Legal opinion: risk tax for certain credit institutions – State aid analysis with respect to the exclusion of foreign liabilities connected to the Swedish credit market

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1 Purpose of the legal opinion and limitations

This legal opinion is written at the initiative of the Swedish Bankers' Association. The purpose of the opinion is to analyse the compatibility with the State aid rules of the territorial scope of a new tax envisaged in Sweden. The suggested tax is a risk tax that would be levied on certain credit institutions. It is presented in a memorandum drafted by the Swedish Ministry of Finance.[1]

This opinion does not contain a comprehensive assessment of the compatibility with the State aid rules of the suggested tax, as it only focuses on an analysis from a State aid perspective of the exclusion of liabilities connected to foreign credit activities for the purpose of the determination of the tax base. Other issues are not in the scope of this opinion, and I have not performed investigations outside the field of State aid law. To conduct this legal analysis, I have been relying on the information contained in the memorandum drafted by the Swedish Ministry of Finance.

The analysis contained in this opinion is not fully exhaustive: because of the complexity of the issue of the territorial scope of the tax, and the diversity of situations where differences of treatment may arise, I have not been able to analyse all issues in the most thorough manner. Different domestic and cross-border situations are described, and several differences in treatment between domestic and cross-border situations are discussed in the light of the State aid rules. Arguments pointing both to the compatibility, and the lack of compatibility with State aid law have been identified. Moreover, certain problems have been identified that have not yet been clearly decided by the Union courts, making it difficult to reach clear conclusions.

Hence, this legal opinion does not contain definitive conclusions as to the compatibility with the State aid rules and the internal market of the territorial scope of the suggested risk tax. This opinion rather contains a contribution to the analysis from a State aid perspective of the exclusion of foreign liabilities. Although further analysis might be

[1] See *Riskskatt för vissa kreditinstitut*, Fi2020/03725/S1: https://www.regeringen.se/4a6a7b/contentassets/3098b7791ca64bb2b41cfb810f4a2726/riskskatt-for-vissa-kreditinstitut.pdf

necessary to come to more precise conclusions, certain tensions have been found (especially in situations where Swedish banks lend money to their clients either from Sweden or from a foreign branch, hereinafter described as "situation 2" and "situation 3"), thus confirming the relevance – as suggested in the memorandum drafted by the Swedish Ministry of Finance – of notifying the suggested risk tax to the European Commission.

2 Terminological precisions and short summary of the proposal for a risk tax on certain credit institutions

2.1 Terminological precisions

Before describing the mechanisms of the suggested risk tax that are relevant for this opinion, certain terminological precisions are made. The object of the risk tax is certain of the liabilities of credit institutions. Indeed, to be able to grant loans, credit institutions may need to borrow money. In addition, there is an important territorial element in the design of the tax: only domestic liabilities, and not foreign liabilities, are subject to the risk tax. In order to distinguish between domestic and foreign liabilities, the suggested risk tax is based on where the credit activities (i.e. the activity of granting loans) that are connected to the liabilities are located, hence irrespective of where the customer is located. In other words, when a credit institution carries out credit activities in Sweden through granting loans to its clients in Sweden or abroad, and that it needs to borrow money to grant these loans, then the liabilities so incurred will be subject to the risk tax. Conversely, liabilities incurred for credit activities carried out outside of Sweden are not in the scope of the tax. Liabilities incurred for other purposes than granting loans to clients are not either in the scope of the tax.

The text of the suggested risk tax relevant for this distinction is the fourth paragraph of the act, first indent, and it is drafted as follows: "*4 § Ett kreditinstitut är skattskyldigt enligt denna lag, om 1. kreditinstitutet har skulder vid beskattningsårets ingång som är hänförliga till verksamhet som kreditinstitutet bedriver i Sverige*". The first sentence of the seventh paragraph of the act follows the same principle, and is drafted as follows: *"7 § Beskattningsunderlaget utgörs av summan av kreditinstitutets skulder vid beskattningsårets ingång, hänförliga till verksamhet som kreditinstitutet bedriver i Sverige.*" A more detailed definition of liabilities connected to credit activities in Sweden, i.e. domestic liabilities, is found at page 25 of the memorandum: "*Med skulder som är hänförliga till verksamhet i Sverige avses huvudsakligen in- och upplåning (inklusive emittering av värdepapper) som används för att finansiera kreditgivning i den svenska verksamheten, men även andra typer av skulder som är ett resultat av den svenska verksamheten omfattas*".

To sum up the above, the following definitions will be used in this opinion:

- Domestic liability: liability that is incurred in Sweden for the purpose of financing credit activities performed in Sweden.

- Foreign liability: liability that is incurred abroad for the purpose of financing credit activities performed outside of Sweden. Here it is important to emphasise that foreign liabilities may be incurred in connection with loans granted to Swedish clients, albeit on the basis of credit activities performed outside of Sweden.

2.2 Short summary of the proposal for a risk tax on certain credit institutions

The suggested tax is designed so that credit institutions (Swedish: *kreditinstitut*) that have liabilities at the beginning of a fiscal year that are connected to credit activities in Sweden, pay a risk tax consisting of a percentage of the liabilities after certain adjustments are made to their liabilities. The tax is to be levied, however, only if the liabilities exceed a given threshold. The tax rate suggested for 2022 is 0,06% of the liabilities, and the threshold suggested for 2022 is 150 billion SEK. The tax rate is set to 0,07% as from 2023, and the liabilities threshold is intended to increase each year.

According to the proposal, a credit institution is liable to the risk tax only if it has liabilities at the beginning of a fiscal year that are connected to credit activities in Sweden. If credit activities are performed by a foreign credit institution, it is only the credit activities performed from a Swedish permanent establishment that are in the scope of the risk tax.[2] My understanding of the memorandum drafted by the Ministry of Finance is that liabilities may be considered connected to credit activities in Sweden no matter if the credit institution is a resident of Sweden or a foreign resident.[3] What matters is where the liabilities that occur in connection with credit activities are deemed to be located.[4] The outcome is the exclusion from the tax base of liabilities connected to credit activities that are carried out outside of Sweden.

How to exactly distinguish between liabilities that are considered as connected to credit activities in Sweden, and liabilities that are considered as connected to foreign credit activities is not entirely clear on the basis of the sole reading of the memorandum. However, no matter where exactly the border goes between liabilities that are in the scope, or outside the scope of the tax base, the fact remains that a distinction is being made between domestic and foreign liabilities, the former being subject to the tax, the latter being exempted from it. Therefore, the suggested tax is designed so that credit

[2] See paragraphs 4§1 and 7§ of the proposal for a risk tax on certain credit institutions. See also the explanatory material: *Riskskatt för vissa kreditinstitut*, Fi2020/03725/S1, p. 25.

[3] The text of the memorandum supporting this description reads as follows: "*Eftersom skatten är tänkt att kompensera för indirekta kostnader i Sverige i händelse av en finansiell kris, bör endast sådana skulder beaktas som är hänförliga till verksamhet som kreditinstitutet bedriver i Sverige eller, såvitt avser ett utländskt bankföretag eller utländskt kreditföretag, från ett fast driftställe i Sverige*" (see *Riskskatt för vissa kreditinstitut*, Fi2020/03725/S1, p. 25).

[4] The text of the memorandum supporting this description reads as follows: "*Med skulder som är hänförliga till verksamhet i Sverige avses huvudsakligen in- och upplåning (inklusive emittering av värdepapper) som används för att finansiera kreditgivning i den svenska verksamheten, men även andra typer av skulder som är ett resultat av den svenska verksamheten omfattas. Skulder hänförliga till verksamhet i ett utländskt fast driftställe ska inte beaktas*" (see *Riskskatt för vissa kreditinstitut*, Fi2020/03725/S1, p. 25).

activities leading to the taking on of liabilities are divided in two categories, subject to different treatments.

