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Company Size Matters

Ruth Mason & Leopoldo Parada*

Abstract

Member States increasingly use classifications based on company size in their tax laws. Because bigger companies are more likely to be foreign, this Article poses the question of whether company-size classifications indirectly discriminate on the basis of nationality in violation of the fundamental freedoms. Our exploration of size-based classifications reveals important open doctrinal questions about the quantum and evidentiary burden required to show indirect discrimination, and about what role, if any, intent to discriminate plays or ought to play in discrimination cases. We also consider potential justifications for company-size-based classifications, including administrability and the goal to tax companies on the basis of ability to pay. Although we conclude that most company-size classifications can be justified, we argue that these justifications would be difficult to apply to recently enacted digital-services and similar taxes.

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I. Introduction

EU law forbids nationality discrimination, including both *direct discrimination*, in which a state uses nationality as a classification, and *indirect discrimination,* in which a state uses some other legal classification that proxies nationality.[1] This Article explores whether company-size classifications—including those based on turnover, capitalization, profit, and even physical size—constitute indirect nationality discrimination in violation of the EU fundamental freedoms. Our argument that company-size classifications may constitute indirect nationality discrimination is simple: because bigger companies tend to be foreign, taxes that fall more heavily on larger companies will tend to disproportionately affect foreign companies.

Part II relies on doctrine to distinguish two types of indirect discrimination cases, namely, those involving facially suspect classifications and those involving facially neutral classifications. Facially suspect classifications are those that obviously and strongly correlate with nationality, while facially neutral rules do not. Cases involving facially suspect rules have typically been easily resolved by the CJEU on judicial notice, without the need for empirical evidence of their correlation with nationality. In contrast, the CJEU typically relies on evidence of discriminatory impact to evaluate facially neutral rules, but it has not set clear guidelines as to the relationship the facially neutral classification must have to nationality for it to be regarded as discriminatory. Although the Court recently has suggested that if a *majority* of companies adversely affected by a facially neutral classification are foreign, then that classification indirectly discriminates, we are skeptical that such a bright-line rule could fit all scenarios.

The Court of Justice regularly emphasizes that what matters in discrimination cases is *effects*, not intent. Notwithstanding that consistent assertion, we show the Court sometimes takes discriminatory intent into account, particularly in cases involving facially neutral rules. In Part III, we argue that there are good reasons for the Court to consider intent to discriminate as at least probative, if not dispositive, in indirect discrimination cases. Although we argue that use of intent is legitimate and could further the goals of the common market, we also raise potential objections to using discriminatory intent, including that it would be difficult to prove.

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* Ruth Mason is the Edwin S. Cohen Distinguished Professor of Tax Law at the University of Virginia (UVA) School of Law. Dr Leopoldo Parada, LLM (Florida) is a visiting professor of international and EU tax law at the Department of Management of the University of Turin and the Faculty of Economics of the Free University of Bolzano in Italy. We are also very grateful to Andrés Báez Moreno (Universidad Carlos III de Madrid), Allison Christians (McGill University), Raymond Luja (Maastricht University), Georg Kofler (Johannes Kepler University of Linz), Wolfgang Schön (Max-Planck Institute), Rita Szudoczky (WU Vienna), and two anonymous reviewers for their valuable comments to earlier drafts of this paper. Justin Aimonetti (UVA Class of 2020), Elizabeth Donald (UVA Law class of 2019), and Emily Ostertag (UVA Law class of 2020) provided valuable research assistance. Nearly every research librarian at UVA Law contributed something to this article, but we must single out the contributions of Kathryn Boudouris, who became nearly as interested in the project as we were. All errors are our own.

[1] *See infra* Part II.A.

We think that most size-based classifications can easily be justified, and in Part IV, we evaluate what we regard as the most promising potential justifications for size-based tax classifications, namely, public policy, administrability, ability to pay, and countering tax abuse. In Part V, however, we discuss a case in which we believe justifications for size-based classifications fail, namely the French digital services tax. This tax involves intentional nationality discrimination, and the promising justifications laid out in Part IV do not apply to it. Part VI concludes.

II. Doctrinal Analysis of Company-Size Classifications

This Part highlights differences in the approach of the Court of Justice to two types of indirect discrimination cases, namely, those involving facially suspect classifications and facially neutral classifications. Understanding how the CJEU might treat size classifications requires us to understand that such classifications are facially neutral and that, as we argue in this Part, the Court approaches facially neutral and facially suspect classifications differently.

Facially suspect classifications are those that obviously and strongly correlate with nationality, while facially neutral rules do not. Cases involving facially suspect rules have typically been easily resolved by the CJEU on judicial notice, without the need for empirical evidence. In contrast, cases involving facially neutral rules are considerably harder to resolve. In such cases, the CJEU relies on empirical evidence of the correlation between the classification and nationality. One of the most important unresolved questions arising in such cases is what relationship the facially neutral classification must have to nationality to be regarded as discriminatory. Facially neutral rules therefore raise what we label the "quantum question," whether a particular numerical correlation between size and nationality indicates nationality discrimination.

We analyze the few cases in which the CJEU has considered whether company-size classifications constitute indirect nationality discrimination. Like all cases involving facially neutral classifications, size classifications raise the quantum question. Although the Court recently has suggested that if a *majority* of companies adversely affected by size-based classifications are foreign, then that classification covertly discriminates, we are skeptical that such a bright-line rule could fit all scenarios. Because our doctrinal analysis of fundamental-freedoms cases involving company-size classifications does not provide a clear answer to the question of how the CJEU might handle them, we look to cases involving facially neutral rules in other areas of EU law, namely, Article 110 TFEU and state aid. These cases suggest a larger role for judicial review of discriminatory intent in cases involving facially neutral rules.

A. Facially Suspect Cases

Indirect nationality discrimination may involve a *facially suspect classification*, that is, a classification that intrinsically or obviously and strongly correlates with nationality. Cases involving facially suspect rules exist on a continuum of "obviousness" or "strength of correlation with nationality," and we do not seek here to draw sharp distinctions among such cases. Instead, our principal goal is to distinguish facially suspect classifications, which involve clear links to nationality, from facially neutral classifications, which do not.

Establishing nationality discrimination in cases involving facially suspect classifications may—but typically does not—require presentation of empirical or other evidence to the Court that proves that the challenged classification disproportionately impacts non-nationals. And such cases typically do not raise questions regarding the quantum of disproportionate impact required to support a finding of indirect discrimination. On the other hand, in cases where the link between nationality and the suspect classification is clear, but not very strong, the Court is more likely to take empirical evidence into account.

For example, in *Baxter* the Court readily accepted without proof that a French tax regime that allowed deductions for research activities only if such activities were conducted *in France* discriminated against companies established in other EU Member States.[2] The Court came to this conclusion without presentation of empirical evidence and notwithstanding that the nationality discrimination was incomplete. That is, not all foreign companies suffered higher tax under the rule, and some French companies suffered higher tax under it. For example, foreign companies that conducted research in France could secure a deduction; as a result, some foreign companies received benefits under the rule. Likewise, French companies that did research outside of France would receive no deduction, so some of the burden of the rule fell on domestic companies. France argued that the deduction could not be regarded as discriminatory unless

> it appeared, taking account of the economic data for the year of reference, that, in fact, generally and by is very nature, it puts undertakings having their headquarters, central administration or principal place of business in a Member State other than that in which the levy is charged at a disadvantage in relation to undertakings for which those places are located in the levying Member State.[3]

Thus, France argued that evidence was needed to establish that the actual effect of the tax fell disproportionately on outsiders. But, as in other cases involving facially suspect classifications, the Court did not demand such evidence.[4] On the contrary, it reasoned that because companies' research facilities were generally located in a company's principal place of business, the "tax allowance in question seems likely to work more particularly to the detriment of undertakings having their principal place of business in other Member States."[5] As such, the deduction

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2 Case C-254/97, *Société Baxter and Others v. Premier Ministre and Others,* EU:C:1999:368, ¶¶ 12–13.

3 *Id.* at ¶ 8. France based its claim on the unusual nature of the tax at issue in Baxter, which was a temporary tax on a prior year's turnover from only certain products. *Id.*

4 *See e.g.,* Case C-204/90, *Bachmann v. Belgium State*, ECLI:EU:C:1992:35 (reasoning without evidence that workers holding life insurance policies written by foreign insurance companies were more likely to be non-nationals); Case C-175/88, *Biehl v. Administration des Contributions*, ECLI:EU:C:1990:186 ¶ 14 (reasoning, without benefit of empirical evidence, that "[e]ven though the criterion of permanent residence in the national territory referred to in connection with obtaining any repayment of an over-deduction of tax applies irrespective of the nationality of the taxpayer concerned, there is a risk that it will work in particular against taxpayers who are nationals of other Member States. It is often such persons who will in the course of the year leave the country").

5 Case C-254/97, *Baxter and Others, supra* note 2, ¶ 13.

indirectly discriminated on the basis of nationality in violation of the freedom of establishment.[6] The holding in *Baxter* strikes us as correct.

Baxter establishes three important principles. First, the Court can draw logical inferences from the text of the statute about the impact of classifications on nationals and non-nationals, without having to resort to evidence of impact. Second, to be discriminatory, a classification need not result in total exclusion of non-nationals from benefits.[7] Third, exclusion of some nationals from the contested benefit does not preclude a finding that the classification indirectly discriminates against non-nationals. Each of these propositions becomes important in cases where the connection between the classification and nationality is sufficiently tenuous that the parties must present empirical evidence to establish the discriminatory impact of the classification.

The list of suspect classifications that the Court of Justice has held to illegally proxy nationality contains no surprises; nor, by definition, should it. These cases involve proxies that obviously or intrinsically disproportionately impact non-nationals;[8] they include corporate tax residence,[9] individual tax residence,[10] domicile of dependent children,[11] location,[12] and residence

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[6] *Id.*

[7] *See also* Case C-172/11, *Georges Erny v. Daimler AG - Werk Wörth*, ECLI:EU:C:2014:157 (citing Case C 542/09 *Commission v. Netherlands* [2012] ECR, ¶ 38) ("In order for a measure to be treated as being indirectly discriminatory, it is not necessary for it to have the effect of placing at an advantage all the nationals of the State in question or of placing at a disadvantage only nationals of other Member States, but not nationals of the State in question…").

[8] *See, e.g.,* Case C-35/97, *Commission of the European Communities v. French Republic*, ECLI:EU:C:1998:431, ¶ 38; Joined Cases C-570/07 and C-571/07, *Blanco Pérez and Chao Gómez*, ECLI:EU:C:2010:300, ¶ 119.

[9] There is a straightforward and strong correlation between tax residence and corporate nationality, because corporate nationality follows charter under EU law, and tax residence, in turn, often follows charter. See CONSOLIDATED VERSION OF THE TREATY ON THE FUNCTIONING OF THE EUROPEAN UNION, 2012 O.J C 326/01, art. 54 ("Companies or firms formed in accordance with the law of a Member State and having their registered office, central administration or principal place of business within the Union shall, for the purposes of this Chapter, be treated in the same way as natural persons who are nationals of Member States.") [hereinafter TFEU]. Many cases confirm this. *See*, *e.g.,* Case C-330/91, *The Queen v. Inland Revenue Commissioners, ex parte Commerzbank,* ECLI:EU:C:1993:303, ¶ 15 (requiring no empirical evidence, but rather taking judicial notice of the fact that "[a]lthough it applies independently of a company's seat, the use of the criterion of fiscal residence within national territory for the purpose of granting repayment supplement on overpaid tax is liable to work more particularly to the disadvantage of companies having their seat in other Member States.").

[10] Case C-175/88, *Biehl v. Administration des Contributions du grand-duché de Luxembourg*, ECLI:EU:C:1990:186.

[11] Joined Cases C-4/95 and C-5/95, *Stöber and Piosa Pereira v. Bundesanstalt für Arbeit*, ECLI:EU:C:1997:44.

[12] Case C-120/95, *Nicolas Decker v. Caisse de maladie des employé privés*, ECLI:EU:C:1998:167 (holding that the requirement to seek pre-approval to receive care from medical provider located out of state was covert nationality discrimination); *see also* Case C-143/87, *Stanton v. Inasti*, ECLI:EU:C:1988:378 (involving the payment of mandatory social security contributions for non-nationals deemed self-employed in Belgium); Joined Cases C-570/07 and C-571/07, *Blanco Pérez and Chao Gómez*, ECLI:EU:C:2010:300 (holding that licensing preferences for pharmacists that had experience in the particular geographic area was covert nationality discrimination); Case C-514/12, *Zentralbetriebsrat der gemeinnützigen Salzburger Landeskliniken Betriebs GmbH v. Land Salzburg*, ECLI:EU:C:2013:799 (holding that for purposes of promotion, Land Salzburg could not take into account periods of relevant professional service that workers completed inside, but not outside, Land Salzburg).

of a company's owners.[13] In none of the cases just mentioned did the Court require empirical evidence to establish the connection between the classification and nationality; instead it observed that there was an intrinsic link between the two.[14]

Although the Court typically does not require evidence in cases involving facially suspect classes, on rare occasions, it does. *Stanton v. Inasti* raised the question of whether Belgium discriminated when it offered social-security tax exemptions for a person's second occupation, but only if that person's first occupation was in Belgium. Although the Court held that the rule was restrictive, it held that it was not necessarily discriminatory because it could disadvantage Belgians whose first occupation was abroad as much as or more than non-nationals whose first occupation was abroad.[15] Notice that once the Court begins to consider empirical evidence of the effect of the tax rule on foreigners, it must also answer the question of how significant the impact must be to warrant a finding of indirect nationality discrimination.[16] In *Stanton v. Inasti,* the standard the Court used was that those disadvantaged by the tax had to be "*exclusively* or *mainly* foreign nationals."[17]

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13 Case C-3/88, *Commission of the European Communities v. Italian Republic*, ECLI:EU:C:1989:606 (holding that an Italian rule preventing the government from awarding data-processing contracts to companies that were not majority-owned by Italy or the Italian public constituted covert nationality discrimination).

14 Case C-35/97, *Commission of the European Communities v. French Republic*, ECLI:EU:C:1998:431, ¶ 38 ("a provision of national law must be regarded as indirectly discriminatory if it is intrinsically liable to affect migrant workers more than national workers and if there is a consequent risk that it will place the former at a particular disadvantage"). *See id*. at ¶ 23 (noting that the residence requirement was intrinsically discriminatory). *Blanco Pérez and Chao Gómez*, *supra* note 8, at ¶ 119 ("a provision of national law must be regarded as indirectly discriminatory if it is intrinsically liable to affect the nationals of other Member States more than the nationals of the State whose legislation is at issue").

15 Case C-143/87, *Stanton v. Inasti, supra* note 12, at ¶ 9 ("[a]lthough it is true that self-employed persons whose principal occupation is employment in a Member State other than Belgium are thereby placed at a disadvantage, nothing has been submitted to the Court to show that the persons disadvantaged are *exclusively* or *mainly* foreign nationals.").

16 In its freedom of movement of goods cases, the Court typically examines empirical evidence, even in cases involving suspect classifications, such as when the state imposes lower tax rates on national products, such as national liquors, than on similar products from other countries. Case 171/78, *Commission v. Denmark*, ECLI:EU:C:1980:54, ¶ 23 (noting that there is a lighter tax for schnapps, most of which was produced in Denmark, than other liquors). *See id*. at ¶ 36 (describing the Danish rule that "does not establish any formal distinction according to the origin of the products, [but] it has been adjusted so that the bulk of the domestic production of spirits comes within the most favorable tax category whereas almost all imported products come within the most heavily taxed category."); See *id.* at ¶ 23 (considering empirical evidence of nationality impact); *see also* Case 277/83, *Commission of the European Communities v. Italian Republic*, ECLI:EU:C:1985:285 (considering empirical evidence of nationality impact of Italian tax regime that preferred marsala); Case C-230/89, *Commission of the European Communities v. Hellenic Republic*, ECLI:EU:C:1991:156 (similar Article 110 case involving Greek ouzo); Case C-3/88, *Commission of the European Communities v. Italian Republic*, *supra* note 13 (noting a rule that prevented Italy from awarding government data-processing contracts to companies that were not majority owned by Italy or the Italian public excluded all non-Italian data-processing firms from public contracts); *see id.* at ¶ 9 ("[T]here are at present no data-processing companies from other Member States all or the majority of whose shares are in Italian public ownership.").

