

126. *Id.* at 1–2.
127. *Id.* at 5.
128. *Id.*
129. *Id.* at 6.
130. *Id.* at 1.