The territorial nature of the suggested risk tax is illustrated with a simplified example, where Bank 1 is a Swedish bank with liabilities amounting to 200 billion SEK that are connected to its credit activities in Sweden, and Bank 2 is a foreign bank with liabilities amounting to 200 billion SEK that are connected to its foreign credit activities. Bank 2 has no permanent establishment in Sweden but does lend money to Swedish clients. Banks 1 and 2 compete on the same markets, and certain Swedish clients take loans from both Bank 1 and Bank 2. As I understand it, the tax regime applicable to the two banks would be as follows:

- Bank 1 (the Swedish bank) has liabilities that are in the scope of the tax. The liabilities are above the threshold of 150 billion SEK. For year 2022, the tax paid by Bank 1 amounts to 200.000.000.000 * 0,06% = 120.000.000 SEK

- Bank 2 (the foreign bank) has no liabilities connected to domestic credit activities. It is not in the scope of the risk tax.

Accordingly, there is a difference in the taxation of the two categories of credit institutions, the risk tax being only levied on the Swedish bank with liabilities connected to its credit activities in Sweden.

3 Methodology to assess the compatibility of a tax measure with the internal market from the perspective of the EU State aid rules

Article 107(1) of the TFEU is drafted as follows: "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."

According to settled case-law from the Court of Justice of the European Union (hereinafter the "CJEU"), the classification of a national measure as State aid, within the meaning of Article 107(1) TFEU, requires several conditions to be fulfilled cumulatively. First, there must be an intervention by the State or through State resources. Second, the intervention must be liable to affect trade between the Member States. Third, it must confer a selective advantage on the recipient. Fourth, it must distort or threaten to distort competition.[5]

The notion of selective advantage is traditionally considered as the most complex element of the State aid definition in the area of taxation, and it is the main issue studied in this opinion. Therefore, in the section below I will be analysing the three other criteria

[5] See e.g. Joined Cases C-20/15 P and C-21/15 P, *Commission v World Duty Free Group and Others*, paragraph 53.

(section 4). I will then focus on the notion of selective advantage, through first analysing the notion of advantage (section 5), before turning to the selectivity criterion (section 6). Concluding remarks are made in section 7.

4 Intervention by the State or through State resources, effect on trade between the Member States, and distortion of competition

First, according to article 107(1) of the TFEU, there must be an intervention by the State or through State resources for a measure to be able to constitute illegal State aid. This requirement is automatically fulfilled with respect to tax measures since only the State, or a public organisation within the State, has the right to levy taxes. The fact that a tax is not levied implies an indirect transfer of resources to the benefit of the taxpayers that are not subject to the tax. Thus, depending on its design, a tax measure may constitute State aid.[6] The risk tax on certain credit institutions suggested in the memorandum would be levied by the Swedish State and it would be imputable to the State. It would strengthen the public finances of the State. Therefore, the risk tax would be considered as an intervention by the State or through State resources for the purpose of the application of the first element of article 107(1) of the TFEU. This criterion is thus fulfilled.

Second, the intervention must be liable to affect trade between the Member States for the measure to potentially constitute State aid. This criterion is normally considered to be fulfilled by the European Commission and by the Union courts when a measure affects undertakings that are globally active and operate in several Member States of the Union.[7] The financial sector is open to cross-border trade and it is frequent that banks or other financial institutions in one Member State lend to foreign clients, or operate in other Member States, assuming they are allowed to do so.[8] Swedish banks are often active abroad or have foreign clients, and several foreign banks are active on the Swedish market. Therefore, in my view a risk tax on credit institutions would be liable to affect trade between the Member States in the sense of article 107(1) of the TFEU, thereby making this criterion fulfilled.

Third, an intervention must distort or threaten to distort competition for it to be potentially deemed as an illegal State aid. It is usually considered in State aid law that a measure granted by a Member State distorts or may threaten to distort competition when it is liable to improve the competitive position of the recipient compared to other

[6] See e.g. Case C-222/04, *Ministero dell'Economia e delle Finanze v Cassa di Risparmio di Firenze SpA, Fondazione Cassa di Risparmio di San Miniato and Cassa di Risparmio di San Miniato SpA*, paragraph 132.

[7] See e.g. Commission Decision of 21.10.2015 on State aid SA.38375 (2014/C ex 2014/NN) which Luxembourg granted to Fiat, paragraph 189; see also Case C-53/00, *Ferring SA v Agence centrale des organismes de sécurité sociale (ACOSS)*, paragraph 21.

[8] On the effect on trade and the distortion of competition in the financial sector, see Case C-222/04, *Ministero dell'Economia e delle Finanze v Cassa di Risparmio di Firenze SpA, Fondazione Cassa di Risparmio di San Miniato and Cassa di Risparmio di San Miniato SpA*, paragraphs 139 and following. See also Case C-148/04, *Unicredito Italiano SpA*, paragraph 60.

undertakings with which it competes. [9] It can reasonably be assumed that the suggested tax measure would distort or threaten to distort competition, since the undertakings subject to the tax and exempted from it are, at least in some respects, competing on similar markets or for similar clients. It is also acknowledged in the memorandum drafted by the Swedish Ministry of Finance that competition would probably be affected if the tax were implemented.[10] Indeed, since it is possible that the banks subject to the risk tax would transfer at least part of this additional cost to their clients (via e.g. increased fees, higher interests charged, or lower interests paid), owners or employees, competition might be distorted as credit institutions that are not in the scope of the tax would save this cost and thus be able to sell their products and services at lower prices, and/or earn higher profit margins. Therefore, it can be assumed that this criterion is fulfilled.

The above analysis leaves one criterion to investigate, the selective advantage. Although the notion of selective advantage is frequently used in State aid practice, it is settled case law that the two notions of advantage and selectivity need to be distinguished: "the requirement as to selectivity under Article 107(1) TFEU must be clearly distinguished from the concomitant detection of an economic advantage".[11] However, it can be observed that, for instance, the General Court has found that this does not prevent the two criteria from being examined "simultaneously", in situations where they overlap.[12] For the sake of clarity, I will first analyse the potential existence of an advantage (section 5), before turning to the selectivity criterion (section 6).

5 Potential existence of an advantage

With respect to the existence of an advantage in the sense of article 107(1) of the TFEU, the CJEU has held in numerous cases that measures that relieve an undertaking of a cost, including a tax cost, may constitute an aid.[13] For example, in the *Congregación de Escuelas Pías Provincia Betania* case, the CJEU held that "measures which, in various forms, mitigate the charges that are normally included in the budget of an undertaking and which therefore, without being subsidies in the strict meaning of the word, are similar in character and have the same effect are considered to constitute aid";[14] on that basis, the Court considered that a tax exemption would confer an

[9] See e.g. Commission Decision of 21.10.2015 on State aid SA.38375 (2014/C ex 2014/NN) which Luxembourg granted to Fiat, paragraph 189, with further references to the case law of the European Courts at footnote 75.
[10] See *Riskskatt för vissa kreditinstitut*, Fi2020/03725/S1, pp. 40-41.
[11] See Case C-15/14 P, *European Commission v. MOL Magyar Olaj- és Gázipari Nyrt.*, paragraph 59.
[12] See Cases T-778/16 and T-892/16, *Ireland and Others v European Commission*, paragraphs 136-138.
[13] See Case C-222/04, *Ministero dell'Economia e delle Finanze v Cassa di Risparmio di Firenze SpA, Fondazione Cassa di Risparmio di San Miniato and Cassa di Risparmio di San Miniato SpA*, paragraph 132.
[14] See Case C-74/16, *Congregación de Escuelas Pías Provincia Betania v Ayuntamiento de Getafe*, paragraph 66.

economic advantage on its beneficiary.[15] To take another example, in the *ANGED* case the CJEU ruled that an exemption from a tax on large retail establishments that was granted to collective large retail establishments with a surface area equal to or greater than 2 500 m2 implied an economic advantage and constituted State aid.[16]

In the case of the suggested risk tax, and when considering the fact that certain credit activities are in the scope of the tax while others are not, it is unquestionable that credit institutions with credit activities exempted from the tax, such as foreign banks with no credit activities in Sweden, receive an economic advantage consisting in this very tax relief.