17 Case C-143/87, *Stanton v. Inasti*, *supra* note 12, at ¶ 9 (emphasis added).

B. Facially Neutral Cases

Far more difficult to resolve than cases involving facially suspect classifications are cases involving what we call facially neutral classifications, those that refer neither to nationality nor to obvious or intrinsic proxies for nationality, such as residence or geographic location of activities. Facially neutral rules may discriminate if they disproportionately impact foreigners. Tax cases involving truly facially neutral classifications appear to be rare, but recent and pending cases raise questions of whether classifications based on company size, including retail square-meterage, net turnover, and gross turnover, constitute indirect nationality discrimination.

This Subpart first considers prior and pending fundamental-freedoms cases involving size classifications; it confirms that the CJEU uses empirical evidence to resolve such cases. We criticize the Court's adoption of a simple majority rule in such cases, under which a facially neutral classification discriminates if a majority of those adversely affected by it are foreign. Next, to enrich our account of indirect discrimination, we consider cases from other areas of law—Article 110 TFEU and state aid—that involved facially neutral classifications. This leads us to conclude that, in cases involving facially neutral rules, the Court seems to be more likely to consider the Member State's intent to discriminate. We conclude that important questions remain open regarding both the quantum of impact needed to show indirect discrimination and whether it matters for the Court's analysis whether a state intended to discriminate against non-nationals by adopting the facially neutral classification.

1. Fundamental Freedoms Cases Involving Size Classifications

Because government classifications on the basis of company size disproportionately affect non-nationals, such classifications may constitute indirect nationality discrimination.[18] Intuition and empirical evidence support this claim. The intuitive argument is that larger firms are more likely to have capital and other resources needed to expand across borders than are smaller firms. Empirical evidence also supports the connection between size and both multi-nationality and cross-border economic activity.[19] Because the connection between nationality and company size is attenuated, however, company size is a facially neutral rule. The rest of this subpart considers the few fundamental-freedoms cases implicating size restrictions; it concludes that the Court of

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[18] For state-aid purposes, the question might be whether the size classification disproportionately *favored* non-nationals. *See, e.g.,* Joined Cases C-182/03 and C-217/03, *Kingdom of Belgium and Forum 187 ABSL v. Commission of the European Communities*, ECLI:EU:C:2006:416.

[19] Owen Gabbitas and Paul Gretton, *Firm Size and Export Performance: Some Empirical Evidence*, COMMISSION WORKING PAPER NO. 1739, *available* at SSRN (noting that the likelihood for a company to become an exporter increases with size); Richard Kneller and Mauro Pisu, *Export Oriented FDI*, UNIVERSITY OF NOTTINGHAM RESEARCH PAPER NO. 2004/35, *available at* SSRN (pointing out that foreign-owned companies are more likely than domestic-owned companies to be exporters); Johannes Voget, *Relocation of Headquarters and International Taxation*, 95 J. PUB. ECON. 1067 (2011) (comparing the number of domestic headquartered firms to the number of multinational headquartered firms for different nations).

Justice observes a majority rule: if more than half of the adversely taxed population is foreign, the Court typically finds the classification to discriminate.

The 2011 case *Commission v. Spain* dealt with physical size. The Commission brought a failure-to-fulfill-an-obligation action against Spain, arguing that Catalonia's business-licensing regime violated the freedom of establishment by discriminating on the basis of physical size and, by proxy, on the basis of nationality.[20] In Catalonia, large (as measured by square footage) businesses were subject to more stringent regulations than were smaller businesses. Catalonia forbade physically large businesses[21] from opening in sparsely populated areas.[22] In addition to this prohibition, physically large businesses were subject to licensing and other requirements and fees not imposed on smaller businesses.[23] As a result of these restrictions, physically large stores could establish in only 4 of Catalonia's 41 municipal districts.[24] Under Catalonia's various regulatory regimes, large businesses thus faced significantly more obstacles to business establishment than did small businesses. But the regulations did not facially discriminate—they made no mention of nationality.

The Commission's argument that Spain violated the freedom of establishment was that the large retailers subject to the stringent regulatory requirements would tend to be foreign, whereas smaller businesses subject to more the permissive regulations would tend to be Spanish.[25] Although this argument makes intuitive sense, the Court ultimately rejected it because the Commission failed to prove that the regulation *actually* disproportionately affected non-nationals.[26] In contrast with earlier cases like *Baxter* that involved facially suspect classes, such as location of research activities, the Court of Justice in *Commission v Spain* demanded "conclusive evidence" of the actual effect of the classification on national compared to other-EU companies.[27] The Court's opinion concurred with Advocate General Sharpston's opinion in the case. Sharpston

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20 Case C-400/08, *Commission v. Spain*, ECLI:EU:C:2011:172. The case involved a number of other claims not considered here.

21 Large businesses, or "hypermarkets," had an area of at least 2,500m².

22 "Under Article 4(1) of Law 18/2005, large retail establishments may be opened only in consolidated urban areas of municipalities which are either the administrative centre of a district or which have a population of more than 25 000 inhabitants or seasonal tourist visitors who may be regarded as such." Case C-400/08, *Commission v. Spain*, *supra* note 20, at ¶ 7.

23 *Id.* at ¶ 53.

24 *Id.* at ¶¶ 38-39. Hypermarkets were defined as self-service outlets with a sales area of at least 2,500m² that sold a wide range of goods and had large parking areas. *Id.* at ¶ 20. Even in the districts open to hypermarkets, "only 23 667m² are available." *Id.* at ¶ 52. The Commission also complained about more onerous licensing demands, which required businesses to supply market surveys and to submit their requires to local "Retail Facilities Committees" review boards whose members might include competitors. *Id.* at ¶ 53.

25 "…That legislation gives rise to indirect discrimination by favouring the setting up of medium-sized retail establishments rather than large retail establishments. Most economic operators wishing to set up medium-sized retail establishments are of Spanish nationality, whereas those wishing to set up large retail establishments are more usually from other Member States." *Id.* at ¶ 55; *see also id.* at ¶ 61 (noting the same).

26 *Id.* at ¶ 60 ("The information provided to the Court does not enable it to determine with certainty either the number of establishments concerned or the breakdown between Spanish and non-Spanish control of a significant part of the establishments falling within the category of large establishments…").

27 *Id.* at ¶ 62.

concluded that "[u]nless it is true that Spanish (in particular Catalan) operators favour smaller retail establishments while operators from other Member States favour large establishments, the measures in issue cannot discriminate against the latter, whatever the extent to which they may restrict the opening of large retail establishments over and above that of other establishments."[28]

To support its case for discrimination, the Commission adduced some evidence, which the Court found inadequate. The Commission showed that foreign operators controlled the majority (53 to 68%) of large establishments, while Spanish operators controlled the majority (72 to 92%) of smaller establishments. But this "broad statistical correlation" between size and nationality was insufficient to show nationality discrimination in the views of both Advocate General Sharpston[29] and the Court of Justice.[30] Advocate General Sharpston noted that "[a]ny tentative conclusion which might be drawn from the figures given would therefore need to be backed up by firm evidence of a different kind."[31] Although the advocate general did not explain what this other evidence might consist of,[32] she appeared to be looking for proof of a causal relationship between size and nationality.[33]

Hervis, a case decided in 2014, also involved a size classification.[34] Hungary had a graduated net turnover tax, which applied higher turnover tax rates to companies with higher net turnover.[35] If a company was a member of a corporate group, then for purposes of determining the applicable tax rate, the company's turnover had to be aggregated with that of all the other members of its group for purposes of determining its tax rate.[36] As a result, companies that were members

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[28] Case C-400/08, *Commission v. Spain* (opinion of Advocate General Sharpston), ECLI:EU:C:2010:588, ¶56 [hereinafter "AG opinion in Commission v. Spain"].

[29] *Id.* at ¶ 58.

[30] *See* Case C-400/08, *Commission v. Spain*, *supra* note 20, ¶ at 60 ("The information provided to the Court does not enable it to determine with certainty either the number of establishments concerned or the breakdown between Spanish and non-Spanish control of a significant part of the establishments falling within the category of large establishments…. Nor has the Court been provided with a breakdown showing the respective shareholdings of the economic operators concerned in the various categories of establishment.").

[31] AG opinion in Commission v. Spain, *supra* note 28, at ¶ 58.

[32] *Id.*

[33] *Id.* at ¶ 59 ("The nearest the Commission has come to explaining the supposed causal relationship underlying the statistical correlation was its suggestion – at the hearing, in response to a question from the Court – that foreign operators would naturally prefer to set up larger establishments in order to achieve the economies of scale necessary to optimise their chances of successful penetration in a new territory. But such reasoning – plausible though it may be – relates to entry into a new market at a distance from the home base, rather than to the operator's nationality, and thus provides only partial support for the Commission's basic premis[e].") (footnotes omitted).

[34] Case C-385/12, *Hervis Sport- és Divatkereskedelmi Kft. v Nemzeti Adó- és Vámhivatal Közép-dunántúli Regionális Adó Főigazgatósága Request for a preliminary ruling from the Székesfehérvári Törvényszék*, ECLI:EU:C:2014:47 [hereinafter "Case C-385/12, *Hervis*"]. The case involved classifications based on net turnover, which is also a size classification. *Id.*

[35] *Id.* at ¶ 8 ("0% for the band of the taxable amount up to 500 million [Hungarian forints (HUF)], 0.1% for the band between HUF 500 million and HUF 30 billion, 0.4% for the band between HUF 30 billion and HUF 100 billion, and 2.5% for the band above HUF 100 billion.").

[36] A company's tax bracket was determined not only by its own turnover in Hungary, but rather by its own Hungarian turnover plus the Hungarian turnover of any company—foreign or domestic—to which it was "linked" directly or indirectly. Companies were linked if, inter alia, one had a "majority influence" over the other, or if a third party had a majority influence over both. *Id.* at ¶ 11. So a Hungarian subsidiary's (Sub's) turnover would be

of corporate groups were more likely to be subject to higher tax rates under Hungary's system. Hervis, an Austrian-parented company with subsidiaries in Hungary, challenged the aggregation rule, arguing that companies operating as groups were more likely to be foreign.

In her opinion in *Hervis*, Advocate General Kokott noted that indirect discrimination cases raise the question of

> …how strong the correlation between the chosen distinguishing criterion and the place in which a company has its seat must be in order for there to be unequal treatment based on the seat. Thus far, the Court has had in view both a correspondence in the *majority* of cases and a *mere preponderance* of non-residents being affected, or even mentioned a *mere risk* of disadvantage. It would appear to have been established thus far only that a 100% correspondence between the criterion and the place in which the company has its seat is not required.[37]

Thus, Advocate General Kokott pointed to an open doctrinal question—what does it take to show discriminatory impact? Advocate General Kokott sought to bring clarity to the doctrine by distinguishing cases in which a classification "inherently" correlates with nationality from cases in which the classification merely "typically correlates" with nationality.[38] Kokott's "inherently" correlating classifications are what that Article calls facially suspect classifications. In contrast, facially neutral rules do not inherently correlate with nationality, but they may do so incidentally. The question then becomes how to distinguish harmless or incidental correlation from indirect nationality discrimination that violates the fundamental freedoms. In Kokott's view, facially neutral rules, that is, those that only typically correlate with nationality and therefore only typically disadvantage foreigners should be regarded as discriminatory only when the classification correlates with nationality in the "vast majority of cases."[39] She did not specify a numerical value for 'vast majority.'

Despite Advocate General Kokott's invitation to distinguish between "inherently correlated" and merely "typically correlated" proxy classifications, when the CJEU decided *Hervis*, it concluded that if *a majority* of those subject to the highest progressive turnover tax rate were foreign-parented (an empirical question to be determined by the referring national court[40]),

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aggregated with its Hungarian and foreign affiliates' Hungarian turnover for purposes of determining the tax rate that applied to the Hungarian subsidiary's (Sub's) turnover.

37 *Hervis* (Opinion of Advocate General Kokott), ECLI:EU:C:2013:531, ¶ 38 [hereinafter "AG opinion in Hervis"] (emphasis added) (citing a number of cases for the majority rule including: Case 143/87 Stanton and L'Étoile, Case C-330/91 Commerzbank, Case C-254/97 Baxter and Others, and Case C-383/05 Talotta); *Blanco Pérez and Chao Gómez*, *supra* note 8, at ¶¶ 113-14 (discussing the preponderance rule); and for the mere risk rule C-383/05 Talotta, Cases C-570/07 and C-571/07 Blanco Pérez and Chao Gómez and Case C-175/88 Biehl).

38 AG opinion in Hervis at ¶ 39. *Id*. at ¶ 45 ("[U]nequal treatment of resident and non-resident companies can also result from a purely factual, more incidental connection between the distinguishing criterion and the place in which a company has its seat.").

39 *Id.* at ¶ 41.

40 Case C-385/12, *Hervis, supra* note 35, at ¶ 40.

the Hungarian tax would constitute nationality discrimination in violation of the fundamental freedoms.[41] The Court's decision focused on the aggregation rule to conclude that

> if it is established that. . .the taxable persons belonging to a group of companies and covered by the highest band of the special tax are, in the majority of cases, 'linked', within the meaning of the national legislation, to companies which have their registered offices in other Member States, the application of the steeply progressive scale of the special tax to a consolidated tax base consisting of turnover is liable to disadvantage, in particular, taxable persons 'linked' to companies which have their registered office in another Member State.[42]

If companies linked to nonresidents constituted the majority of those in the highest bracket, then the Hungarian rule would covertly discriminate on the basis of nationality in violation of the freedom of establishment,[43] unless it was justified.[44]

Another recent physical-size discrimination case rounds out our discussion of the fundamental-freedoms caselaw on size. Spain's National Association of Large Distribution Companies (Asociación Nacional de Grandes Empresas de Distribución, hereinafter ANGED) recently brought challenges under the freedom of establishment to retail taxes imposed by several Spanish municipalities on the grounds that the taxes applied only to retailers that occupied display and sales areas greater than or equal to 4000 square meters.[45] Citing *Hervis*, the CJEU acknowledged "that rules regarding equal treatment forbid not only overt discrimination based on the location of the seat of companies, but also all covert forms of discrimination which, by the application of other criteria of differentiation, lead in fact to the same result."[46] Again citing *Hervis*, the Court seemed to confirm, despite Advocate General Kokott's opinions in *Hervis* and *ANGED* to the contrary,[47] that the crucial question was whether the facially neutral tax in fact burdened *mostly* foreign taxpayers. In the Court's words, the question was whether the "apparently objective criterion of differentiation" "disadvantages in most cases…companies whose seat is in other Member States and that are in a comparable situation to companies whose seat is situated in the

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41 *Id.* at ¶ 39.
42 Case C-385/12, *Hervis, supra* note 35, at ¶ 39.
43 *Id.* at ¶ 41 (noting that legislation need not make "formal distinction according to the registered office of the companies" to be "indirect discrimination…for the purposes of Articles 49 TFEU and 54 TFEU").
44 *Id.* at 43–44 (noting that neither protectionism nor revenue need could be valid justifications).
45 *See, e.g.,* Case C-234/16, *Asociación Nacional de Grandes Empresas de Distribución ANGED v. Consejeria de Economia y Hacienda del Principado de Asturias* ECLI:EU:C:2018:281, ¶ 6 [hereinafter "Case C-234/16, *ANGED*"]. It is worth noting that the Commission also challenged certain exemptions from the tax as state aid.
46 *Id*. at ¶ 22.
47 *See*, Case C-234/16, *Asociación Nacional de Grandes Empresas de Distribución ANGED v. Consejeria de Economia y Hacienda del Principado de Asturias*, ECLI:EU:C:2017:853 (Opinion of Advocate General Kokott), ¶ 32 [hereinafter "AG opinion in ANGED"] ("In my view, it cannot be sufficient to have regard solely to whether foreign undertakings are affected in the majority of cases in order to be able to accept the existence of covert discrimination in the context of the fundamental freedoms"). *See id.* (emphasizing that if the taxable population is majority-foreign "more or less by chance," then there is no covert discrimination).

Member State where that tax is charged."[48] Although acknowledging that size *could* proxy nationality, the Court concluded that there was no violation of the freedom of establishment in *ANGED* because the challenged tax on physically large retailers did not, as an empirical matter, seem to disadvantage companies established in other Member States compared to those established in Spain.[49]

Hervis and the Spanish cases suggest that the Court requires empirical evidence of the impact of the facially neutral classification upon non-nationals, but that to matter for fundamental freedoms purposes, that impact need not result from an intrinsic connection between the two. Moreover, the impact need not be vastly disproportionate, despite Kokott's suggestion. Instead, the Court seems willing to accept a majority rule. Finally, in these cases, the Court did not expressly consider whether the Member State intended to discriminate on the basis of nationality.

2. Pending Size Cases

In two pending cases, *Vodafone* [50] and *Tesco-Global*, [51] Hungarian courts referred to the CJEU questions concerning whether Hungary indirectly discriminated on the basis of nationality when it applied higher turnover-tax rates to companies with higher net turnover.[52] The taxes at issue in these cases were structurally very similar or identical to the graduated turnover tax discussed in *Hervis*.[53] Because the aggregation rule that the Court of Justice found so problematic in *Hervis* was not implicated in these cases, however, they raise the size discrimination question differently than did *Hervis*.[54] The cases are pending before the CJEU, and Advocate General Kokott wrote opinions in both. Because Advocate General Kokott's reasoning in them is so similar, we mostly limit our discussion to the earlier of her two opinions, *Vodafone*.

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48 Case C-234/16, *ANGED*, *supra* note 46, at ¶ 23.

49 *Id.* at ¶ 25 ("Nor does the evidence submitted to the Court show that that criterion disadvantages in most cases nationals from other Member States or companies whose seat is in another Member State.").

50 Case C-75/18, *Vodafone Magyarország Mobil Távközlési Zrt. v. Nemzeti Adó- és Vámhivatal Fellebbviteli Igazgatósága,* ECLI:EU:C:2019:492 ["AG opinion in Vodafone"] The opinion of Advocate General Kokott was delivered on 13 June 2019. *Id*.

51 Case C-323/18, *Tesco-Global Aruhazak Zrt. v Nemzeti Ado- es Vamhivatal Fellebbviteli Igazgatosaga,* ECLI:EU:C:2019:567 ["AG Opinion in Tesco-Global"]. The Opinion of the Advocate Kokott was delivered on 4 July 2019. *Id*.

52 Request for a preliminary ruling from the *Fővárosi Közigazgatási és Munkaügyi Bíróság (Hungary) lodged on 6 February 2018 — Vodafone Magyarország Mobil Távközlési Zrt. v. Nemzeti Adó- és Vámhivatal Fellebbviteli Igazgatósága,* C- 75/18 [hereinafter, "C-75/18, *Vodafone*"]. Request for a preliminary ruling from the *Fővárosi Közigazgatási és Munkaügyi Bíróság (Hungary) lodged on 16 May 2018 — Tesco-Global Áruházak Zrt. v. Nemzeti Adó- és Vámhivatal Fellebbviteli Igazgatósága*, C-323/18 [hereinafter, "C-323/18, *Tesco Global"*]. For thorough analysis of these two pending cases, *see* Rita Szudoczky, *Vodafone Magyarország* C- 75/18 and *Tesco-Global Áruházak* C-323/18, in M. Lang et al. (eds.), *CJEU- Recent Developments in Direct Taxation 2018*, Linde Verlag, Vienna (forthcoming).

53 The tax regime in *Tesco* is identical to that challenged in *Hervis*. In *Vodafone*, the Hungarian tax increased as follows: the first 500 Million HUF was exempt, 500 to 5,000 million was taxable at 4.5%, and amounts over 5,000 million were taxable at 6.5%. AG opinion in Vodafone, supra note 51, at ¶ 12.

54 *Id.* at ¶ 52.

Advocate General Kokott noted that net turnover was a facially neutral classification; it involved, in her terms: "[n]o overt or direct discrimination against foreign undertakings."[55] The problem was disproportionate impact. Specifically, as the referring court observed, "Hungarian-owned taxable persons" disproportionately fell into the exempt net turnover band, whereas "Hungarian subsidiaries of foreign parent companies" comprised the majority of the companies in the highest tax band.[56] The Hungarian court asked whether this effect—that most of the highest-taxed companies were foreign-owned, while most of the exempt companies were domestically owned—violated the freedom of establishment.[57]

Noting that "[e]xisting case-law does not provide a consistent picture" about the extent to which the statutory classification must correlate with nationality to raise discrimination concerns, Advocate General Kokott renewed the call she made in *Hervis* to clarify the standard for indirect discrimination.[58] She argued against the majority-foreign rule adopted by the Court *Hervis* and endorsed by the Commission in *Vodafone*. Instead, Kokott argued that a majority rule was not a "reliable indicator for a correlation" with nationality. Moreover, she argued that the meaning of the majority rule was unclear.[59] For example, the *Hervis* Court directed the national court to determine whether a majority of the taxpayers in the highest tax bracket were foreign, but Kokott observed that there was no good reason to examine the nationality of only the taxpayers in the highest tax bracket, while ignoring those in the other brackets.[60] She also argued that the nationality composition of those subject to the highest tax rate could change from year to year,[61] and it may not always be easy to determine the nationality of entities subject to the highest rate of tax.[62] Finally, even if the group subject to the highest rate of tax was majority-foreign, she argued that this could be merely "incidental," rather than the result of discrimination.[63] For example, Hungary could simply have a very high proportion of foreign companies operating within its borders.[64] For these reasons, Kokott concluded that as a manner to establish indirect discrimination, "a quantitative approach is not appropriate."[65]

In lieu of a quantitative approach, Kokott advocated for a return to what she called the "qualitative criterion" the Court applied in earlier cases, under which a classification was indirectly

55 Id. at ¶ 58. *See id*. at ¶ 81 (arguing that net turnover was as "neutral" as profit or wealth as a classification).

56 There is some dispute about the foreign versus domestic composition of the tax brackets. The referring court claimed that only Hungarian-owned taxpayers fell into the exempt bracket, and the Commission noted that both foreign and domestic-controlled companies comprised the population in the middle bracket, and six of 16 companies in the highest band were foreign-controlled.

57 AG opinion in Vodafone, *supra* note 51, question 1.

58 *Id.* at ¶ 61.

59 *Id.* at ¶ 66.

60 *Id.* at ¶ 65.

61 *Id.* at ¶ 71.

62 *Id.* at ¶ 72.

63 *Id.* at ¶ 66.

64 *Id.* at ¶ 82.

65 *Id.* at ¶ 69.

discriminatory only if it "intrinsically" affected foreign companies."[66] In Advocate General Kokott's view, an "intrinsic" effect "clearly suggests the likelihood of a correlation in the vast majority of cases."[67] That a classification intrinsically correlates with nationality can be, on Kokott's account, determined "on an abstract analysis,"[68] by which we assume she means without empirical support. Thus, Kokott would limit review for indirect nationality discrimination to cases involving facially suspect classifications that do not require empirical evidence to establish or support the connection between the classification and nationality. Kokott ultimately concluded that because high net turnover was "a neutral distinguishing criterion" that did not intrinsically correlate with nationality, imposing higher taxes on companies with higher net turnover did not violate the freedom of establishment.[69]

Although she thus advocated a general presumption of legality for classifications that do not intrinsically correlate with nationality, Kokott was willing to permit an exception for cases of *intentional* discrimination; that is, "where a distinguishing criterion … was, in subjective terms, intentionally chosen to effect a high degree of disadvantage, in quantitative terms, for undertakings with generally foreign shareholders."[70] Because such intentional discrimination would constitute an abuse of rights by the state in violation of Article 4(3) TEU, the state should not, in Kokott's view, benefit from a presumption of legality.[71] Although the Commission submitted evidence in both pending cases of intentional discrimination—including parliamentary debates, statements by members of parliament, and extracts from government documents[72]—this evidence did not met Kokott's stringent standards for establishing discriminatory intent. As a result, she concluded that the taxes did not violate the fundamental freedoms.[73] The next Part will consider more deeply Kokott's arguments about legislative intent. Before we do so, we consider cases decided outside the fundamental freedoms in the hopes that they may shed light on the Court's approach to facially neutral rules.

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66 *Id.* at ¶ 74 (emphasis in original). *Id.* (*"*A merely incidental link, even if it is sufficiently high in quantitative terms, cannot therefore be sufficient, in principle, to establish indirect discrimination.") (citing Case C-496/15, *Eschenbrenner*, EU:C:2017:152, ¶ 36; with regard to free movement of workers, see, e.g., Case C-514/12, *Zentralbetriebsrat der gemeinnützigen Salzburger Landeskliniken Betriebs*, EU:C:2013:799, ¶ 26; Case C-172/11, *Erny*, EU:C:2012:399, ¶ 41; *Blanco Pérez and Chao Gómez*, *supra* note 8, at ¶ 119; with regard to freedom of establishment, see, e.g., Case C-269/07, *Commission v. Germany*, EU:C:2009:527; Case C-254/97, *Baxter and Others, supra* note 2, ¶ 13.

67 AG opinion in Vodafone, *supra* note 51, at ¶ 78.

68 *Id.*

69 *Id.* at ¶ 81.

70 *Id.* at ¶ 84.

71 *Id.* at ¶ 90.

72 *Id.* at ¶ 95-8 (referring to Commission citations to parliamentary debates, statements by members of parliament, and extracts from government documents). To provide a sense of the stringency of Kokott's standard, she concluded that the legislative intention may have been to excessively burden multinationals companies, not foreign companies. Obviously, multinationals are necessarily in part foreign, but this connection is evidently too attenuated to meet Kokott's standards. See *id.* at ¶ 95.

73 *Id.* at ¶ 103.

3. Article 110 TFEU and State-Aid Cases Involving Facially Neutral Classifications

We enrich our understanding of facially neutral classifications by considering some cases that the Court decided in other areas of EU law, namely Article 110 cases and state-aid cases. All of: the fundamental freedoms, Article 110, and the prohibition of state aid prevent Member States from taxing cross-border commerce less favorably than domestic commerce.[74] Thus, although Article 110 and state aid cases do not directly bear on fundamental-freedoms questions, they raise closely related questions. Our analysis under Article 110 TFEU and state aid is not exhaustive. We focus only on facially neutral classifications that tell us something useful about size classifications. No matter the substantive area of law, facially neutral classifications present the same essential question: what kind of link is needed between the putatively neutral classification and nationality to enable a judicial determination of discrimination? The Article 110 and state-aid doctrines reveal that the Court of Justice looks to both disproportionate impact on foreigners and whether the state intended to discriminate.

a) Article 110 TFEU

Article 110 prevents states from imposing protectionist or otherwise higher taxes on imported than domestic products.[75] The Court's approach in Article 110 cases to facially neutral tax classifications that disproportionately impact foreign goods suggests how the Court might analyze fundamental-freedoms cases, which among other functions, protect cross-border commerce from higher tax than purely domestic commerce. It is important to emphasize that we use the Article 110 cases because they involve reasoning analogous to what we might find in

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[74] In addition, the prohibition of state aid prevents Member States from treating cross-border commerce *better* than domestic commerce. Preventing discrimination between cross-border and domestic commerce is commonly referred to as "maintaining a level playing field" between competitors hailing from different EU member states, a concept known in U.S. literature as competitive neutrality. *See* Michael S. Knoll and Ruth Mason*, What is Tax Discrimination,* 121 YALE L. J. 1014 (2012) (arguing that the fundamental freedoms uphold competitive neutrality); Christina Dimitropoulou, *The Digital Services Tax and Fundamental Freedoms: Appraisal Under the Doctrine of Measures Having Equivalent Effect to Quantitative Restrictions*, 47 INTERTAX 201, 212 (2019) (noting that the free movement of goods prevents protectionism and promotes a level playing field); Ruth Mason, Identifying Illegal Subsidies 69 AMER. U. L. REV. ___ (2019) (contending that the prohibition of state aid prevents Member States from treating cross-border and domestic commerce differently); AG opinion in Vodafone, *supra* note 51, at ¶ 162 ("I concur with Advocate General Bobek that in essence the [state-aid] selectivity test is 'merely' a discrimination test.") (citing Case C-270/15 P, *Belgium v. Commission*, ECLI:EU:C:2016:289, ¶ 28 (opinion of Advocate General Bobek) (describing the question of whether state aid analysis is a nondiscrimination inquiry as 'rather academic')).

[75] Article 110 of the TFEU ("No Member State shall impose, directly or indirectly, on the products of other Member States any internal taxation of any kind in excess of that imposed directly or indirectly on similar domestic products. Furthermore, no Member State shall impose on the products of other Member States any internal taxation of such a nature as to afford indirect protection to other products.").

income tax cases decided under the fundamental freedoms.[76] Nor are we alone in regarding Article 110 precedents as relevant by analogy to fundamental freedoms cases.[77]

We start with *Humblot*, a landmark case decided in 1985 in which the CJEU held that France discriminated against imported cars when it imposed a two-part car tax.[78] The first part of the tax increased progressively with the car's horsepower, but the second part imposed nearly five times the highest progressive car tax on cars that exceeded a certain power threshold. Since France manufactured no cars above that power threshold, the highest tax fell entirely on imported cars. Notice that engine power is a facially neutral classification; it does not obviously or intrinsically correlate with nationality. There is no way to confirm, without knowing something about French car manufacturing, that the highest tax would fall exclusively on imported cars. Thus, if engine-power classifications discriminate on the basis of nationality, they do so through disproportionate impact on foreign products. A French court asked the Court of Justice whether the tax violated the predecessor of Article 110 TFEU. Arguing that it did, the Commission claimed that the French tax was "not geared to an economic policy objective, such as heavier taxation of luxury products or vehicles with high fuel consumption."[79]

In finding the tax to violate Article 110, the Court of Justice first noted that progressive taxation was generally permitted under Article 110, provided the tax increased with

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[76] We acknowledge that EU law governing free movement of goods has a long history characterized by several shifts in the doctrine. *See, e.g.,* Gareth Davies, "Between Market Access and Discrimination: Free Movement as a Right of Fair Conditions of Competition," in *Research Handbook on the Law of the EU's Internal Market* 13, 18 (2017). We do not seek to contribute to the academic debate over whether the fundamental freedoms forbid market access restrictions or whether they merely forbid discrimination. Our argument can be read as support for convergence of analysis between the free movement of goods and the other freedoms, but the Court of Justice has not yet (if it ever will) fully assimilated interpretations of the various freedoms, and it finds both discrimination and restrictions on cross-border commerce to be relevant to its fundamental-freedoms analysis. Discrimination analysis clearly plays a more important role and has a stronger textual basis under the fundamental freedoms other than the free movement of goods; it clearly dominates in income tax cases. Mason and Knoll*, supra* note 75.

We do not argue that classifications based on company size themselves constitute "restrictions" on free movement, although we regard such arguments as plausible. *See, e.g.,* Dimitropoulou, *supra* note 75. Unlike Advocate General Kokott, who regards discrimination analysis as sufficient to dispose of tax cases, we regard restrictions analysis as indispensable, although defending it lies outside the scope of this paper. *See, e.g.,* Case C-482/18, *Google Ireland Limited v. Nemzeti Adó- és Vámhivatal Kiemelt Adó- és Vámigazgatósága*, ECLI:EU:C:2019:728, ¶ 36 (arguing that because taxes always restrict intracommunity commerce, taxes should be subject *only* to discrimination analysis, and not to restrictions analysis). For more on differentiating discrimination and restrictions in tax cases, see, e.g., Ben Terra and Peter Wattel, *European Tax Law*, 6th Ed., Wolter Kluwers, 83-92 (2012); Ruth Mason & Michael S. Knoll, *Waiting for Perseus: A Sur-Reply to Professors Graetz and Warren*, 67 TAX L. REV. 375, 400-403 (2014).

[77] *See, e.g.,* AG opinion in ANGED, *supra* note 48, at ¶ 36 (citing *Humblot*, an Article 110 case, in a case considering whether a rule constituted covert discrimination that violated the freedom of establishment); Case C-190/98, *Volker Graf v. Filzmoser Maschinenbau GmbH* ECLI:EU:C:1999:423, ¶¶ 18-30 (opinion of Advocate General Fennelly) (including an extended discussion of the application of free movement of goods precedents in a freedom of establishment case).

[78] Case C-112/84, *Michel Humblot v. Directeur des services fiscaux*, ECLI:EU:C:1985:185, ¶ 14 [hereinafter Case C-112/84, *Humblot*].

[79] *Id.* at ¶ 10.