The advantage criterion is thus, in my view, fulfilled. This does not make the tax at breach of the State aid rules: it remains to be investigated whether or not the selectivity criterion is met.

6 The selectivity criterion

The selectivity criterion implies a prohibition of discriminations between comparable undertakings,[17] which in essence leads to an obligation to provide equal treatment.[18] To test the potential selectivity of a tax measure, the CJEU has developed a method in three steps. This methodology has recently been recalled by Advocate General Pitruzzella in his opinion in the *World Duty Free Group* case:[19] one must first identify the ordinary or "normal" tax system applicable in the Member State concerned.[20] Second, one needs to demonstrate that the tax measure at issue is a derogation from that ordinary system to the benefit of only certain undertakings, in so far as it differentiates between operators who, in the light of the objective pursued by that ordinary tax system, are in a comparable factual and legal situation; even if there is no formal derogation included in the tax system from what is deemed as "normal taxation", a measure may still be selective if its effects favour certain undertakings over others (so-called *de facto* selectivity).[21] Third, assuming that a tax measure is *prima facie* selective (i.e. it implies a difference in treatment between comparable undertakings), it may nevertheless be

[15] See Case C-74/16, *Congregación de Escuelas Pías Provincia Betania v Ayuntamiento de Getafe*, paragraph 68.
[16] See Case C-233/16, *Asociación Nacional de Grandes Empresas de Distribución (ANGED*), paragraph 68.
[17] See Case C-233/16, *Asociación Nacional de Grandes Empresas de Distribución (ANGED*), paragraph 38; Joined Cases C-105/18 to C-113/18, *Asociación Española de la Industria Eléctrica (UNESA) and Others v Administración General del Estado*, paragraph 60.
[18] See Case C-524/14 P, *European Commission v. Hansestadt Lübeck*, paragraph 53.
[19] See the opinion delivered on 21 January 2021, Joined Cases C-51/19 P and C-64/19 P, *World Duty Free Group v Commission*, paragraphs 11-21.
[20] See Case C-88/03, *Portugal v Commission*, paragraph 56; Cases C-78/08 to C-80/08, *Paint Graphos*, paragraph 49.
[21] See Joined Cases C-20/15 P and C-21/15 P, *Commission v World Duty Free Group and Others*, paragraph 74. See also Case C-203/16 P, *Dirk Andres v European Commission*, paragraphs 90-93.

justified if it flows from the nature or the general structure of the system of which it forms part[22] and is in line with the principle of proportionality.[23]

The potential selectivity of the suggested risk tax for certain credit institutions with respect to the territorial scope of the tax is analysed below in the light of this methodology. Accordingly, I shall first determine the relevant reference system (section 6.1). I will then emphasise that within this reference system, a difference of treatment is made between different undertakings (section 6.2). Once a difference of treatment has been confirmed, it can be proceeded with the selectivity analysis. To that end, I will identify the objective pursued by the tax system (section 6.3), before turning to the comparability and the justification analyses (section 6.4).

6.1 What is the reference system?

The reference system must be determined carefully, because an improperly chosen reference system is likely to lead to a biased State aid analysis.[24]

A definition of the reference system is suggested in the Commission notice from 2016. Although this definition has not yet been adopted by the CJEU,[25] it rightfully emphasises the notion of consistency in the definition of the reference system.[26] The European Commission defines the reference system as follows: "a consistent set of rules that generally apply — on the basis of objective criteria — to all undertakings falling within its scope as defined by its objective. Typically, those rules define not only the scope of the system, but also the conditions under which the system applies, the rights and obligations of undertakings subject to it and the technicalities of the functioning of the system".[27] The European Commission observes that the reference system "is based on such elements as the tax base, the taxable persons, the taxable event and the tax rates". Consequently, it will often be the tax system itself that constitutes the reference system.[28] This is especially true for sectoral taxes, which are taxes with a narrow scope of application, and where it is logical to take into account the whole sectoral tax as a reference system for it to include all the elements necessary to its full functioning, especially the main rules together with the possible exceptions. Examples of sectoral taxes such as turnover taxes applied on the retail sector or environmental taxes illustrate the use of the whole sectoral tax as a reference system, as opposed to excluding from the reference system the undertakings that are not in its scope of

[22] See e.g. Case C-88/03, *Portugal v Commission*, paragraph 52; Joined Cases C-20/15 P and C-21/15 P, *Commission v World Duty Free Group and Others*, paragraph 58.
[23] See Cases C-78/08 to C-80/08, *Paint Graphos*, paragraph 75.
[24] See Case C-203/16 P, *Dirk Andres v European Commission*, paragraph 107.
[25] See the opinion delivered on 21 January 2021, Joined Cases C-51/19 P and C-64/19 P, *World Duty Free Group v Commission*, paragraph 37.
[26] See the opinion delivered on 21 January 2021, Joined Cases C-51/19 P and C-64/19 P, *World Duty Free Group v Commission*, paragraph 43.
[27] See Commission Notice on the notion of State aid as referred to in Article 107(1) of the Treaty on the Functioning of the European Union, C/2016/2946, paragraph 133.
[28] See Commission Notice on the notion of State aid as referred to in Article 107(1) of the Treaty on the Functioning of the European Union, C/2016/2946, paragraph 134.

application.[29] As the General Court emphasises, a reduction from a tax "de facto forms part of the structure of taxation";[30] therefore, although it is exempt from a tax, an exempted activity falls within the sectoral scope of application of the tax. It can also be observed that the European Commission and the Union courts have adopted a broad approach to the determination of the reference system, even for taxes that have broader scopes than a sectoral tax.[31] In certain rather exceptional cases the reference system may even encompass legal provisions that are not *per se* included in the tax system under review, if there is a link between the two.[32]

Accordingly, in my view in this case the most correct reference system is the whole risk tax, including the territorial elements of the tax that result in the exclusion of liabilities connected to foreign credit activities from the scope of the tax. An alternative view could have been to consider that the two categories of credit activities distinguished by the territorial scope of the risk tax constitute two separate reference systems that operate in parallel. However, in my opinion one could not validly hold such a view: the reference system should preferably be a *consistent* set of rules, which should reasonably include all the rules necessary for the normal operation of the tax system so that its effects can be fully assessed. In addition, the CJEU has repeatedly held that the regulatory technique should not influence the outcome of a State aid analysis; instead, focus is on the effects of a tax.[33] If the reference system was only made of credit institutions with credit activities that are in the territorial scope of the tax or outside the territorial scope, thereby creating two parallel reference systems, the effect of the risk tax consisting in excluding foreign credit activities from the tax base could not be fully assessed as a consequence of the regulatory technique chosen, through excluding in the text of the law liabilities that are not connected to domestic credit activities.

The next question is whether there is, within this reference system, a difference in treatment between different undertakings.

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[29] Concurring, see Rita Szudoczky and Balázs Károlyi, 'Progressive Turnover Taxes under the Prism of the State Aid Rules: Effective Tools to Tax High Financial Capacity or Inconsistent Tax Design Granting Selective Advantages?', 19 European State Aid Law Quarterly (2020) 3, p. 256.

[30] See Joined Cases T-836/16 and T-624/17, *Republic of Poland v European Commission*, paragraph 68.

[31] See e.g. the decisions and court cases in the field of corporate income tax. It is in most cases the whole corporate income tax system that constitutes the reference system, as opposed to a specific provision within the corporate income tax. An example is provided by the *Apple* case, where the General Court found that the provisions for the attribution of profits to permanent establishments could not constitute a reference system on its own: see Cases T-778/16 and T-892/16, *Ireland and Others v European Commission*, paragraph 163. Generally, on the question of the scope of the reference system, see Jérôme Monsenego, *Selectivity in State Aid Law and the Methods for the Allocation of the Corporate Tax Base*, Kluwer Law International 2018, pp. 45 and following.