"an objective criterion."[80] Furthermore, horsepower could be such an objective criterion.[81] The Court seemed to regard the first tier of the tax, which applied to both imported and domestic cars and increased with the power rating, to be permissible. The problem was that France had "two distinct taxes, … a differential tax which increases progressively and is charged on cars not exceeding a given power rating for tax purposes and a fixed tax on cars exceeding that rating which is almost five times as high as the highest rate of the differential tax."[82] Because the higher tax fell exclusively on foreign products, the Court of Justice concluded that the impact of the facially neutral classification was discriminatory.

Two year later in *Feldain*, another case challenging a different aspect of the same French car tax regime, the Court of Justice confirmed the approach it had taken in *Humblot*.[83] According to Court: under the French system, when "one tax band comprises more power ratings for tax purposes than the others, with the result that the normal progression of the tax is restricted in such a way as to afford an advantage to top-of-the-range cars of domestic manufacture, and in which the power rating for tax purposes is calculated in a manner which places vehicles imported from other Member States at a disadvantage [it] has a discriminatory or protective effect."[84]

Decided just five years after *Humblot*, *Commission v. Hellenic Republic*,[85] involved very similar facts. Like the French car tax, the Greek car tax increased with engine size, but, similar to the French tax, there was a discontinuity in the Greek tax at 1600 cc, where the tax increased by 50 percent. As in the French tax, this break point coincided with foreign manufacture, so that the highest tax applied to only imported cars. In contrast with *Humblot*, however, the Court concluded that the Commission, which had brought the case, failed to show that consumers who wanted to avoid the highest tax would select a Greek-manufactured car instead, since both foreign and domestic car manufactures produced cars that were taxable in the lower bands. The Court did not offer clear reasons why this case should come out differently from *Humblot* or *Feldain*, but the Court in the Greek case wrote at greater length about states' entitlements to enact progressive taxes.[86]

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[80] *Id.* at ¶ 12 ("the Member States are at liberty to subject products such as cars to a system of road tax which increases progressively in amount depending on an objective criterion, such as the power rating for tax purposes, which may be determined in various ways").

[81] *Id.*

[82] Case C-112/84, *Humblot*, *supra* note 79, at ¶ 14.

[83] Case C-433/85, *Jacques Feldain v. Directeur des services fiscaux du département du Haut-Rhin*, ECLI:EU:C:1987:371 [hereinafter Case C-433/85, *Feldain*].

[84] *Id.* at ¶ 19.

[85] Case C-132/88, *Commission v. Hellenic Republic*, ECLI:EU:C:1990:165.

[86] *Id.* at ¶ 9. Commentators have criticized the inconsistency in the cases. *See* Noel Travers, *The Regulation of Tariffs and Indirect Taxation in the Intra-Community Trade*, 16 DUBLIN U.L.J. 55, 76-77, 81 (1994) (criticizing the decision in *Commission v. Hellenic* Republic and arguing for more substantial justifications than a simple social policy in cases of taxes that compartmentalize national markets by disproportionately affecting imported products). Another difference between the two is that the French tax rose much more steeply than did the Greek tax. The highest French rate was five times the rate of the next highest rate, whereas the highest Greek rate was only fifty percent more.

Although the French and Greek cases are difficult to reconcile, the Court in the Greek case seemed take a step back from finding indirect nationality discrimination in cases involving genuinely facially neutral classifications, those where the discriminatory effect was not discernable from the face of statute alone. Advocate General Mischo's opinion reflects a certain amount of discomfort with finding nationality discrimination in facially neutral cases. He wrote,

> I consider therefore that tax differentiation based on a criterion recognized as objective does not — suddenly — cease to be objective and become incompatible with Article 95 [current Article 110] solely because there are no domestic products which meet the conditions for the higher tax rate, provided that the imported products are not 'by definition', '*ex hypothesi*' or 'inherently' the only which could meet those conditions. [87]

This language previews the approach Advocate General Kokott would take in the Hungarian turnover-tax cases, and it tracks the same idea: facially neutral classifications should not be regarded as discriminatory solely because they have discriminatory impacts.

The Article 110 cases also confirm that the Court of Justice considers intent to discriminate as relevant to its analysis. In *Humblot*, the Court of Justice seemed to take the structure of the tax itself, together with its impact on foreign products, as evidence of intent to discriminate. According to the Court:

> Although the system embodies no formal distinction based on the origin of products it manifestly exhibits discriminatory or protective features contrary to Article 95 [now Article 110], since the power rating determining liability to the special tax has been fixed at a level such that only imported cars, in particular from other Member States, are subject to the special tax whereas all cars of domestic manufacture are liable to the distinctly more advantageous differential tax.[88]

In other Article 110 cases, the Court of Justice also paid attention to discriminatory intent—as evidenced by the structure or content of the statute itself, rather than statements by politicians. For instance, in *Commission v. Denmark*, Denmark subjected aquavit (schnapps) to a lower tax rate compared to other liquors that tended to be imported. In holding the tax to violate EU law, the Court noted that

> [a]lthough it does not establish any formal distinction according to the origin of the products, [the tax] has been adjusted so that the bulk of the domestic production of spirits comes within the most favorable tax category whereas almost all imported products come within the most heavily taxed category.… It therefore

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87 Case C-132/88, *Commission v. Hellenic Republic,* ECLI:EU:C:1990:83, ¶ 21.
88 *Id.* at ¶ 14.

> appears that the tax system is devised so that it largely benefits a typical domestic product and handicaps imported spirits to the same extent.[89]

Unlike engine size, schnapps is arguably not a neutral a classification; it is a national product of Denmark and closely associated with that country, but the Court's emphasis on the legislature's "adjustment" and "devising" of the tax suggests that the Court considers discriminatory intent as part of its review under Article 110.[90]

Although the Article 110 cases do not provide a clear framework for analyzing facially neutral rules, *Humblot* and the alcohol cases suggests that both empirical evidence and Member State intent—which intent is discernable from the statute itself, rather than external evidence such as statements by politicians—can help establish that a tax is protectionist. The Court of Justice has never overruled *Humblot*, and Advocate General Kokott cited it in her opinions on the Hungarian turnover taxes. She also suggested in those opinions in that the presence of discriminatory legislative intent could warrant stricter scrutiny of facially neutral classifications, a view that we explore at greater length in the next Part.

b) State Aid

The EU prohibition of state aid prevents Member States from distorting the common market by selectively subsidizing private taxpayers.[91] Although state aid and the fundamental freedoms overlap, there are many differences between the two in both scope and procedure. Most importantly for our purposes are that state aid and the fundamental freedoms protect different, albeit overlapping, classes.[92] Both legal rules prohibit states from taxing cross-border commerce less favorably than domestic commerce. But the state-aid rules go farther. They also prohibit states from favoring cross-border commerce over domestic commerce ("reverse discrimination"), and, importantly for our purposes, the state-aid rules arguably also forbid Member States to subsidize companies selectively based on their size.[93] Other differences divide the two areas of law and limit

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89 Case 171/78, *Commission v. Denmark*, *supra* note 16, at ¶ 36.

90 Likewise, in 1991 in *Commission of the European Communities v. Hellenic Republic*, another case involving the exemption of the national liquor (in Greece's case, ouzo), the Court stated in that "[a]lthough [the tax] does not establish any formal distinction according to the origin of products, it is *arranged* in such a way that all the national production of spirits falls within the most favourable tax category." *Supra* note 16, at ¶ 10 (emphasis added).

91 Article 107(1) of the TFEU ("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 favouring certain undertakings or the production of certain goods shall, in so far as it affects trade between Member States, be incompatible with the internal market").

92 For example, the fundamental freedoms forbid nationality discrimination, as does the prohibition of state-aid, But the prohibition of state aid arguable also prevents size discrimination itself, whereas the fundamental freedoms would only forbid size discrimination to the extent that it resulted in nationality discrimination as applied. *See, e.g., See* Ruth Mason, *An American View of State Aid*, 157 TAX NOTES 645 (2017) (arguing that state aid's "suspect classes," subsidization of which will garner strict scrutiny from the Commission, include sector, region, nationality, size, engagement in cross-border commerce, and individual aid).

93 *Id*. at 648-9.

the extent to which caselaw from one area can be transposed to the other.[94] Nevertheless, we think to the extent that prohibition of state aid and the fundamental freedoms have overlapping purposes—to prevent protectionism and maintain a level playing field among companies—state-aid cases can be useful by analogy to fundamental-freedoms analysis. Thus, we use state-aid cases in the same way that we used the Article 110 cases: not because we believe them to be controlling in fundamental-freedoms cases, but because they help shed light on how the Court of Justice might approach challenges to facially neutral rules that disproportionately impact foreigners.[95]

We begin with *Ramondin*, in which the Commission regarded a tax credit for large investments in certain tangible assets to be state aid because it selectively benefited "large investors" that were more likely to make qualifying investments. The lower EU court upheld the Commission's decision, but it based its decision on size discrimination, without connecting size discrimination to nationality discrimination.[96] Instead, the lower EU court held that "by restricting the application of the tax credit to investments in new fixed assets of over ESP 2 500 million, the Basque authorities *in fact* reserved the tax concession in question only to undertakings with significant financial resources."[97] The lower therefore held that the Commission did not err when it concluded that the tax credit was "*intended* to apply selectively to 'certain undertakings.'"[98] Thus, in *Ramondin* in reviewing indirectly discriminatory (selective) taxes, the lower EU court looked to both the impact of the classification and the intention of the Member State.[99]

No discussion of facially neutral rules that discriminate as applied would be complete without *Gibraltar*, a 2011 state-aid case.[100] *Gibraltar* was an interesting case because in it the Commission challenged a facially neutral (i.e., facially non-selective) tax regime. Instead of a more typical comprehensive corporate income tax regime, Gibraltar proposed to assess both resident and nonresident companies to tax based on their payroll and property in Gibraltar.[101] Even though the proposed regime nominally would apply the same way to all taxpayers and was

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[94] For example, the state-aid rules, but not the fundamental freedoms, prohibit individual aid. *Id*. The state-aid rules are not directly effective, and they are subject to many exceptions that do not apply to the fundamental freedoms. And so on.

[95] Again, we are not alone in thinking that fundamental freedoms and state-aid cases raise similar issues. *See, e.g.,* AG opinion in Vodafone*, supra* note 51, at ¶ ¶ 91, 101 (discussing fundamental-freedoms cases in her analysis of whether graduated turnover taxes constituted state aid).

[96] Joined Cases T-92/00 and T-103/00, *Territorio Histórico de Álava - Diputación Foral de Álava, Ramondín, SA and Ramondín Cápsulas, SA v. Commission of the European Communities*, ECLI:EU:T:2002:61, ¶ 24. State aid has more "suspect" classifications than do the fundamental freedoms. State aid's suspect classifications include, at a minimum, sector, region, nationality and size. *See* Ruth Mason, *An American View of State Aid*, 157 TAX NOTES 645 (2017).

[97] *Id.* at ¶ 39 (emphases added).

[98] *Id*.

[99] Although the decision was upheld by the CJEU, it could not rule on the substantive issue because of a procedural flaw. As stated by the Court (Second Chamber). Joined Cases C-186/02 P and C-188/02 P (Appeal), *Ramondín SA and Ramondín Cápsulas SA and Territorio Histórico de Álava - Diputación Foral de Álava v. Commission of the European Communities*, ECLI:EU:C:2004:702, ¶ 50.

[100] Joined Cases C-106/09 P and C-107/09 P, *Commission and Spain v. Government of Gibraltar and United Kingdom*, ECLI:EU:C:2011:732 [hereinafter, "Cases C-106/09 P and C-107/09 P, *Gibraltar*"].

[101] *Id.* at ¶ 21. The regime also included a registration fee that would be paid by all companies.

therefore facially neutral,[102] the Commission reasoned that the regime would confer state aid *as applied* because in practice it would favor offshore companies, which tended not to have payroll and property in Gibraltar, over onshore companies that tended to have property and payroll in Gibraltar.[103]

Spain intervened in the case to argue that the proposed regime was state aid because it was *de facto* selective. To support its argument, Spain claimed that that 28,798 out of 29, 000 of the undertakings established in Gibraltar would not pay taxes at all under it.[104] The United Kingdom did not directly refute these figures but raised doubts regarding their accuracy.[105] Both, the U.K. and Gibraltar responded that "the mere fact that some companies do not pay tax was not sufficient to conclude that their tax treatment is selective and to consider that those companies receive State aid."[106]

In upholding the Commission's decision, the Court of Justice acknowledged that the Gibraltar regime was facially neutral; it contained no *de jure* derogations favoring offshore companies. Nevertheless, the Court emphasized not only the effect of the proposed Gibraltar regime, but also Gibraltar's *intention* to discriminate. The Court concluded that the exemption of offshore companies was "not a random consequence" of the regime.[107] Rather than being random, exclusion of offshore companies was Gibraltar's intended result, "achieve[d]… by adjusting and combining the tax rules in such a way that their very application results in a different tax burden for different undertakings."[108] Frustrating Gibraltar's impermissible intent warranted, in the Court's view, adoption of a new judicial approach to identifying state aid; one that was not limited to finding state aid only in cases involving derogations from regularly applicable law. While the Court's use of intent in *Gibraltar* was remarked upon as a departure from its usual reliance on discriminatory impact,[109] our discussion in this Part shows that the Court regularly considers discriminatory intent in cases involving facially neutral rules.

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[102] *Id.* at ¶¶ 85-110.
[103] *Id.* at ¶ 106. Although the Commission did not define offshore companies, the term seems to apply to "letterbox" companies, companies formally incorporated in Gibraltar, but that did not have much substantive activity there. *Id.* at ¶ 17.
[104] *Id.* at ¶ 55.
[105] Gibraltar said that such estimates were difficult to make, but it noted that out of the 24 000 companies registered in Gibraltar, around 3 000 were already 'exempt' companies under the prior tax regime, approximately 260 were utility or financial services companies, and 18 000 were inactive companies holding assets. *Id.* at ¶ 64.
[106] *Id.*
[107] *Id.* at ¶ 106.
[108] *Id.* at ¶ 93.
[109] For an analysis of the notion of material selectivity after Gibraltar, *see* Raymond Luja, *Chapter 5: Material Selectivity after Gibraltar,* in *EU Income Tax Law: Issues for the Years Ahead* (D. (Dennis) Weber ed., IBFD 2013), Online Books IBFD (arguing that although the result of *Gibraltar* was unexpected, its affect is relatively limited). For a detailed analysis on Gibraltar, *see e.g.* Michael Lang, *Das Gibraltar-Urteil des EuGH: Neue beihilfe-rechtliche Vorgaben für das Steuerrecht?*, ÖSTERREICHISCHE STEUERZEITUNG 24, 593-600 (2011)*; see also* Conor Quigley, *Direct Taxation and State Aid: Recent Developments Concerning the Notion of Selectivity*, 40 INTERTAX 2, 112-119 (2012) (noting the same).

As Member States have increased their use of size classifications, the Commission has challenged several of them as conferring illegal state aid. For example, graduated turnover taxes, while facially neutral, may disproportionately favor small companies, domestic companies, or both.[110] In 2017, the Commission decided that a graduated retail gross turnover tax applied by Poland was state aid.[111] The Commission reasoned that the lowest rate (the zero bracket) in the graduated rate system was a favorable derogation from what it argued should have been a flat turnover tax.[112] As such, the exemption conferred illegal aid to select companies, namely those with lower turnover.[113] Although Poland argued that the rate structure was justified based on ability to pay and as a response to strategic income-shifting by multinationals, the Commission rejected Poland's claims, concluding that

> the Act taxes undertakings on the level of their turnover. As opposed to taxes based on profit, a turnover-based tax does not take into account the costs incurred in the generation of sales. Hence, turnover taxes hit companies in respect of their size rather than their profitability or ability to pay, their ability to generate efficiencies resulting from economies of scale, their ability to influence producers' and suppliers' margins to their own benefit, and their ability to exploit the tax optimisation strategies alleged by Poland. Consequently, none of those factors can constitute a justification for a progressive tax levied on an undertaking's turnover.[114]

Moreover, the Commission concluded that the Polish rule was "*specifically designed* to favour smaller retailers over larger ones by…subjecting undertakings with lower turnover to a lower average effective tax rate than undertakings with a higher turnover, which also tend to be foreign-owned."[115] Despite this hint that Poland intended the graduation in the turnover tax rate structure to effectuate nationality discrimination, the Commission on appeal clarified that it had not found the measure selective on the basis of nationality discrimination, [116] so the General Court on appeal did not consider whether the measure constituted covert selectivity on the basis of nationality.