[32] See Case C-308/01, *GIL Insurance Ltd and Others v Commissioners of Customs & Excise*.

[33] See Case C-487/06 P, *British Aggregates Association v Commission of the European Communities and United Kingdom*, paragraph 89, last sentence; Joined cases C-106/09 P and C-107/09 P, *European Commission (C-106/09 P) and Kingdom of Spain (C-107/09 P) v Government of Gibraltar and United Kingdom of Great Britain and Northern Ireland*, paragraph 92; Case C-219/16 P, *Lowell Financial Services GmbH v European Commission*, paragraph 92; Joined Cases C-20/15 P and C-21/15 P, *Commission v World Duty Free Group and Others*, paragraph 67; Case C-219/16 P, *Lowell Financial Services GmbH v European Commission*, paragraph 93.

6.2 Is there within the reference system a difference in treatment between different undertakings?

The suggested tax system implies a difference in treatment between different credit institutions, partly because the territorial scope of the tax excludes liabilities connected to foreign credit activities from the tax base. The example mentioned in section 2 of this opinion illustrates a type of difference in treatment that may arise within the reference system.

The existence of a difference in treatment appears whether one is reasoning on the basis of the *de jure* or the *de facto* selectivity test:

- Under the *de jure* selectivity test, a measure implies a difference in treatment if the taxation of certain undertakings deviates from what is deemed as "normal taxation". In this case, "normal taxation" would be the taxation of credit institutions on their liabilities; the exception constituting a difference in treatment would be an exemption from the tax for liabilities connected with foreign credit activities.

- Under the *de facto* selectivity test, a measure might be selective if its effects imply a difference in treatment, without the tax system necessarily including both a principle and a derogation. In this case, if one does not consider the exclusion of liabilities connected to foreign credit activities as an exception to a main rule, the tax system could be seen as producing different, or inconsistent types of effects: credit institutions with domestic liabilities are subject to the tax, while credit institutions with foreign liabilities are exempt from it.

The proposition that the suggested tax system implies a difference in treatment between different credit institutions, no matter if one is reasoning on the basis of the *de jure* or the *de facto* selectivity test, does not make the risk tax selective. One needs to investigate whether or not the difference in treatment takes place between operators who, in the light of the objective pursued by the tax system, are in a comparable factual and legal situation. To answer this question, I will now investigate the objective pursued by the tax system (section 6.3). I will then proceed with the comparability and justification analyses (section 6.4).

6.3 Determination of the objective of the reference system

The determination of the objective of the reference system might be a difficult exercise, because the objective of a tax system is not necessarily explicitly mentioned in the legislative material relevant for the tax, such as the preparatory works or the actual tax provisions. Even if the objective of a tax is explicitly mentioned in the tax law or in the preparatory works, in my opinion it would not be correct to fully and solely rely on

what the lawmaker chose to mention or not.[34] I believe that a more correct method rather consists in understanding the essence and the practical operation of a tax system, to be able to deduce its objective. Similarly, the Commission notice on the notion of State aid insists on the determination of objectives that are "intrinsic" to the system.[35] However, this method may not always be satisfactory, for example when a tax system pursues several objectives not necessarily consistent with each other.

In the case of the proposal for a risk tax on certain credit institutions, the main objective of the tax mentioned in the memorandum is the need to strengthen the Swedish public finances to be able to assume the indirect costs caused by future financial crises.[36] However, as from 2023 the tax rate is to increase from 0,06% to 0,07% of the liabilities; the difference (a tax rate corresponding to 0,01%, or approximately 1 billion SEK per year[37]) is, according to the press release that accompanied the proposal,[38] to be attributed to the defence budget, which is a different objective than the one stated as a main purpose for the tax. In addition, the objective that initially motivated the idea of a "bank tax" (at that time it was not yet, at least not officially, a risk tax on certain credit institutions) was the strengthening of the defence budget.[39] The impression that the proposal for a risk tax on certain credit institutions is motivated by the objective to strengthen the defence budget is consistent with the revenues yielded by the suggested risk tax, which broadly match the revenues to be allocated to the defence budget in the original presentation of a bank tax.

The precise determination of the objective of the tax might be important for the comparability analysis between the two categories of undertakings: if the objective of the tax is generally to strengthen the Swedish public finances, the revenues of which would contribute to different public efforts, it is more likely that the two categories of undertakings will be in a comparable situation. This is because the objective to levy taxes and improve the public finances does not, in itself, mandate a differentiated taxation between credit institutions with liabilities connected to domestic or foreign credit activities. If, in contrast, the objective of the tax is really to face the indirect costs caused by a financial crisis, and that the two categories of credit institutions indeed may

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[34] Concurring see Michael Lang, 'State Aid and Taxation: Selectivity and Comparability Analysis', in Isabelle Richelle, Wolfgang Schön and Edoardo Traversa (eds.) *State Aid Law and Business Taxation* (Springer 2016), p. 34: "Searching for the legislator's intention (…) cannot lead to any result". See also Case C-562/19 P, *European Commission v Republic of Poland*, Opinion of Advocate General Kokott delivered on 15 October 2020, paragraph 75, where the objective pursued by the tax system is considered to be determined "by way of interpretation from the nature of the tax and its design".

[35] See Commission Notice on the notion of State aid as referred to in Article 107(1) of the Treaty on the Functioning of the European Union, C/2016/2946, paragraphs 128 and 135.

[36] See *Riskskatt för vissa kreditinstitut*, Fi2020/03725/S1, e.g. at p. 24.

[37] See *Riskskatt för vissa kreditinstitut*, Fi2020/03725/S1, p. 38.

[38] See https://www.regeringen.se/pressmeddelanden/2020/09/forslag-om-riskskatt-for-storre-kreditinstitut-pa-remiss/ (accessed 22 January 2021): "*Den beräknade offentligfinansiella effekten från höjningen planeras användas till ökade försvarsanslag*".

[39] See the press release dated 31 August 2019: https://www.regeringen.se/pressmeddelanden/2019/08/langsiktig-finansiering-av-det-militara-forsvaret/ (accessed 24 October 2020).

trigger different indirect costs for the State, a differentiated levy of the risk tax may appear more motivated.

However, in this case I do not believe that the choice of either objective is decisive to proceed with the comparability analysis. This is because the levy of the risk tax is still a tax, which by definition is not directly affected to a special purpose, be it the defence budget or the indirect costs that occur with a financial crisis; it is rather a general contribution to the State's revenues, which may, in turn, be affected (or not) to different purposes. The general character of the risk tax is demonstrated by the fact that it might aim at covering *indirect* costs that occur with a financial crisis (i.e. the deteriorated public finances due to an economic downturn, with no precise determination of who should benefit from the intervention of the State), not the *direct* costs that the State may have to assume in case of financial crisis (i.e. when the State must improve the financial stability by targeting its interventions). The risk tax would apply in addition to existing mechanisms such as the resolution fees and capital requirements, the purpose of which is to mitigate the risk that a financial crisis happens and the exposure of the State in case such a crisis occurs. There is no mention of investments aimed at decreasing the probability of a financial crisis or at minimizing the consequences of a financial crisis that might be financed with the revenues of the risk tax. The suggested risk tax does not either aim predominantly at influencing behaviours, for example by discouraging credit institutions from taking risks that may result in a financial crisis. The risk tax would be affected to the State budget, which supports various types of public expenditures, including (but not limited to) both the defence budget and the indirect costs that occur with a financial crisis. There is no obligation for the State to actually allocate the revenues of the risk tax to certain purposes; the State may also change its priorities over time.

As a subsidiary way of reasoning, if there really were a need to specifically strengthen the financial reserves of the State in view of potential future financial crises, one could have conceived a system that is not a tax, but a fee paid to a blocked account aimed at supporting indirect costs occurring in case of financial crisis. The funds could be reimbursed after some time in case the risk has not (fully) materialized. However, the suggested risk tax does not follow this kind of logic: the risk tax is to be paid whether or not the risk materializes, and no reimbursement is envisaged.