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[110] C-323/18, *Tesco Global*, *supra* note 52; see also C-75/18, *Vodafone, supra* note 51 (noting the same).

[111] On The State Aid, SA.44351(2016/C) (ex 2016/NN), Polish Tax on the Retail Sector (June 30, 2017) C(2017) 4449 final [hereinafter "Commission Decision in Polish Turnover Tax Case"].

[112] Joined Cases T–836/16 and T–624/17, *Republic of Poland v. European Commission*, ECLI:EU:T:2019:338, ¶ 43 (hereinafter, "General Court Decision in Polish Turnover Tax Case") ("The Commission simply took the view that there should be only one tax rate"). In the Polish case, like so many other state-aid cases involving tax rates, the Commission faced the difficulty of determining what tax rate or rates ought to be regarded as part of the reference base system from which favorable derogations (i.e., state aid) could be measured. *See, e.g.,* Joined Cases C 164/15 P and C 165/15 P, *Aer Lingus*, ECLI:EU:C:2016:*990* (arbitrarily selecting one of the two rates in an dual-rate system to constitute the reference rate, which enabled the other to be characterized as an derogation that conferred state aid).

[113] General Court Decision in Polish Turnover Tax Case, *supra* note 112, at ¶ 68.

[114] Commission Decision in Polish Turnover Tax Case, *supra* note 111, at ¶ 58 (internal citations omitted).

[115] *Id.* at ¶ 47 (emphasis added). Commission Decision in Polish Turnover Tax Case

[116] General Court Decision in Polish Turnover Tax Case, *supra* note 112, at ¶ 101 ("…the Commission itself noted at the hearing with regard to proving the selective nature of the advantages entailed by the rate structure of that

On appeal the General Court held that there was no state aid; it rejected the Commission's reasoning that the rate variations in a graduated tax system necessarily confer state aid to companies in lower brackets.[117] The General Court held that the proper reference baseline for determining advantage was the state's actual tax regime, which included the rate structure, complete with exemption and any other brackets.[118] Since the graduated rate structure was baked into the reference baseline, Poland did not derogate from it when it imposed higher rates on higher turnover companies or when it exempted lower-turnover companies. The General Court also concluded that the Commission had not adduced sufficient evidence to show the connection between the graduation in the tax rates and company size, let alone company nationality.[119] The General Court added that even if foreign-owned companies comprised a disproportionate share of the highest-taxed companies, that could be "merely the corollary of the application of a progressive tax structure corresponding to the objective and general scheme of the tax in question,"[120] including Poland's redistributive goals.[121] Thus, the General Court understood the Commission's argument to be that graduated turnover taxes conveyed state aid per se;[122] and the court rejected that argument.[123]

Despite its general lack of receptiveness to the Commission's arguments, the General Court noted that if the Commission had "proven" that "the progressive taxation structure actually chosen was adopted in a manner which largely deprives the objective of the tax in question of its substance, it could be considered that the advantage which may be derived by undertakings benefiting from zero or low taxation compared with other undertakings is selective."[124] We read this to mean that if the Commission had shown that Poland structured its tax to be selective with the result that the

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tax, that the contested decisions had not been taken on the basis that discrimination on the ground of the *national origin of the taxable persons* had been identified.") (emphasis added).

[117] See generally General Court Decision in Polish Turnover Tax Case, *supra* note 112. A brief analysis on the General Court of 16 May 2019 can be found in: Leopoldo Parada, *EU loss in Polish State aid case may be a win for digital services tax,* MULTINATIONALS & TRANSFER PRICING NEWS (May 17, 2019). *See also* Leopoldo Parada, *Ayudas de Estado e Impuestos Digitales en Europa: Sentencia del Tribunal General en los Asuntos Acumulados T–836/16 y T–624/17* [State Aid and Digital Taxes in Europe: The EU General Court Decision in the Joined Cases T–836/16 and T–624/17], REVISTA ARANZADI UNIÓN EUROPEA 7 (2019). Appeals are pending.

[118] General Court Decision in Polish Turnover Tax Case, *supra* note 112.

[119] *Id.* at ¶ 47 (according to publicly available information of 200,000 operators, only about 100 were liable for tax, the remainder being exempt. 80% of the tax due would be paid by only 10 companies).

[120] *Id.* at ¶ 101 (also noting that even if franchisees experienced lighter tax under the Polish regime, both foreign and Polish companies were entitled to operate franchising structures).

[121] *Id.* at ¶ 76.

[122] *Id*. at ¶ 108 (noting that "the Commission held its view as a matter of principle, according to which view, in particular, progressive taxation applies to a turnover tax inherently fives rise to selective advantages"). *See id.* at ¶ 97 (noting that the Commission submitted only limited empirical evidence to support its claim that the Polish tax would not serve Poland's "redistributive purpose"); *Id.* at ¶ 92 (emphasis added Consequently, as regards a turnover tax, a variation criterion taking the form of progressive taxation above a certain threshold — even if that threshold is a high one — which may reflect the wish to tax an undertaking's activity only when that activity reaches a certain level, does not in itself imply the existence of a selective advantage

[123] *Id.* at ¶ 92 ("Consequently, as regards a turnover tax, a variation criterion taking the form of progressive taxation above a certain threshold — even if that threshold is a high one — which may reflect the wish to tax an undertaking's activity only when that activity reaches a certain level, does not in itself imply the existence of a selective advantage.")

[124] *Id.* at ¶ 94.

tax was selective as applied, the case would have been analyzed more like *Gibraltar*. At a minimum, the General Court might have more strictly scrutinized Poland's proffered justification for the tax, which was that Poland had adopted the graduated turnover tax rate regime in order to distribute the turnover-tax according to ability to pay. We consider ability-to-pay justifications for turnover taxes later, Part IV.

C. Conclusions

Our brief doctrinal review of company-size cases under the fundamental freedoms and cases in other areas of law that involved facially neutral classifications leads to some tentative conclusions. Most obvious is that classifications based on company size can raise serious discrimination concerns. Our conclusions are tentative for two reasons. First, there are simply not enough cases to allow us to reach confident conclusions. Second, the Court's reasoning has not always been consistent in them. This is most obvious in the French and Greek car tax cases, in which the Court arrived at opposite conclusions on the basis of very similar facts.

Need for evidence. First, unlike with cases involving facially suspect classifications, in cases involving facially neutral classifications, the Court does not accept on judicial notice that the neutral classification discriminates. That is no surprise. If the classification does not discriminate on its face, there must be some other evidence of discrimination—either of impact or intent or both. Discriminatory impact clearly matters. In every case, the Court either considered empirical evidence submitted by the parties—as when it considered the impact of the Spanish restrictions linked to physical-size—or it made informed conclusions about impact based on information provided by the parties about the market—as when it concluded that the French car tax discriminated because no French cars met the highest-tax engine-size requirement.

Quantum question. Second, although evaluating neutral rules that disproportionately impact foreigners calls for evaluation of the empirical correspondence of the facially neutral classification and the protected class of taxpayers, the quantum needed to find a violation is unclear. The standard for proxy discrimination that the Court used in *Hervis* and favorably cited in *ANGED* was not overly stringent. In the Court's view, the relevant question was whether *a majority* of those subject to unfavorable taxation were either foreign companies or linked to foreign companies.[125] In the Greek car tax case, however, the Court rejected the notion that a facially neutral classification indirectly violated Article 110, notwithstanding that to applied *exclusively* to foreign products. In her opinions in the Hungarian turnover-tax cases Advocate General Kokott argued that the Court should not propound an iron rule of fifty percent, and we agree. Indeed, we think it obvious that a tax classification does not discriminate simply because falls disproportionately, or even wholly, on foreign taxpayers. Kokott is right that such correlations can be purely coincidental. But eschewing a bright numerical standard presents the question of how the Court can distinguish discriminatory disproportionate impacts from merely incidentally disproportionate impacts.

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[125] *Hervis, supra* note 34, at ¶ 39.

Advocate General Kokott's opinion in the Hungarian turnover tax cases could be understood to support multiple different approaches to facially neutral classifications. One was to limit indirect discrimination analysis to proxies that *inherently* discriminate on the basis of nationality, that is, cases where the correlation between the classification and nationality can be discerned on the face of the statute, without appeal to statistics. This would be tantamount to ignoring nationality discrimination that arises from facially neutral classifications. Our difficulty in finding cases that involved truly facially neutral rules suggests that ignoring such cases would not do significant damage to the common market. On the other hand, announcing an intent to ignore facially neutral rules could motivate states that would like to discriminate on the basis of nationality to use such classifications more often. Moreover, while there may not be a super-abundance of facially neutral classifications that correspond well to nationality, our doctrinal analysis suggests that various company-size-based classifications correspond reasonably well to nationality.

Advocate General Kokott's opinions in *Hervis* and the Hungarian turnover-tax cases suggest another possibility: facially neutral rules could enjoy a presumption of legality, unless *as applied* they correlate with nationality in the "vast majority of cases."[126] Compared to the majority rule announced in *Hervis* and favorably cited in *ANGED*, a vast-majority rule would reduce the risk of false positives. But of course, it would not prevent them, and although Advocate General Kokott rightly warned that over-zealous review of facially neutral rules could infringe Member State tax sovereignty,[127] it seems to us that if a Member State rule indirectly discriminates, then the quantum of discrimination should not matter, just as it does not matter in direct discrimination cases. But if our argument about quantum is correct, it brings us no closer to a method for identifying discrimination that could be applied consistently in every case. We are not optimistic that a "one-size fits all solution" could be devised for such cases. We agree with Kokott that the *Hervis* majority-rule is over-inclusive. But her vast-majority rule is not necessarily better. While reducing false positives, it could increase false negatives. We see no clear alternative to case-by-case inquiries when evaluating facially neutral rules.

Finally, Advocate General Kokott suggested a third approach in her turnover-tax opinions. She suggested that legislative intent to discriminate could inform the Court's analysis. Considerations of intent factor into discrimination decisions under Article 110 and state aid, other areas of EU law that raise closely analogous questions to the fundamental freedoms. We discuss intent in Part III.

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[126] AG opinion in Hervis, *supra* note 37, at ¶ 41; see also AG opinion in ANGED, *supra* note 47, at ¶ 37 (noting the same); Julianne Kokott, *Facts and Law-Finding Issues in the Preliminary Ruling and Infringement Procedures before the ECJ in Tax Matters*, INTERNATIONAL TAX STUDIES 5, 4 (2019) (reinforcing the idea that a provision entailing indirect discrimination must affect foreign undertakings in particular, either intrinsically or in the vast majority of cases).

[127] Specifically, she expressed concern that "covert discrimination is not intended to extend the scope of the definition of discrimination, but only to include cases which do not constitute discrimination from a purely formal perspective, but have the same effect." AG opinion in Vodafone, s*upra* note 51, at ¶ 62.

Implications for Size Classifications. Our doctrinal analysis suggests that size classifications could constitute indirect nationality discrimination that violates the fundamental freedoms. Such claims would have to be supported with clear empirical evidence. Although we have argued that no single numerical standard could serve all cases, the most authoritative case we have, *Hervis*, suggests that the Court will find discrimination if a bare majority of those most adversely affected by the tax are foreign.[128] The CJEU tends not to take discriminatory intent into account in fundamental-freedoms cases, though it does so in other areas of law that afford protections similar to those offered by the fundamental freedoms. Advocate General Kokott's opinions in the pending Hungarian cases suggest a broader role for legislative intent, although her conception of how to prove such intent is very narrow, as the next Part explains.

III. Intent to Discriminate

The Court of Justice regularly emphasizes that what matters in discrimination cases is *effects*, not intent. Notwithstanding that consistent assertion, as Part II showed, the Court sometimes takes discriminatory intent into account, particularly in cases involving facially neutral rules. We argue that there are good reasons for the Court to give more weight to discriminatory intent as at least probative, if not dispositive, in indirect discrimination cases. Although we argue that use of intent is legitimate and could further the goals of the common market, we also raise potential objections to using intent, including that it would be difficult to prove.

Although this Part may seem like something of an aside in a larger discussion of company-size discrimination, it matters because there have been suggestions in the recent cases involving size classifications that states deliberately selected size thresholds to effectuate nationality discrimination.[129] Thus, if intent matters at all in judicial review of indirect discrimination cases, it will matter in company-size cases.

A. Using Intent

We see at least three ways that the Court could consider intent to discriminate in indirect discrimination cases: the Court could (1) ignore it, (2) use it to trigger impact analysis, or (3) use it to lower the quantum of impact required to establish nationality discrimination. Although intent may be relevant to indirect discrimination cases that employ facially suspect classifications, we focus exclusively on facially neutral rules. The Court readily disposes of cases involving facially suspect classifications by finding them discriminatory without the need for presentation of evidence. Thus, we do not suggest that intent ought to be an element of *every* indirect discrimination case.

[128] *Hervis, supra* note 34.

[129] *See* discussion *infra* Part III.A.2.

1. Ignore Intent

One possibility is that the Court could completely ignore evidence of intent. And, indeed, this is the path that the Court actually follows in almost all cases, and which it purports to follow in every case. Most cases can be judged without appeal to intent, for example because the state uses a facially suspect classification that obviously or intrinsically correlates with nationality. In such cases, the Court needs neither evidence of impact nor evidence of intent to find discrimination. Thus, establishing discriminatory intent is not a necessary component of every fundamental-freedoms case. On the other hand, in cases where the discriminatory effect is less clear, ignoring intent would seem to unnecessarily ignore relevant evidence.

Notwithstanding the Court's pronouncements that only effects matter, at least four reasons support considering Member States' *intent* to discriminate. First, evidence of intent to discriminate—and more precisely, protectionist or retentionist intent—is a helpful signal. It alerts affected parties and reviewing courts that a law or regulation may have discriminatory affects. Second, intent to discriminate matters because it undermines social and political cohesion within the EU. This is true even if, despite the legislature's intention, the enacted law does not disproportionately impact nationals from fellow EU states. Intentional discrimination sends the message that the state regards non-nationals as inferior or undervalued. Third, and related to our second argument, accounting for intent would further goals underlying the prohibition of nationality discrimination. A commonly accepted justification for nondiscrimination rules is that they protect disenfranchised (or otherwise politically ineffective) groups from politically powerful groups that would harm them without fear of political repercussions. When legislators express a desire to harm outsiders who lack voting rights or proxy representation in the taxing state, those expressions suggest that outsiders need protection. To the extent that eliminating nationality discrimination enhances the economic welfare of Europeans, using intent to identify discrimination likewise could further those economic goals. Fourth, and perhaps most relevant for our inquiry into size discrimination, any discrimination standard that relies exclusively on impact will face a line-drawing problem regarding the degree of impact needed to establish discrimination.[130] Thus, intent may impact the answer to what we have been calling the quantum question.

2. Use Intent to Trigger Impact Analysis

In her opinions in the pending Hungarian turnover tax cases, Advocate General Kokott suggested an alternative to ignoring intent. She argued that the Court should, in general, limit its review to facially suspect classifications.[131] Such a limitation would, in Kokott's view, pay proper respect to state tax autonomy. Many tax rules may apply disproportionately to nationals from other EU Member States, but most of the time, such disproportionate impacts are cause for alarm.

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[130] This is also true of Article 110 cases. See *supra* Section II.B.3.a.

[131] Facially suspect classifications are evident on "abstract" analysis, that is, without resort to statistical evidence. Tax residence would be the classic example—we do not need statistics to know that a classification based on tax residence will tend to apply differently to nationals and foreigners.

Net income taxes may, for example, disproportionately tax foreign companies because those companies may be more profitable than domestic companies due to the ability of multinationals to benefit more than domestic companies do from economies of scale and other firm benefits. As Kokott pointed out in the Hungarian turnover tax cases, the Court should not constantly second-guess Member States tax policy decisions simply because they happen to *incidentally* correlate with nationality.[132]

In contrast, evidence of the Member State's intent to discriminate calls into question what might be described as the presumption of legality of facially neutral rules. According to Advocate General Kokott

> the question arises whether a restriction of a fundamental freedom is also to be taken to exist where a distinguishing criterion — that is intrinsically not disadvantageous — was, in subjective terms, *intentionally chosen* to effect [sic] a high degree of disadvantage, in quantitative terms, for undertakings with generally foreign shareholders. To that end, *such an intention must be legally relevant*…[133]

Interestingly, Kokott argues that the Treaty's principle of sincere cooperation authorizes considerations of Member State intent.[134] Under this principle, Member States must faithfully apply and respect EU law, and they must refrain from jeopardizing the objectives of the Union. Therefore, Member States must not *intentionally* choose a criterion that disproportionately adversely affects nationals from other EU Member States.[135] In Kokott's view, the deference normally afforded to facially neutral rules should not apply in the face of evidence[136] of intent to disproportionately impact other EU nationals.[137] But Kokott would not consider intent to discriminate as sufficient to establish a violation of EU law. Instead, she would use it to trigger an inquiry into whether the neutral classification correlates with nationality in the "vast majority" of cases.[138] Only if the intentional discrimination resulted in the requisite effect would Kokott hold it to violate EU law.