Moreover, for State aid purposes, the Commission emphasised in the 2016 notice on the notion of State aid that one needs to determine the objectives that are "intrinsic" to the system.[40] This position makes sense, as it is reasonable that the intrinsic features of a tax system reveal its objectives. For that reason, it was mentioned above that in my view a correct method to determine the objective of the reference system consists in understanding the essence and the practical operation of a tax system, to be able to deduce its objective. Therefore, it is my understanding that the intrinsic objective of the suggested risk tax, for State aid purposes, is the taxation of credit institutions on the

[40] See Commission Notice on the notion of State aid as referred to in Article 107(1) of the Treaty on the Functioning of the European Union, C/2016/2946, paragraphs 128 and 135.

basis of their liabilities. If one were to formulate a more detailed objective, it could be described as the taxation of the largest credit institutions (because of the liabilities threshold of 150 billion SEK) on the basis of their liabilities connected to domestic credit activities (because of the exclusion of foreign credit activities), to generally finance public expenditure.

After having determined the objective of the reference system, I shall now consider the comparability and justification analyses.

6.4 Comparability and justification analyses

6.4.1 Introduction

Now that the objective pursued by the tax system has been determined, the next question consists in analysing whether undertakings with domestic and foreign credit activities, are, in the light of this objective, in a comparable factual and legal situation. If they are not in a comparable situation, the differentiation included in the tax system on the basis of the location of the credit activities cannot have a selective nature. If they are in comparable situation, the differentiation included in the tax system is *prima facie* selective. It can still be justified by the nature or the logic of the tax system.

It is argued in the memorandum that all credit institutions and credit activities do not imply the same risks of indirect costs in case of financial crisis. The difference would mainly stem from the size of the operators.[41] In addition, it seems to be implied in the memorandum that only domestic credit activities might trigger risks of indirect costs.[42] However, this argument is not made very clearly. It is not either investigated in the memorandum whether credit institutions with liabilities connected to domestic and foreign credit activities are in a factual and legal comparable situation. Yet this question is central to the assessment of the compatibility of the suggested risk tax with the State aid rules. Therefore, I now turn to analysing this question.

The comparability analysis is often a difficult exercise, and it is particularly complex in this case. This is partly due to the diversity of situations that may occur. Therefore, I do not perform a single comparability and justification analysis. I first need to identify the situations where differences in treatment might occur, and choose the most relevant for the comparability and justification analyses (section 6.4.2). I will then consider several situations, and analyse them separately (sections 6.4.3, 6.4.4, and 6.4.5).

6.4.2 Identification of situations where differences in treatment might occur

[41] See *Riskskatt för vissa kreditinstitut*, Fi2020/03725/S1, p. 23.
[42] See *Riskskatt för vissa kreditinstitut*, Fi2020/03725/S1, p. 25: ”*Eftersom skatten är tänkt att kompensera för indirekta kostnader i Sverige i händelse av en finansiell kris, bör endast sådana skulder beaktas som är hänförliga till verksamhet som kreditinstitutet bedriver i Sverige eller, såvitt avser ett utländskt bankföretag eller utländskt kreditföretag, från ett fast driftställe i Sverige*”.

There are at least eight different situations that might be relevant to analyse in the light of the State aid rules, when these situations are subject to different tax treatments. These eight situations are not exhaustive, and there may be different variants between these situations.

1) Swedish credit institution with all activities in Sweden.

2) Swedish credit institution with foreign branch from which some sales and credit activities are being carried out and directed towards Swedish clients (whether remotely or with some limited physical presence).

3) Swedish credit institution with foreign branch from which some credit activities are being carried out, while all sales activities remain in Sweden.

4) Foreign credit institution with all activities abroad, and no loans are granted to Swedish clients.

5) Foreign credit institution with Swedish branch from which some sales and credit activities are being carried out towards Swedish clients.

6) Foreign credit institution with Swedish branch from which some sales activities are being carried out towards Swedish clients, while all credit activities remain abroad.

7) Foreign credit institution with Swedish branch from which some credit activities are being carried out towards Swedish clients, while all sales activities remain abroad.

8) Foreign credit institution with all activities abroad and no branch in Sweden, but with some sales and credit activities directed towards Swedish clients, whether remotely or with some limited physical presence in Sweden, but with no branch located in Sweden.

I now assume – based on my understanding of the tax regime suggested in the memorandum – that the above situations would be subject to the risk tax as follows:

1) Situation 1: all liabilities are in the scope of the risk tax

2) Situation 2: some liabilities are in the scope of the risk tax (those which are connected to the domestic credit activities), while some other liabilities are not in the scope of the risk tax (those which are connected to the foreign credit activities exercised through the foreign branch).

3) Situation 3: same tax treatment as situation 2.

4) Situation 4: no liabilities are in the scope of the risk tax.

5) Situation 5: some liabilities are in the scope of the risk tax (those which are connected to domestic credit activities through the Swedish branch), while some other liabilities are not in the scope of the risk tax (those which are connected to the foreign credit activities exercised at the foreign head office).

6) Situation 6: in principle the foreign credit institution might be subject to the risk tax because of the existence of a Swedish branch, but in practice there should be no liabilities in the scope of the risk tax because the credit activities are located abroad.

7) Situation 7: same tax treatment as situation 5.

8) Situation 8: same tax treatment as situation 4. The lack of Swedish branch prevents any liability to the risk tax: the memorandum is clear as to the absence of tax liability when a foreign credit institution has no permanent establishment.[43]

In my view the most relevant comparison for State aid purposes is between domestic and foreign credit activities, when the former ones are subject to the risk tax while the latter ones are exempt from it, but when both do lend money to Swedish clients: it is at this point that a difference in treatment most obviously occurs and needs to be analysed in the light of the State aid rules. In other words, one needs to compare the tax treatment of a Swedish credit institution with Swedish activities (situation 1) that is in the scope of the risk tax (assuming the other criteria are met, such as the liabilities threshold), with the tax treatment of credit institutions with foreign liabilities that are not in the scope of the risk tax but that do lend money to Swedish clients. Comparisons between situations with cross-border elements but subject to differentiated taxation may also be relevant to analyse (e.g. a comparison between situations 6 and 7); however, a priority had to be made, and it was chosen to focus the analysis on a comparison between domestic and cross-border situations.

The domestic element of the comparison shall thus be situation 1, to avoid any doubt as to the liability to the risk tax of the chosen domestic situation (it is assumed that the other criteria are met, such as the liabilities threshold). It now needs to be determined which cross-border situations to compare to situation 1. In the examples above, situation 2 is relevant to compare to situation 1, when foreign credit and sales activities are carried out by the foreign branch and directed towards Swedish clients: here, a difference in treatment exists since the risk tax will be applicable to situation 1, but not situation 2. Situation 3 is also relevant to consider (i.e. a Swedish credit institution with a foreign branch from which some credit activities are being carried out, while all sales

[43] See *Riskskatt för vissa kreditinstitut*, Fi2020/03725/S1, particularly at p. 25 where it is mentioned that "*Eftersom skatten är tänkt att kompensera för indirekta kostnader i Sverige i händelse av en finansiell kris, bör endast sådana skulder beaktas som är hänförliga till verksamhet som kreditinstitutet bedriver i Sverige eller, <u>såvitt avser ett utländskt bankföretag eller utländskt kreditföretag, från ett fast driftställe i Sverige</u>* (my underlining)".

activities remain in Sweden), although it makes in principle no difference with situation 2 as to the place of the liabilities, and may be less frequent in practice. Therefore, the analysis that is made for situation 2 should, in principle, be equally relevant for situation 3. However, since situation 2 may be more frequent in practice than situation 3, and for the sake of simplicity, no distinction is made below between situations 2 and 3. Only in the conclusions is it recalled that the conclusions relevant for situation 2 may be equally valid for situation 3.

Moreover, there are five situations that concern foreign credit institutions: situations 4 to 8. However, not all these situations are the most relevant to investigate in this opinion. I will now review situations 4 to 8 to consider which one(s) should be chosen for the comparability and justification analyses:

- Credit institutions in situation 4 are out of the scope of the risk tax, because they have no branch in Sweden. They have no remote sales or credit activities directed towards Swedish clients. There are good reasons not to subject such credit institutions to the risk tax, as they have no connection to Sweden. Situation 4 is, accordingly, not a relevant benchmark for comparison with situation 1.

- Credit institutions in situation 5 are in the scope of the risk tax to the extent of their liabilities that are deemed connected to domestic credit activities. No fundamental difference in treatment exists with credit institutions in situation 1 when it comes to their activities directed towards Swedish clients, as both are liable to the risk tax.[44] Given the lack of important difference in treatment with situation 1, situation 5 is not a particularly relevant benchmark for comparison with situation 1 and will thus not be investigated in this opinion.

- Credit institutions in situation 6 are not in the scope of the risk tax because no liabilities are connected to domestic credit activities. All credit activities are located abroad. However, sales activities are exercised from a Swedish branch towards Swedish clients. Situation 6 is a relevant benchmark to use as a comparison with situation 1, because while credit institutions in both situations grant loans to Swedish clients, only credit institutions in situation 1 are subject to the risk tax.

- Credit institutions in situation 7 are in the scope of the risk tax to the extent of their liabilities that are deemed connected to domestic credit activities. No significant difference in treatment exists with credit institutions in situation 1 as both are liable to the risk tax. Given the lack of important difference in treatment with situation 1, situation 7 is not a relevant benchmark for comparison with situation 1.

[44] However, other issues may arise, especially in the light of the fundamental freedoms. Such issues are, however, outside the scope of this opinion.

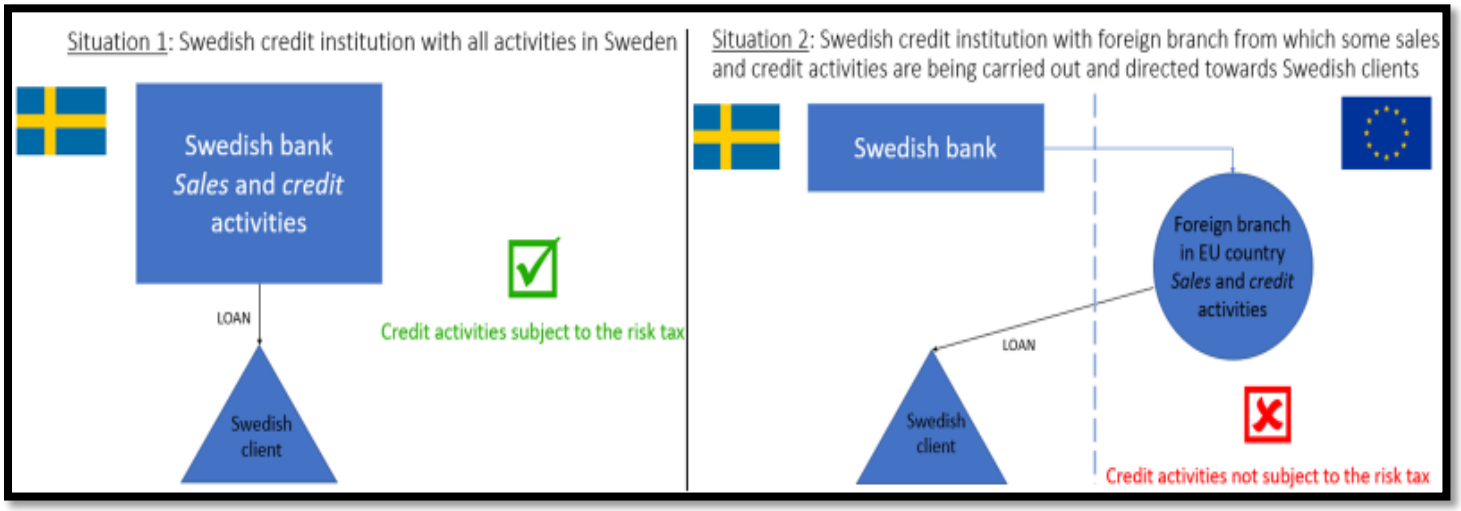
- Credit institutions in situation 8 are not in the scope of the risk tax because of the lack of a permanent establishment in Sweden. However, in situation 8 it is assumed that some sales and credit activities are directed towards Swedish clients, whether remotely or with some limited physical presence in Sweden that does not lead to the existence of a permanent establishment. Situation 8 is a relevant benchmark to use as a comparison with situation 1, because while credit institutions in both situations grant loans to Swedish clients, only credit institutions in situation 1 are subject to the risk tax.

To conclude, the most relevant situations to compare with situation 1 are situations 2, 6 and 8. It must also be emphasised that cross-border situations are not purely theoretical: in reality foreign banks or foreign branches do lend money to Swedish clients. In situations 2, 6 and 8, loans are granted to Swedish clients, but without the foreign credit activities being subject to the risk tax; this is because the credit activities that trigger the liabilities are located abroad (i.e. they would normally appear on a foreign balance sheet), not in Sweden. In these cases, a difference in treatment appears to the disadvantage of Swedish credit institutions in situation 1, and to the advantage of credit institutions in situations 2, 6 or 8. These four situations are illustrated with pictures that are found in appendices 1, 2, 3, and 4, at the end of this opinion.

After having determined which situations to use as a benchmark, I will now proceed with the comparability and justification analyses between situations 1 and 2 (section 6.4.3), situations 1 and 6 (section 6.4.4), and situations 1 and 8 (section 6.4.5). Indeed, as these comparisons are different from each other, I need to analyse them separately. Given the complexity and the diversity of these situations, I have not been able to analyse them in an exhaustive manner. Moreover, definitive answers are difficult to provide given that certain questions do not receive a precise answer in the case law of the Union courts. This confirms the relevance of notifying the suggested risk tax to the European Commission, as suggested in the memorandum drafted by the Swedish Ministry of Finance.

6.4.3 Comparability and justification analyses for situations 1 and 2

To be able to easily compare situations 1 and 2, a picture summarising these situations is presented below:



Situations 1 and 2 could be compared, to some extent, to the *World Duty Free Group* case. In this case, the Grand Chamber of the CJEU found that a measure that favoured cross-border transactions over domestic transactions was selective.[45] The CJEU also held that "a measure (…) designed to facilitate exports, may be regarded as selective if it benefits undertakings carrying out cross-border transactions, in particular investment transactions, and is to the disadvantage of other undertakings which, while in a comparable factual and legal situation, in the light of the objective pursued by the tax system concerned, carry out other transactions of the same kind within the national territory".[46] Since the effect of the suggested risk tax is to provide an advantage to foreign credit activities, it could be compared to an aid to certain export activities: the design of the risk tax provides an incentive to Swedish credit institutions to carry out their credit and sales activities towards Swedish clients from a foreign branch.

In the case of the suggested risk tax, a difference is made between two resident credit institutions, one having domestic activities, the other having foreign activities directed towards the domestic market. In other words, situation 2 has a cross-border element and is subject to a worse treatment than a purely domestic situation.

I will consider factual comparability first. The standard set by the CJEU with respect to factual comparability is such that there must be clear differences between different undertakings in the light of the objective of a given tax, for these undertakings to be in a different factual situation. For example, electricity producers may or may not be in a comparable situation with respect to a tax on the use of inland waters for the production

[45] See Joined Cases C-20/15 P and C-21/15 P, *Commission v World Duty Free Group and Others*.
[46] See Joined Cases C-20/15 P and C-21/15 P, *Commission v World Duty Free Group and Others*, paragraph 119.

of electricity, when they use or do not use water as a source of electricity production;[47] in such a case, the tax makes sense only with respect to certain undertakings, which are not comparable to other undertakings.