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132 AG opinion in Vodafone, *supra* note 51, at ¶ 87; AG opinion in Tesco Global, *supra* note 51, at ¶ 83

133 AG opinion in Vodafone, *supra* note 51, at ¶ 84; AG opinion in Tesco Global, *supra* note 51, at ¶ 80 (emphasis added).

134 AG opinion in Vodafone, *supra* note 51, at ¶¶ 86-87; AG opinion in Tesco Global, *supra* note 51, at ¶¶ 82-83.

135 AG opinion in Vodafone, *supra* note 51, at ¶ 90; AG opinion in Tesco Global, *supra* note 51, at ¶ 86.

136 AG opinion in Vodafone, *supra* note 51, at ¶ 84; AG opinion in Tesco Global, *supra* note 51, at ¶ 80.

137 AG opinion in Vodafone, *supra* note 51, at ¶ 87; AG opinion in Tesco Global, *supra* note 51, at ¶ 83.

138 AG opinion in Hervis, *supra* note 37, at ¶ 38.

3. Use Intent to Answer the Quantum Question

We can think of at least one more way that the Court might tax intent into account: Evidence of discriminatory intent could be used to lower the evidentiary burden for proving disproportionate impact in cases involving facially neutral classifications.[139]

For example, while the Advocate General Kokott was justifiably reluctant to adopt an iron rule of majority-impact in *Hervis*,[140] evidence that a majority of the population harmed by a regulation is foreign is more probative when combined with evidence that the state intended to discriminate against non-nationals. In other words, even if disproportionate impact is an essential element of discrimination doctrine, combining an impact assessment with evaluation of the legislature's intent would seem to improve the Court's decision-making accuracy over impact assessment alone.

There are two main differences between this approach and the one Advocate General Kokott suggested in *Vodafone.* First, Kokott's approach includes a presumption of legality in the absence of evidence of intent to discriminate. A presumption of legality is warranted only if we think that in the absence of bad intentions, tax laws should not be regarded as discriminatory unless they use a facially discriminatory classification. In other words, unintentional but not "intrinsic" (i.e., facial) discrimination would presumably be permissible under Kokott's approach. Second, even in the face of evidence of intentional discrimination, Kokott would still find discrimination only if the facially neutral rule corresponded with nationality in the "vast majority" of cases.[141] But it seems to us that with sufficient evidence of bad intent, the Court would be warranted in finding discrimination even if the impact was not vastly disproportionate. Still, we do not pretend to know the magic number that ought to sustain a finding of discrimination. A case-by-case approach is not only appropriate, we regard it as unavoidable in indirect discrimination cases.

The approaches could also be combined—the Court could adopt Advocate General Kokott's presumption of legality and, after overcoming this threshold question, the Court could vary the quantum of impact needed to establish discrimination to account for evidence of discriminatory intent. Under any of these approaches, intent to discriminate would be relevant whenever a Member State used a facially neutral classification.

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139 Referring to an earlier draft of this paper, Professor Szudoczky notes that our "proposal may find – an admittedly rather implicit – support in the Court's judgment in *Hervis*. Although the Court did not refer to the intent of the legislature, it did emphasize the specific characteristics of the special tax, i.e. the steeply progressive rate on turnover especially in the upper band and the obligation to consolidate, which meant that group companies were taxed on a fictitious turnover. This emphasis could indicate that the Court had a suspicion that these rules were specifically designed to disadvantage group companies and thus, in turn, foreign-owned companies." Szudoczky, *supra* note 52, at 14.

140 Kokott argued that the fact that a "majority" of the companies affected by a discriminatory measure were non-resident/non-national was not be enough to show indirect nationality discrimination. In contrast, she concluded that the correlation between the use of thresholds and the seat of companies must be identifiable in the "vast majority" of the cases. AG opinion in Hervis, *supra* note 37, at ¶ 38.

141 AG opinion in Vodafone, *supra* note 51, at ¶¶ 84, 93-94.

B. Proving Intent

Parties typically prove discriminatory intent through the clear language of the statute, lawmakers' statements, and similar techniques.[142] We acknowledge the potential failings of these methods, including the difficulty or impossibility of ascribing a collective motive to legislatures comprised of individual lawmakers. Some commentators argue that intent can be inferred only from the clear language of the statute; on such a view, courts would not be permitted to consider legislative history or extra-statutory statements made by legislatures, governments, politicians, or officials. In cases like *Humblot* and *Gibraltar*; the Court did look to legislative history or statements by government administrators, instead, the Court discerned the intent to discriminate from the statute itself, reasoning that only the intent to discriminate could explain the particular provisions enacted into statute. On other views, more kinds of evidence would be admissible to establish discriminatory intent. Although resolving enduring questions about how to prove legislative intent lie outside the scope of this paper, to completely ignore evidence of intentional discrimination would be to ignore valuable information that could improve judicial decision-making.

As we noted in Part II, Advocate General Kokott regards intent to discriminate as relevant to judicial review under the fundamental freedoms, but she takes a very narrow view of what constitutes evidence of discriminatory intent. She argued in *Vodafone*:

> there must be clear evidence that disadvantaging foreign companies was the primary objective of the measure which was perceived and endorsed as such by the Member State (and not merely individuals involved), and there also cannot be any other evident objective reason for the option chosen.[143]

This view of establishing intent is unnecessarily restrictive.[144]

First, the advocate general gives no reason why discrimination is only illegal if discrimination was the "primary objective" of the measure and there is no other evident reason for the classification. When a tax rule both discriminates and achieves other objectives, the Court typically considers whether the other reasons justify the use of the discriminatory criteria. It is simply unclear why the standard should be different for facially neutral rules. Moreover, Advocate General Kokott's phrasing would seem to suggest that EU law permits a Member State to intentionally use a discriminatory classification, which classification results in discrimination as

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[142] *See* Richard H. Fallon, Jr., *Constitutionally Forbidden Legislative Intent*, 130 HARV. L. REV. 523 (2016)*; see also* Case C-310/98, *Hauptzollamt Neubrandenburg v Leszek Labis and Sagpol SC Transport Miedzynarodowy i Spedycja*, ECLI:EU:C:2000:154, ¶ 29 (holding in a case involving establishing where a customs duty offense occurred that in the absence of relevant EU legislation "governing the concept of proof, any type of evidence admissible under the procedural law of the Member States in similar proceedings is in principle admissible.").

[143] AG opinion in Vodafone, *supra* note 51, at ¶ 92. This is repeated in her opinion in *Tesco-Global* too. *See* AG opinion in Tesco-Global, *supra* note 52, at ¶ 88.

[144] One of us has already criticized Kokott's approach as overly restrictive, and we supplement those views here. Leopoldo Parada, *How the Vodafone Magyarország Opinion Affects EU Debate on Turnover-Based Digital Taxes*, 95 TAX NOTES INT'L 399 (2019).

applied, and the Member State still would not violate EU law so long as its "primary motivation" was something other than discrimination or there was some other "evident objective" for the classification. Such a standard would seem to unnecessarily accommodate intentional nationality discrimination, including in cases where such intentional discrimination has vastly disproportionate impacts.

Second, Advocate General Kokott's requirement that discriminatory intent must be "perceived and endorsed as such by the Member State (and not merely individuals involved),"[145] strikes us as so stringent that it rules out consideration of intent except as evidenced through the statute itself. Although we readily agree that that there are difficulties in establishing legislative intent, it is unclear why the motives of individual lawmakers should never be considered. It is equally unclear why, in addition to evidence of legislators' intent to discriminate, proof of impermissible intent must also be available from government documents. Demonstrating how stringent her standard is for establishing intent, in the Hungarian turnover-tax cases Kokott declared that evidence from parliamentary debate in Hungary and other governmental documents, such as explanatory legal memorandums, were insufficient to establish discriminatory intent.[146] Troublingly, Advocate General Kokott's standard sets forth a clear roadmap for states that want to discriminate on the basis of nationality by using facially neutral classifications: they should be sure to include a nondiscriminatory purpose somewhere in the law or legislative history, which inclusion would seem to *immunize* the tax from challenge as indirect discrimination.[147]

C. Conclusions

In cases involving facially suspect classifications, intent to discriminate typically plays no role. This does not mean that intent is irrelevant as a matter of law in cases involving facially suspect classifications, but rather that the Court typically does not reach questions of discriminatory intent in such cases. Intent appears to be superfluous in cases involving facially suspect classifications for two reasons. First, considerations of intent seem to be entwined with the quantum question in cases involving facially neutral classifications, but not facially suspect classifications. Because the CJEU essentially takes a strict liability approach in cases involving facially suspect classifications, it typically does not consider quantum, that is, the degree of impact of the classification on non-nationals. Second, in cases involving facially suspect classifications, legislative intent to discriminate readily can be inferred from the text of the statute itself, without need to appeal to empirical impact or statements by officials.

In contrast, in cases involving facially neutral classifications, discriminatory intent seems to matter. We offered three alternatives ways to use discriminatory intent to help resolve cases involving facially neutral classifications. We argued that the first option—ignoring discriminatory intent—would be wrong. It could harm the common market, and it would abdicate the Court's

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145 AG opinion in Vodafone, supra note 51, at ¶ 92.

146 *Id.* at ¶ 94. *Id.* at ¶ 19 (rejecting evidence of intentional discrimination that came from government sources, rather than legislative sources, on the grounds that "[s]ince the government is normally bound by the parliament's decision, and not vice versa, I also have reservations over having regard to individual government documents").

147 Parada, *supra* note 138, at 403 (providing a similar example as regards the Spanish DST).

responsibility to safeguard the fundamental freedoms through judicial review. We were more equivocal between the other two options, which we see as similar. One possibility—suggested by Advocate General Kokott in *Vodafone*—is to use intent as a threshold question. The Court would presume all facially neutral classifications are legal except in cases involving discriminatory intent. The presence of discriminatory intent would trigger disproportionate-impact analysis. Advocate General Kokott's approach has the virtue of providing a safe harbor to Member States, who could be confident that their tax laws would not be regarded as discriminatory merely because they used a classification that coincidentally, even if very highly, correlated with nationality.

Another possibility is that rather than serving as a threshold that triggered disproportionate-impact analysis, evidence of intent could be used to lower the quantum of disproportionate impact needed to make out a discrimination claim. The virtue of this approach—which makes it distinct from Advocate General Kokott's approach—is that impact-only cases involving facially neutral rules could proceed even in the absence of evidence of discriminatory intent. In such cases, absence of discriminatory intent would mean that the quantum for finding discrimination on the basis of disproportionate impact would be higher.

The main problem with both of the approaches that consider intent is that they cannot specify the quantum—the degree of impact—needed to prove discrimination. Although it makes sense to require a smaller impact in a case where there is evidence of discriminatory intent, cases involving facially neutral classifications require case-by-case analysis. Still, taking discrimination into account rather than ignoring it better represents extant doctrine, should improve the accuracy of judicial review by reducing false negatives, and seems truer to the Court's obligations to prevent violations of the fundamental freedoms.

IV. Justifications for the Use of Company-Size Classifications

Differences in treatment, even if they coincide with nationality, are permissible as long as they apply to taxpayers in different situations. EU law forces states to treat likes alike, but it permits states to treat unalikes differently. Differences in treatment also can be justified on grounds of public policy, public security, or public health.[148] The CJEU has accepted some justifications for discrimination, including, for example, the need to maintain fiscal cohesion, prevent fraud, and administer the tax system.[149] Likewise, the Court has accepted the need for "balanced allocation" of taxing rights, which helps justify states' adherence to international tax laws, such as allocation rules designed to prevent double taxation that are memorialized in tax treaties.[150] Thus, even if the CJEU were to accept that company size proxies nationality, it is still possible that treating taxpayers differently based on their size could be consistent with EU law. The Court construes justifications narrowly, and to be justified, a discriminatory provision must be proportional, that is, it must be no more discriminatory than necessary to achieve the legitimate public policy goal.[151]

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[148] Article 52 of the TFEU.

[149] *See* RUTH MASON, PRIMER ON DIRECT TAXATION IN THE EUROPEAN UNION 93-108 (2005).

[150] *See, e.g.,* Case C-446/03, *Marks & Spencer plc v. Halsey*, ECLI:EU:C:2005:763.

[151] *See* Case C-134/15, *Lidl GmbH & Co. KG v. Freistaat Sachsen*, EU:C:2016:498, ¶ 33; Case C-189/01, *Jippes and Others*, C-189/01, EU:C:2001:420, ¶ 81; Case C-283/11, *Sky Österreich*, EU:C:2013:28, ¶ 50.

This Part briefly analyzes what we regard as the most promising potential justifications for classifications based on company size, namely public policy, administrability, ability to pay, and ensuring single taxation. We think that most size-based classifications can easily be justified, but that such justifications become harder when there is evidence of intentional nationality discrimination.

A. Public Policy

Justifications may be available when company size itself is a particular source of the harm the state hopes to avoid with the challenged regulation.[152] For example, in *ANGED* in addition to considering whether the tax on physically-large retailers constituted a restriction of the freedom of establishment, the Court of Justice also considered whether the tax constituted illegal state aid to smaller retailers.[153] The Court held that there was no state aid; the higher tax was meant to ameliorate traffic problems from larger retailers, and larger retailers uniquely generated traffic and other environmental impacts.[154] Particularly if there were no evidence of intentional nationality discrimination, one could imagine the Court accepting an car-engine-size classification if the state's goal for the classification had been to reduce pollution, since larger engines produce more pollution. In the same vein, regulatory burdens that apply disproportionately with company size could be justified when company size itself generates special risks, other externalities, or otherwise constitutes a particular source of a public harm. Thus, public policy reasons could justify size-based reserve requirements, insurance requirements, and the like, even if those requirements, as applied, disproportionately impact foreign companies. Note, however, that to be acceptable, the measure must not be more discriminatory than necessary to must achieve the public policy goal.

B. Administrability

Another promising justification for size-based classifications is administrability. Excusing small companies from certain tax obligations could be justified because compliance imposes too high a burden on either small companies or the tax administration relative to the tax collected from those small companies. Our assumption is that most size thresholds are chosen in an arbitrary manner. The threshold in the proposed CCCTB is €750 million in global income, but there is probably no convincing reason that it should not have been €740 or €760 million. It would place too high a burden on states to have to defend the exact place where they drew the line for

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152 *Maine v. Taylor*, 477 U.S. 131 (1986) (holding that the baitfish import ban was discriminatory but justified and narrowly tailored; foreign baitfish were a particular source of the fish parasites the state sought to protect against). Another option would be to argue that the large companies are "not comparable" to their smaller competitors.

153 Case C-234/16, *ANGED*, *supra* note 46, at ¶ 55 (approving a tax on large retailers in the state-aid context because larger retailers were a particular source of the harm sought to be avoided, namely environmental impacts from traffic).

154 *Id.* at ¶ 45 (holding purpose of the tax was "to correct and counteract the environmental and territorial consequences of the activities of these large retail establishments, deriving, inter alia, from the ensuing rise in traffic flows, by having those establishments contribute to the financing of environmental action plans and making improvements to infrastructure networks").

administrative reasons.[155] Still, size thresholds should be grounded by a genuine administrative concern; they should not be chosen for their discriminatory effects.[156] Thus, we would assume that nearly any size threshold that was actually selected for administrative reasons could be justified. Such administrative justifications could include additional reporting requirements on large companies, additional tax obligations related to having a certain number of employees, and so on.

The analysis changes when the size threshold was not chosen for reasons genuinely related to administrative concerns. Even if readers disagree with us that intent should form part of the discrimination stage of judicial review, it is clear that intent already forms part of the justification stage of judicial review for discrimination, because an essential aspect of justification analysis is to identify the purpose or object of the challenged rule. If a purpose was nationality discrimination, we would expect that this impermissible purpose would influence the Court's justification analysis, even if the size threshold also serves administrative goals. Thus, as Part V explains at greater length, we see a significant difference between digital services taxes, for which the threshold was chosen specifically to impact the nationality composition of the tax,[157] and more run-of-the-mill size-based classifications.