From a factual perspective, situations 1 and 2 are comparable when it comes to the presence of the headquarters and the clients in Sweden. Since the European financial sector is largely subject to similar legal – albeit not fiscal – rules, and given that banks are both global and mobile, it is easy for banks to lend from abroad, for example to avoid a domestic bank tax. The fact that domestic and foreign banks have the same clients should, accordingly, be granted some importance in the factual comparability. Despite outsourcing sales and credit functions to the foreign branch, many functions of the bank in situation 2 might still be performed by the head office in Sweden, as is the case in situation 1. The main factual differences concern the sales function (i.e. the direct contact with the clients, potentially including the negotiation of the terms of a loan) and the credit function (i.e. the exercise of functions, by employees of the bank, linked to actually granting loans, assessing risks, deciding on securities, taking on liabilities to provide funds that will be lent to the clients, etc.). These differences are not unsignificant, but do not necessarily imply a lack of factual comparability between situations 1 and 2.

Since factual comparability needs to be assessed in the light of the objective of the tax system – which I suggest consists in the taxation of credit institutions on the basis of their liabilities – a relevant question to ask is how and why liabilities occur. In the present case, credit institutions in situations 1 and 2 that lend money to their Swedish clients might need to take up loans to provide funds to their clients. They would then incur liabilities,[48] no matter where the sales and credit functions are exercised. Therefore, the location of liabilities is not necessarily linked exclusively to the location of the credit activities. The location of liabilities could also be linked to where they arise, i.e. the origin of the liabilities. In that respect, despite the different locations of the credit activities in situations 1 and 2, the origin of the need of credit institutions to borrow money is the same: the conclusion of loan agreements with the clients, and the provision of funds to such clients. Consequently, although the sales and credit activities are located in Sweden (situation 1) or abroad (situation 2), this does not automatically place domestic and foreign liabilities in incomparable factual situations with respect to the objective of the tax system to tax liabilities, since such liabilities occur in connection with loans being provided to the same, Swedish clients.[49] The degree of factual

[47] See Joined Cases C-105/18 to C-113/18, *Asociación Española de la Industria Eléctrica (UNESA) and Others v Administración General del Estado*, paragraphs 66-67.

[48] Once a loan agreement is concluded, credit activities need to be managed, and a credit institution might need to borrow money on the financial markets to be able to provide funds to clients. This is when liabilities arise.

[49] In contrast, it would be irrelevant to tax credit institutions in situation 4, which in my opinion are not comparable to credit institutions in situation 1: indeed, the standard of comparability set by the CJEU in cases such as *UNESA* or *Paint Graphos* supposes, as I understand it, that a tax appears as irrelevant or inapplicable to certain undertakings, for such undertakings and others that are in the scope of the tax to be considered as not comparable.

comparability would be even higher if only credit functions were located in the foreign branch, while sales functions remain at the level of the head office (situation 3).

I now turn to legal comparability. Incomparability from a legal perspective requires true legal differences between the categories of undertakings subject to different tax rules, as emphasised in the *Paint Graphos* case.[50] From a legal perspective, credit institutions in situations 1 and 2 are both resident of Sweden, are subject there to unlimited tax liability for income tax purposes, and are subject to largely similar legal and accounting rules with respect to their Swedish activities. The main difference consists in the existence of a foreign branch, which employs staff responsible for certain sales and credit functions. The branch would normally for accounting and tax purposes prepare financial statements, and it would normally record on its balance sheet the liabilities connected to its credit activities. However, the existence of the liabilities on the balance sheet of the foreign branch would normally not exclude their presence on the balance sheet of the Swedish head office, since the branch and the head office are part of the same legal entity (a Swedish credit institution) which owns both domestic and foreign assets, and incurs both domestic and foreign liabilities. Given the objective of the tax to apply to liabilities, the existence of the liabilities at the level of the Swedish head office would make it possible to levy the risk tax on the foreign liabilities of Swedish credit institutions, not just their domestic liabilities. This possibility may place credit institutions in situations 1 and 2 in a legally comparable situation.

Finally, I will consider potential justifications in case the difference in treatment is deemed *prima facie* selective. Assuming that credit institutions in situations 1 and 2 are in a factual and legal comparable situation, the risk tax would be *prima facie* selective. It may still be justified by the nature or the logic of the tax system. To that end, the reason for discriminating must flow from the nature or the general structure of the system of which the measure forms part.[51] This test is strictly applied by the Union courts and leaves little leeway to the Member States. It must be the intrinsic characteristics of the tax system that make it necessary to treat differently the two categories of undertakings. The judgement of the Grand Chamber of the CJEU in the *A-Brauerei* case illustrates the view of the Court on the possibility to justify a difference in treatment with respect to the intrinsic characteristic of a tax system: the need to avoid double taxation in case of corporate restructurings, and thus in essence the need to preserve the principle of neutrality, justified the exemption from tax in certain cases.[52] In contrast, a tax advantage that is motivated by external reasons, such as the preservation of employment or the safeguard of certain enterprises, has repeatedly been rejected as a justification by the Union courts.[53]

It can also be observed that the Commission notice on the notion of State aid makes clear that "(a) measure which derogates from the reference system (*prima facie*

[50] See Cases C-78/08 to C-80/08, *Paint Graphos*.
[51] See e.g. Case C-203/16 P, *Dirk Andres v European Commission*, paragraph 87; Case C-88/03, *Portuguese Republic v Commission of the European Communities*, paragraph 52.
[52] See Case C-374/17, *Finanzamt B v A-Brauerei*.
[53] See e.g. Case C-6/12, *P Oy*; Case C-88/03, *Paint Graphos*, paragraph 82.

selectivity) is non-selective if it is justified by the nature or general scheme of that system. This is the case where a measure derives directly from the intrinsic basic or guiding principles of the reference system or where it is the result of inherent mechanisms necessary for the functioning and effectiveness of the system. In contrast, it is not possible to rely on external policy objectives which are not inherent to the system".[54] The Commission provides examples of justifications that might be valid: "The basis for a possible justification could, for instance, be the need to fight fraud or tax evasion, the need to take into account specific accounting requirements, administrative manageability, the principle of tax neutrality, the progressive nature of income tax and its redistributive purpose, the need to avoid double taxation, or the objective of optimising the recovery of fiscal debts".[55]

Considering how the justification test has been applied by the Union courts, in this case the Swedish Ministry of Finance would need to demonstrate that the distinction on the basis of the geographical location of the credit activities is mandated by the inner logic of a risk tax on credit institutions. The memorandum does not contain explicit justifications in this situation, but my interpretation is that it is assumed, in the memorandum, that indirect costs for the Swedish State may only be triggered by domestic credit activities, hence justifying the exclusion from the tax base of foreign credit activities.[56] However, the need to generate fiscal revenues to finance indirect costs in case of financial crisis is – in my opinion – more external than internal to the risk tax since the risk tax does not, *per se*, mandate the taxation of solely domestic credit activities and the exclusion of foreign liabilities from the tax base. In addition, it can be questioned whether risks of indirect costs indeed are triggered exclusively in domestic situations, and not at all in cross-border situations. There is a concrete example in Sweden that might be interesting in this respect: the bank Nordea moved its residence from Sweden to Finland in 2018. The Swedish National Debt Office (Swedish: *Riksgälden*) has expressed the view that Nordea's move of its parent entity to Finland "will not decrease the risks posed to financial stability in Sweden". The Swedish National Debt Office has also considered that "the ability of Swedish authorities to avert and manage these risks will shrink".[57] Experience from the financial crisis in 2008-2009 seems also to support the idea that risks of indirect costs may be incurred as a consequence of the activities of foreign banks: Sweden was affected by the situation of foreign banks, and certain countries with no own banks were nevertheless impacted by the crisis. In other words, the need to generate fiscal revenues on domestic credit activities only, to finance indirect costs in case of financial crisis is not, in my view, a valid justification.