C. Ability to Pay

Another auspicious basis for justifying size discrimination is ability to pay. Classifications based on the size of a company's profits, including those needed for progressive income taxes, either do not discriminate in violation of EU law, or any discrimination that arises from them is justified. Multinationals may, on average, have more net income than domestic companies due to, for example, economies of scale.[158] Classifications based on net income, including progressive tax rates, could, as applied, impose higher burdens on foreign companies.[159] In our view, a genuine goal to tax on the basis of ability to pay would justify such discriminatory effects. Obviously, the stronger the connection between the size classification used by the state and ability to pay, the more likely the CJEU would be to find the classification justified for ability to pay reasons. Thus,

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155 AG opinion in Vodafone, *supra* note 51, at ¶ 99 (noting that whether the rate bracket "is the 'best'. . .or another amount would. . .have been 'better' is a decision for the national legislature which cannot be reviewed by either the Court or the Commission, unless there is abuse;" she regards *intentional* nationality discrimination as abuse).

156 Member States concerned about the potential discriminatory impact of size threshold could conduct impact studies of the administrative issue that concerns them (e.g., cost of compliance), which studies could help support their chosen threshold.

157 *Commission Staff Working Document Impact Assessment,* COM (2018) 147 final (March 21, 2018), at 68 (considering how various revenue thresholds would affect the composition of the taxable populations).

158 Ronald H. Coase, *The Nature of the Firm*, 4 ECONOMICA 386, 387, 390–91 (1937).

159 This would raise Advocate General Kokott's criticisms about the correct way to measure such effects. Is the relevant question whether foreign companies pay more absolute tax than do domestic companies? Is it whether foreign companies comprise a disproportionate share of those taxable in the highest bracket? If the latter, what do we mean by disproportionate? Is the question whether foreigners comprise a majority of those in the highest bracket, or is the question whether foreign companies represent a disproportionate share of the highest taxed relative to their incidence in the host state? Or should some other measure of disproportionate govern? We have argued that such questions must be resolved in context on a case-by-case basis.

we agree with the reasoning of the Court of Justice in *Gibraltar* when it confirmed that taxes on profits did not impermissibly subsidize companies that had losses.[160]

But the less tenuous the connection between the classification and ability to pay, the harder it becomes to justify the classification on ability to pay grounds. States have tried to justify graduated[161] net (and even gross) turnover taxes on the basis of their desire to impose taxes consistently with ability to pay. For example, the General Court recently observed that even if Poland's graduated gross turnover tax had disproportionately affected foreign companies (a fact not established in the case), that impact would have been justified by the "redistributive purpose" of the tax.[162] The General Court thought that higher taxes on companies with higher turnover could effectuate redistributive goals because

> It may reasonably be presumed that an undertaking which achieves a high turnover may, because of various economies of scale, have proportionately lower costs than an undertaking with a smaller turnover — because fixed unit costs (buildings, property taxes, plant, staff costs for example) and variable unit costs (raw material supplies for example) decrease with levels of activity — and that it may, therefore, have proportionately greater disposable revenue which makes it capable of paying proportionately more in terms of turnover tax.[163]

While it is no doubt true that high turnover may coincide with higher ability to pay, it is equally clear that it need not do so. As far as we know, the Commission adduced no evidence showing that high-gross-turnover companies were not also high-income companies, such that taxing high-turnover companies more than low-turnover companies would not fulfill Poland's purported "redistributive purpose."[164] Nevertheless, it is inconsistent with the Court's generally narrow view of justifications for it to accept an unproved assumption about a class of taxpayers (e.g., they have more income) to justify discriminating against them.[165]

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[160] Cases C-106/09 P and C-107/09 P, *Gibraltar*, *supra* note 98, at ¶¶ 80, 84; *see also* C-143/99, *Adria-Wien Pipeline and Wietersdorfer & Peggauer Zementwerke*, EU:C:2001:598, ¶ 35 ("A State measure which benefits all undertakings in national territory, without distinction, cannot therefore constitute State aid.").

[161] We regard as "progressive" taxes that increase with ability to pay, as measured by a meaningful proxy, such as net income. We do not regard gross turnover as a meaningful measure of ability to pay; we therefore refer to taxes that increase with gross turnover as "graduated" rather than "progressive."

[162] General Court Decision in Polish Turnover Tax Case*, supra* note 111, at ¶ 76.

[163] Id. at ¶ 75.

[164] The burden of proof to show selective advantage is on the Commission in state-aid cases. Although the Commission observed that the Polish graduated turnover tax could more heavily tax high-turnover companies with losses than low-turnover companies with profits, it offered no evidence of this claim in the Polish case. General Court Decision in Polish Turnover Tax Case, *supra* note 112, at ¶ 49. Had it adduced such evidence, the Commission may have been more successful in challenging Poland's purported tax objective, namely, a "redistributive purpose." *Id.* at ¶ 15.

[165] *See, e.g.,* Case 279/93, *Finanzamt Köln-Altstadt v. Roland Schumacker.* ECLI:EU:C:1995:31 (rejecting such a justification in the cross-border work context).

Similarly, we are not persuaded by Advocate General Kokott's analysis in the recent Hungarian net-turnover tax cases.[166] Unlike the Polish graduated turnover tax, which was based on gross turnover, the Hungarian graduated turnover tax was based on *net* turnover.[167] The Hungarian net turnover tax therefore is more likely than the Polish gross turnover tax to capture ability to pay. Still, there are problems with using net turnover to measure ability to pay. As Advocate General Kokott noted, "volume of turnover"[168] is "not a compelling indicator for financial capacity."[169] But Advocate General Kokott also noted, as she had in *Hervis*, that "high profits are not actually possible without high turnover."[170] Kokott accepted Hungary's use of net turnover to determine tax rates as justified for ability-to-pay reasons, in part because no measure of ability to pay was perfect, not even net income.[171]

Although Kokott is correct that net income is not a perfect measure of ability to pay, that observation seems beside the point in an inquiry aimed at determining whether the state used the least discriminatory means to achieve its goal.[172] If net income taxation or proportional turnover taxation would achieve the state's goal to tax based on ability to pay as well or better than graduated turnover taxation, but with less discrimination, then the state is not entitled to use the more discriminatory option. Taxation based on ability-to-pay as measured by net corporate income is a widely recognized principle among Member States, achieving constitutional status in some of them.[173] The notion that net (or in the case of the Polish tax, gross) turnover could adequately measure economic capacity or ability to pay enjoys no such widespread support. This should come as no surprise, as turnover taxes are not designed to measure ability to pay. This is

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[166] AG opinion in Vodafone, *supra* note 51, at ¶ 100.
[167] Id. at ¶ 109.
[168] AG opinion in Vodafone, *supra* note 51, at ¶ 110.
[169] *Id*. at ¶ 100.
[170] *Id*. at ¶ 121. AG opinion in Hervis, *supra* note 37, para. 61. *See also*, Kokott, *supra* note 121, at 5. That Kokott's argument that "high profits are not actually possible without high turnover" applies equally well to gross turnover and to gross income should help us reject her argument and the faulty reasoning that underlies it.
[171] AG opinion in Vodafone, *supra* note 51, at ¶ 110 (turnover is "an indicator of a certain ability to pay") *Id*. at ¶¶ 122-3 (imperfection of net income); *Id*. at ¶ 182 ("…income taxation based on profit is not the only correct ('normal') form of taxation, but merely a technique for mathematically determining and taxing the taxable capacity of the taxable person in a uniform manner…"). *See also* AG opinion in Tesco-Global, *supra* note 52, at ¶ 166 ("Contrary to the view apparently taken by the Commission, and as the General Court has also recently ruled, proportional income taxation based on profit is not the only correct ('normal') form of taxation, but merely a technique for mathematically determining and taxing the taxable capacity of the taxable person in a uniform manner.").
[172] Likewise, we do not know how Advocate General Kokott derived the standard she applied in *Vodafone.* She seemed to conclude that any tax that the state purports to be aimed at ability to pay and fair distribution of the tax burden is proportionate, unless it has "a choking effect and is thus tantamount to a prohibition on the taxed activity." AG opinion in Vodafone, *supra* note 51, at ¶ 131. Such a *choking* standard would vitiate proportionality.
[173] For example, in Germany the ability-to-pay principle is specifically recognized in Article 3 of the German Constitution, which grants equal treatment to taxpayers in similar circumstances, including corporations. This recognition of an entitlement to ability-to-pay taxation in the case of corporations is known as the "objective net principle." *See* Werner Haslehner, *EU and WTO Limits on Digital Business Taxation,* in: Werner Haslehner et al., *Tax and the Digital Economy: Challenges and Proposals for Reform*, Kluwer Law International, Alphen aan den Rijn (2019) (arguing that even though digital turnover-based taxes were not designed to reach only foreign taxable persons, the progressive tax on turnover does not comport with the ability-to-pay principle).

not to condemn turnover taxes; it is simply to recognize that it is unlikely that graduated turnover taxes could be justified on the basis that they measure ability to pay, which is something they are not designed to do.

In sum, we think that size classifications could be justified by ability-to-pay reasons. The most obvious example is size of net income. Such a size-based classification, even if it resulted in the highest tax rates being imposed on disproportionately foreign companies, would plainly be justified. But the more attenuated the connection between the classification and ability to pay, the harder it will be for a Member State to justify its classification. Net turnover is harder to justify than net income (which concept was invented to measure ability to pay); gross turnover is harder to justify than net turnover, and indeed, in our judgment, cannot be justified for ability-to-pay reasons. Gross turnover is not designed to, and does not, measure economic capacity or ability to pay for purposes of redistribution any more than a gross income tax would. Importantly, if the CJEU is to faithfully discharge its obligation to review Member State laws for consistency with the fundamental freedoms, it must not simply accept any justification proffered by the challenged state, no matter how improbable and how far removed from the state's actual reason for enacting a provision.

D. Ensuring Single Taxation

The Court of Justice recognizes that avoiding double taxation is an important policy goal for the states, and it defers to the states as to how to allocate income from cross-border commerce.[174] Presumably, in a post-BEPS era, the Court of Justice will increasingly recognize the importance of ensuring single taxation, although neither avoiding double taxation nor ensuring single taxation would seem to be a result demanded by the TFEU.[175]

It is possible that states would argue that size-based classifications help ensuring single taxation. Indeed, Advocate General Kokott considered a BEPS-based defense for the disproportionate impact on foreign companies effectuated by Hungary's graduated net turnover tax regime. She argued that states could reasonably conclude that higher turnover taxes for multinational companies serve as a counter to those companies' greater access to profit shifting opportunities under net income taxes.

There are a couple of ways we could understand this line of argument. One is that higher turnover taxes on multinationals compensates for lower income taxes on multinationals. States have not had success in the past when they tried to justify discriminatory taxes imposed on foreign

174. Case C-513/04, *Mark Kerckhaert and Bernadette Morres v. Belgische Staat*, ECLI:EU:C:2006:713, ¶ 22.

175 *Id.; see also*, Leopoldo Parada, *Double Non-Taxation and the Use of Hybrid Entities: An Alternative Approach in the New Era of BEPS*, KLUWER LAW INTERNATIONAL, ALPHEN AAN DEN RIJN, 51 (2019) (expressing skepticism about the global importance of ensuring single taxation and arguing that double non-taxation is a vague concept that should not be "regarded per se as a cause of concern").

companies as helping to balance out tax advantages that were disproportionately available to foreign companies.[176]

Another way of thinking about this argument that is truer to how Advocate General Kokott seems to intend it is that each state is entitled to choose the "tax mix" it prefers, and one reason a state might employ a turnover tax in addition to (or in lieu of) a corporate net income tax is that the turnover tax is less avoidable. In particular, it is less avoidable by multinationals through profit shifting.[177] Kokott noted Hungarian legislative history showing Hungary's intent to "avoid non-taxation of high-turnover undertakings which did not contribute to corporate tax revenue in Hungary or did so only very little…."[178] That turnover taxes could be helpful in insuring taxation of companies that have greater access to profit shifting under the income tax strikes us as correct, but in need of one more analytical step. A further question must be asked, namely, is the discriminatory measure narrowly tailored to address the state's legitimate interest?[179] Discrimination against high-turnover companies to compensate for gamesmanship by multinationals does not seem proportionate, at least not without a firmer link between the two.

Moreover, a 1998 case, *ICI*, suggests that the Court will closely scrutinize size-based classifications when states purport to justify them by the need to combat profit shifting.[180] The Court of Justice in *ICI* held that the United Kingdom violated its own residents' freedom of establishment when it denied them group relief unless a majority of their subsidiaries were established in the United Kingdom.[181] Although it is clear that smaller, domestically headquartered groups would have an easier time satisfying such a majority requirement than would larger, foreign-headquartered groups with more subsidiaries in more countries, the Court did not focus on size-based discrimination in finding a fundamental-freedoms violation. Instead, it relied

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176 *See, e.g.,* Case C-294/97, *Eurowings Luftverkehrs AG v. Finanzamt Dortmund-Unna*, ECLI:EU:C:1999:524 (holding that Germany could not tax foreign companies more on their German activities to make up for the fact that those companies were taxed less in Ireland, their home state). To be justified such compensatory tax must be expressly conditioned on the offsetting tax benefit. *See, e.g.,* Case C-204/90, Bachmann v. Belgium, ECLI:EU:C:1992:35 (holding that a disadvantage was permissible because it was offset by a linked tax advantage).

177 The OECD has criticized turnover taxes as a response to BEPS activity, because they are "likely to generate some economic distortions, double taxation, increased uncertainty and complexity, and associated compliance costs for businesses operating cross-border and, in some cases, may potentially conflict with some existing bilateral tax treaties." *OECD/G20 Base Erosion and Profit Shifting Project Tax Challenges Arising from Digitalisation – Interim Report 2018 Inclusive Framework on BEPS*, OECD Publishing, 159, ¶ 368 (2018). Likewise, the OECD recognized the legal constrains that may apply to taxes tied to size. See OECD, *Programme of Work to Develop a Consensus Solution to the Tax Challenges Arising from the Digitalization of the Economy*, OECD Publishing, 17, ¶ 37 (2019).

178 AG opinion in Vodafone, *supra note* 51, at ¶ 181.

179 Case C-196/04, *Cadbury Schweppes Overseas Ltd v. Commissioners of Inland Revenue*, EU:C:2006:544 [hereinafter "Case C-196/04, *Cadbury Schweppes*"].

180 Case C-264/96, *Imperial Chemical Industries plc (ICI) v Kenneth Hall Colmer (Her Majesty's Inspector of Taxes)*, ECLI:EU:C:1998:370, ¶ 26.

181 *Id.* at ¶ 21.

on the facially suspect classification, residence of the subsidiaries.[182] But the Court did address the size issue in the justification stage of the inquiry. The United Kingdom argued that its majority-British rule was needed to combat profit-shifting opportunities available to groups with foreign subsidiaries.[183] The Court of Justice, however, held that the majority rule was not a proportionate response to that risk. Because the risk of profit-shifting arose if even one subsidiary was foreign, denying loss offsets only when a majority of the subsidiaries was foreign would not serve the United Kingdom's stated purpose.[184] *ICI* suggests that the Court's will closely scrutinize the fit between size thresholds and claimed justifications, making it harder to pass off rules intended to favor domestic companies as anti-abuse rules.[185]

Thus, Kokott's observation that multinational companies may artificially reduce their net income, while true, seems irrelevant to the question of whether a state can enact a *discriminatory* turnover tax in response. States define net income in the way that they regard as best capturing ability to pay. If a Member State thought that its own income tax did not adequately capture ability to pay, then the obvious solution would be for it to amend its income tax rules, not to adopt a discriminatory turnover tax that performs even worse at measuring ability to pay. Indeed, Hungary has undertaken such income tax reforms under BEPS, a development about which Advocate General Kokott is clearly aware. If a state wants to rely less on ability-to-pay taxation and more on turnover taxation, that is also permissible under the fundamental freedoms. What the state must not do, however, is use its turnover tax to covertly discriminate against residents of other EU Member States. The turnover-tax cases therefore are not—despite how Advocate General Kokott frames them—about whether a state is allowed to use turnover taxes (or equivalently, whether it is forced to use income taxes), but rather, those cases are about whether a state that chooses to have a turnover tax can implement it in a discriminatory way. Turnover taxes are plainly permissible, but unjustifiably discriminatory turnover taxes are not. A principle justification that states have offered for graduated turnover taxes is that multinationals have greater access to avoidance techniques under the income tax. But if such a justification is acceptable without further proof of the link between the companies benefiting from income shifting and the companies subject to higher turnover taxes, one wonders what, if anything, would prevent a state from adopting a graduated turnover tax whose highest rate applies *expressly* to multinationals, while exempting domestic companies. If the tax-avoidance justification would not succeed in the overt discrimination context, why should it succeed in the indirect discrimination context?

V. Example: Digital Services Taxes

Applying our doctrinal and normative analysis from Parts II and III, we now consider whether digital services taxes (DSTs) constitute indirect nationality discrimination under the fundamental freedoms, and, if so, whether they can be justified. DSTs employ two types of facially

[182] *Id.* at ¶ 22.
[183] *Id.* at ¶ 25.
[184] *Id.* at ¶ 27.
[185] As does the Court's close scrutiny of facially suspect anti-abuse rules that Member State defended by arguing that they were needed to combat profit shifting. *See, e.g.,* Case C-196/04, *Cadbury Schweppes, supra* note 173.

neutral classifications that correspond with nationality, namely particular kinds revenue streams[186] and turnover size. Both of these classifications are problematic and can lead to nationality discrimination, but in keeping with the theme of this Article, in this Subpart we mainly focus on turnover-size.

Under the DST proposed by the Commission, and under various unilateral DSTs that were modeled on the Commission proposal, only companies with €750 million in gross turnover would be subject to tax. DSTs typically require groups to aggregate their global turnover for purposes of triggering the DST threshold.[187] These high revenue triggers ensure that only very large, and therefore disproportionately foreign, companies pay digital taxes. The Commission set the €750 million gross turnover threshold with the aim of taxing principally U.S.-headquartered companies,[188] and Member States copied that threshold into their unilateral proposals. The problem is that, when enacted unilaterally, the burden of DSTs will fall on the EU subsidiaries of U.S.-headquartered companies. To the extent that these EU subsidiaries are established outside of states enacting DSTs, those states may disproportionately tax companies residing in other EU Member States.[189] The turnover triggers are facially neutral; they formally burden neither nationality nor familiar proxies for nationality such as tax residence. Nevertheless, we can expect that for all or nearly all EU member states enacting unilateral DSTs, the taxable population would be predominately or even exclusively foreign. Moreover, domestic companies that manage to surpass the revenue triggers are likely to be foreign-parented, rather than domestic-parented.[190] Although states have not released much empirical analysis of the expected nationality composition of the taxable population for DSTs, there simply do not exist very many domestic digital companies that have such high turnover. Most of those companies are U.S. parented, but their EU subsidiaries—which are fully entitled to protection under the TFEU—would be liable for digital taxes.

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186 Digital services taxes only apply to turnover from specified activities, such as selling online advertisements, selling user data, or providing an online two-sided marketplace like AIRBNB. PROPOSAL FOR A COUNCIL DIRECTIVE ON THE COMMON SYSTEM OF A DIGITAL SERVICES TAX ON REVENUES RESULTING FROM THE PROVISION OF CERTAIN DIGITAL SERVICES, COM (2018) 148 final (March 3, 2018) [hereinafter "EU DST PROPOSAL"].

187 This means that DSTs have the same infirmity examined in *Hervis*—the aggregation rule disproportionately adversely impacts groups, and it likely disproportionately adversely affects cross-border groups as compared to domestic groups. The *Hervis* court ruled that the national court should determine whether the aggregation rule as applied disproportionately burdened cross-border groups, because if it did, the rule would violate the fundamental freedoms. The Court would presumably reason analogously about DSTs. DSTs may violate EU law in other ways, see Ruth Mason and Leopoldo Parada, *Digital Battlefront in the Tax Wars*, 92 TAX NOTES INT'L 12, 1190-1192 (2018) (arguing that DSTs could constitute state aid).

188 *Id.* at 1185-1186.

189 *Id.*

190 Although the Spanish government did not publish empirical analysis of the expected effects of the tax, it concluded that the tax would "mainly… affect multinational companies." *Memorandum of the Regulatory Impact Analysis of the Law XX/2018, of XX of XX, on the Digital Service Tax* (translation by the authors)], at 21 [hereinafter, "Spanish DST Impact Analysis"].

To take a specific example, out of a total of 29 companies it expects to be liable for DST, France estimates that only one will be French.[191] This impact far exceeds the majority rule that the CJEU applied in *Hervis*. Thus, if the Court sticks to the majority rule, it presumably would conclude that the French DSTs is discriminatory.

How, if at all, the Court of Justice would take into account evidence of discriminatory intent is an open question. If the Court took intent into account, there is a further question of whether it would matter for such purposes—we think it should, up to a point—that the states' primary goal was to discriminate against U.S., not other EU, companies. There exists abundant evidence that DSTs will disproportionately impact foreigners and that that outcome was well-understood by the French legislature.[192] For example, providing the Finance Committee's opinion, Jan-Noël Barrot, Deputy from the party and *Mouvement Démocrate* Vice-president of Finance Committee noted : "We must also emphasize the fact that the new tax will be selective. It will only hit large digital enterprises. In this sector, which benefits from considerable economies of scale, this will give a comparative advantage to start-ups and to French start-ups that could compete with these large, often foreign, platforms."[193] Likewise, Frédérique Dumas, Deputy from the party *Union des Démocrates, Radicaux et Libéraux* confirmed that the tax's "aim is to help French and European enterprises."[194] The impact assessment of the French DST also shows intent to protect smaller, domestic companies from foreign competition. In particular, it explains the exemption of

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191 Taking the three categories of services affected by the tax, Deloitte produced a hypothetical list of 29 entities that would be liable for French DST in 2019. The list included only one French company (Critéo). See Julien Fellefigue, *The French Digital Services Tax: An Economic Impact Assessment,* Taj, société d'avocats & Deloitte (21 March 2019), at 52, Appendix 7 (listing potentially liable entities).

192 The legislative history of the tax suggests that members of parliament understood the effects it would have. *See generally* Loi 2019-759 du 24 juillet 2019 portant création d'une taxe sur les services numériques et modification de la trajectoire de baisse de l'impôt sur les sociétés [Law 2019-759 of July 24, 2019 on the creation of a tax on digital services and the modification of the downward trajectory of corporate tax], Journal Officiel de la République Française [J.O.], July 25, 2019. *Cf. Letter from Senator Hatch and Senator Wyden to President Tusk and President Juncker* (October 18, 2018) (October 18, 2018) (urging the Commission to abandon the EU-wide DST proposal because it was "designed to discriminate against US companies" and because it would "undermine the international tax treaty system," create trade barriers, lead to double taxation, and possibly violate the WTO); Mason and Parada, *supra* note 176, 1190 (detailing evidence of discriminatory intent in the European Commission's Impact Statement on its own DST proposal).

193 Letter to the Ambassador Robert E. Lighthizer from Baker McKenzie LLP regarding a Section 301 Investigation of France's Digital Services Tax (August 26, 2019), p. 8 (citing Assemblée Nationale, Rapport N° 1838 de M. Joël Giraud sur le projet de loi, après engagement de la procédure accélérée [Report No. 1838 of the National Assembly, by Mr. Joël Giraud on the draft of the law, after initiation of the accelerated procedure], 3 avril 2019, p. 89, *available in French at* http://www.assemblee-nationale.fr/15/rapports/r1838.asp).

194 Letter to the Ambassador Robert E. Lighthizer from the Silicon Valley Tax Directors Group ("SVTDG") regarding the Initiation of a Section 301 Investigation of France's Digital Services Tax (August 18, 2019), p. 8 (citing Assemblée Nationale, Rapport N° 1838 de M. Joël Giraud sur le projet de loi, après engagement de la procédure accélérée [Report No. 1838 of the National Assembly, by Mr. Joël Giraud on the draft of the law, after initiation of the accelerated procedure], 3 avril 2019, p. 232, *available in French at* http://www.assemblee-nationale.fr/15/rapports/r1838.asp). Frédérique Dumas emphasized that the DST would level the playing field between French companies, which were liable for French corporate tax, and foreign companies, which avoided French corporate tax. See Assemblée Nationale, Rapport N° 1838 at 231 (noting that "one of the objectives of this tax was to reduce fiscal injustice").

companies with less turnover as follows: "Applying a turnover tax to small undertakings operating in a high fixed-cost market could jeopardize them, reinforcing existing imbalances and ultimately having a negative impact on the market's competitive function."[195] Senator Albéric de Montgolfier, general reporter from Finance Commission, also raised concerns about the potential selectivity of the tax under the state-aid rules.[196]

French officials have also been clear in their public statements regarding the DST's intent. For example, prior to the introduction of the French DST, French Finance Minister Bruno Le Maire repeatedly advocated for a "GAFA" tax, indicating a tax that would target Google, Amazon, Facebook, and Apple.[197] Le Maire also openly confirmed that France used the same revenue thresholds as in the Commission's DST proposal in part to ensure that the tax would not impact French digital start-ups.[198] Other French officials, such as Digital Minister Mounir Mahjoubi, have touted that the tax would not apply to European companies,[199] and it would specifically benefit French companies over their competitors, especially those from the United States.[200]

Despite this evidence of discriminatory intent, it is hard to know what the Court could reliably infer from it. Given only the evidence just described—and we have only provided a small sample—what can we conclude about the intention of the French legislature? Was its intention to discriminate on the basis of nationality, but only against U.S. companies, which receive no protection under the fundamental freedoms? Or did it intend to help French companies compared to all their competitors, including European competitors? Different people reading the same statements might conclude that both propositions are supportable, or that the evidence we

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195 *Id.* (citing Étude d'Impact, Project de loi portant création d'une taxe sur les services numériques et modification de la trajectoire de baisse de l'impôt sur les sociétés [Impact Assessment, Draft of the law on the creation of a tax on digital services and the modification of the downward trajectory of corporate tax], 5 Mars 2019, p. 13, para. 3.4.1.4 (translation by the authors) [hereinafter "French DST Impact Assessment"]).

196 Senat, Rapport N° 615 de M. Joël Giraud et M. Albéric de Montgolfier au nom de la Commission Mixte Paritaire chargée de proposer un texte sur les dispositions restante en discussion du projet de loi portant création d'une taxe sur les services numérique et modification de la trajectoire de baisse de l'impôt sur les sociétés [Report No. 615 by Mr. Joël Giraud and Mr. Albéric de Montgolfier on behalf of the Joint Committee responsible for proposing a text on the remaining provisions in discussion of the draft law for the creation of a tax on digital services and modification of the downward trajectory of corporate tax], 26 Juin 2019, p. 15. (raising concerns about the compatibility of the threshold with the state-aid rules), *available in French at* http://www.assemblee-nationale.fr/15/rapports/r2080.asp.

197 Letter to the Ambassador Robert E. Lighthizer from the Information Technology Industry Council (ITI) regarding the Initiation of a Section 301 Investigation of France's Digital Services Tax (August 22, 2019), pp. 4-5 (stating that Le Maire has referred to the acronym GAFA at least in 75 tweets since he took office until March 6, 2019 when the French proposal was released).

198 *Id.* at 6 (citing Boris Cassel & Séverine Cazes, "*Taxer les géants du numérique, une question de justice fiscal," affirme Bruno Le Maire*, LE PARISIEN (Mar. 2, 2019), http://www.leparisien.fr/economie/taxer-les-geants-du-numerique-une-question-de-justice-fiscale-affirme-bruno-le-maire-02-03-2019-8023578.php).

199 *Id.* (citing *Taxation des GAFA: la France peut-elle faire cavalier seul?*, L'EXPRESS (Mar. 1, 2019), https://lexpansion.lexpress.fr/actualite-economique/taxation-des-gafa-la-france-peut-elle-faire-cavalier-seul_2055669.html).

200 *Id.* (citing Boris Cassel, Matthieu Pelloli & Aubin Laratte, *Taxe Gafa: Amazon va faire payer les Français*, LE PARISIEN (Aug. 1, 2019), http://www.leparisien.fr/economie/taxe-gafa-amazon-va-faire-payer-les-francais-01-08-2019-8127462.php).

presented is insufficient to establish intent to discriminate against any group.[201] It is hazardous to speculate how the Court of Justice might evaluate this evidence, and this uncertainty lends support to Kokott's concerns about the role that such evidence should play in discrimination cases.

On the other hand, even if the Court were to conclude that it would be improper to look at legislative history or other evidence of discriminatory intent, that legislatures intend digital taxes to discriminate can reasonably be inferred solely from the text of the statute itself, combined with generalized knowledge about the economy. For example, the very high turnover thresholds self-evidently would exclude almost all domestic companies. The inference about the incidence of the tax, which is clear based on the statute and rudimentary knowledge of facts about the French economy, is similar to that drawn by the Court of Justice in *Humblot*. The Austrian DST proposal evinces even clearer discriminatory intent on the face of the proposed statute than does the French DST.[202] Finally, it is worth noting that if the Court used intent to lower the quantum of impact needed to prove discrimination, rather than using intent as a gateway to impact analysis, as Advocate General Kokott suggested, then even if there were no evidence *at all* that France sought to manipulate the nationality of population subject to the DST, the Court would nevertheless analyze the impact of the size threshold on companies established in other EU Member States. The anticipated impact of the French DST is expected to be very disproportionate. Thus, a reasonable case can be made on impact and intent that the gross turnover threshold in the French DSTs constitutes indirect nationality discrimination.

Assuming the size classification in the French DSTs amounts to indirect nationality discrimination, we think it unlikely that France, or a state with a similar DST, could justify it. As far as we know, France has offered no commonly accepted public policy-based justification for the tax or its high turnover threshold. Protecting domestic start-ups from foreign competition is not a justification for nationality discrimination. Likewise, it will be hard for France to support an argument that it adopted the high-turnover threshold for administrative reasons, especially in light of so much evidence that the threshold was chosen to protect French companies. The argument that companies with less than €750 million in gross turnover are exempt for ability-to-pay reasons stretches credulity. The *gross* turnover threshold in the French DST is both a poorer measure of ability to pay and more discriminatory than was the graduated net turnover tax that the Court rejected in *Hervis*. And there is more evidence available of discriminatory intent for the DST than for the Hungarian graduated turnover taxes. Thus, it is unlikely that the €750 million gross turnover threshold in the French DST could be justified by ability-to-pay reasons. Finally, the argument

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201 Similar questions arise for the types of revenue streams.

202 The recently released draft of the Austrian DST indicates that revenue obtained through the DST will be used to support the technological development of domestic companies. As stated in Article 1, Sec. 8(4) of the Austrian Digital Tax Act 2020: "Out of the revenues from the digital tax, 15 million will be annually used to finance the digital transformation process of Austrian media companies". The draft of the law is available in German language at https://www.parlament.gv.at/PAKT/VHG/XXVI/A/A_00983/fnameorig_759954.html. *Cf.* Francois Murphy, David Goodman, and Elaine Hardcastle, "Austria Says Will Tax Internet Giants 3 Percent of Ad Revenue," Reuters, 10 Jan. 2019 (noting that Austrian Chancellor Sebastian Kurz "…told reporters at the start of a cabinet meeting… that…no Austrian firms would be hit by the tax").

that DSTs compensate for tax-avoidance activity by multinationals still faces an insurmountable proportionately problem. There is no clear reason why a state's dissatisfaction with its own net income tax should justify its adoption of a *discriminatory* turnover tax, rather than a *nondiscriminatory* turnover tax.

VI. Conclusion

Classifications based on company size may constitute indirect nationality discrimination that violates the fundamental freedoms. The CJEU evaluates indirect nationality claims by looking to the practical impact of the size classification on the nationality composition of the taxable population. If past cases are a reliable guide, the Court will regard company-size classifications as discriminatory if more than half the adversely affected population is foreign. Preferring a more particularized inquiry, we expressed doubts that this bright-line majority rule could fit all cases. We also gave reasons for the Court to consider a Member State's *intent* to discriminate on the basis of nationality. Various public policy goals could justify size classifications, even when those classifications result in foreign companies paying disproportionately high taxes. The most promising justifications for company-size discrimination involve administrability and ability to pay. Finally, we argued that the French digital services tax likely constitutes unjustified indirect nationality discrimination. The analysis we provide should prove useful as more states adopt graduated turnover taxes and other size-based classifications. Our conclusion is simple: company size matters.