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[54] See Commission Notice on the notion of State aid as referred to in Article 107(1) of the Treaty on the Functioning of the European Union, C/2016/2946, paragraph 138.

[55] See Commission Notice on the notion of State aid as referred to in Article 107(1) of the Treaty on the Functioning of the European Union, C/2016/2946, paragraph 139.

[56] See *Riskskatt för vissa kreditinstitut*, Fi2020/03725/S1, particularly at p. 25 where it is mentioned that "*Eftersom skatten är tänkt att kompensera för indirekta kostnader i Sverige i händelse av en finansiell kris, bör endast sådana skulder beaktas som är hänförliga till verksamhet som kreditinstitutet bedriver i Sverige*".

[57] See https://www.riksgalden.se/en/press-and-publications/press-releases-and-news/news/2018/risks-stemming-from-nordea-will-not-decrease-following-change-of-domicile/ (accessed 5 January 2021).

Moreover, if the aim of generating fiscal revenues to finance indirect costs in case of financial crisis were deemed as intrinsic to the risk tax system, it would still need to be proportionate.[58] In this respect, the difference in treatment between situations 1 and 2 may not be proportionate: the two banks are Swedish banks with Swedish clients, the only difference being the existence of a foreign branch from which sales and credit activities are carried out. However, it is not obvious that risks of indirect costs are triggered only in situation 1, and not at all in situation 2. It may very well be so that the Swedish State is exposed to risks of indirect costs in situation 2, since the bank is Swedish and certain functions such as management functions are performed in Sweden. As mentioned above, it seems doubtful that no risks at all are incurred in cross-border situations.[59] However, situation 2 is excluded from the scope of the tax. Therefore, it seems (although this question would need to be analysed more in details to provide a more definitive answer) that the difference in treatment may not be proportionate to the actual risks of indirect costs for the Swedish State.

There are other potential justifications when comparing situations 1 and 2. One justification could be the need to avoid double taxation: indeed, if the bank in situation 2 were subject to the risk tax, and that the country of its foreign branch would levy a comparable risk tax on the credit activities of the foreign branch, a situation of international double taxation would arise. However, this justification does not seem convincing. On the one hand, the current case law of the CJEU in the area of fiscal State aid may deem the prevention of domestic double taxation as a valid justification,[60] but not necessarily the prevention of international double taxation. Indeed, international double taxation is not an issue that is intrinsic to a single tax system, as it occurs as a consequence of the combination of several tax systems. This means that the internal logic of a tax system cannot, in my opinion, mandate the elimination of international double taxation by a given State. On the other hand, even if the prevention of international double taxation were an acceptable justification, there may be less discriminatory measures to eliminate such double taxation: the risk tax could be levied on the worldwide liabilities of all Swedish credit institutions, with a tax credit being provided in case a similar tax is levied abroad on the liabilities of a foreign branch.

Another potential justification could be the fiscal principle of territoriality, i.e. the right of a country to tax only domestic activities, and exempt from tax foreign activities. Such a potential justification has not been clearly accepted by the CJEU in the area of fiscal State aid, but it cannot be excluded that this principle is deemed as a valid justification,

[58] For selective measures to be justified, it must be demonstrated that the measures "are proportionate and do not go beyond what is necessary to achieve the legitimate objective being pursued, in that the objective could not be attained by less far-reaching measures": see Commission Notice on the notion of State aid as referred to in Article 107(1) of the Treaty on the Functioning of the European Union, C/2016/2946, paragraph 140, referring to the *Paint Graphos* case.
[59] See https://www.riksgalden.se/en/press-and-publications/press-releases-and-news/news/2018/risks-stemming-from-nordea-will-not-decrease-following-change-of-domicile/ (accessed 5 January 2021).
[60] See particularly Case C-374/17, *Finanzamt B v A-Brauerei*.

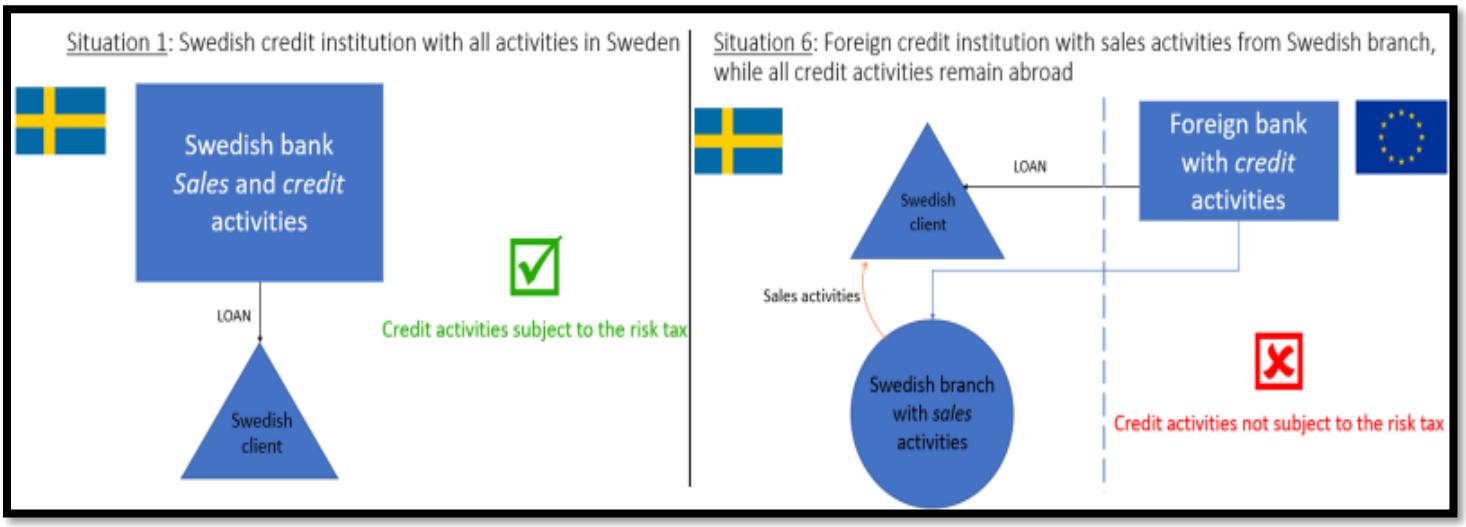
as it is a traditional principle of taxation particularly accepted in the area of the fundamental freedoms applied to direct taxation.[61]

To conclude, there are potential compatibility issues with the State aid rules when it comes to situations 1 and 2. This conclusion should be equally valid if one compares situations 1 and 3, since the degree of factual comparability would be even higher in situation 3. A difference in treatment with situation 1 would thus be less motivated.

After comparing situations 1 and 2, attention is now put on a comparison between situations 1 and 6.

6.4.4 Comparability and justification analyses for situations 1 and 6

To be able to easily compare situations 1 and 6, two pictures summarising these situations are presented below:



To start with, it can be observed that in the field of the fundamental freedoms, resident and non-resident banks have been found to be in a comparable situation with respect to the determination of the tax base.[62] This does not, however, imply that the same result should be reached in the field of fiscal State aid.

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[61] See Case C-382/16, *Hornbach-Baumarkt AG v Finanzamt Landau*, paragraph 40, where the principle of territoriality is recognized as a principle "whereby Member States are entitled to tax income generated on their territory". See also Case C-250/95, *Futura Participations SA and Singer v Administration des contributions*, paragraph 22.

[62] See Case C-311/97, *Royal Bank of Scotland plc*, paragraph 29: "It is true that companies having their seat in Greece are taxed there on the basis of their world-wide income (unlimited tax liability) whereas foreign companies carrying on business in that State through a permanent establishment are subject to tax there only on the basis of profits which the permanent establishment earns there (limited tax liability). However, that circumstance, which arises from the limited fiscal sovereignty of the State in which the income arises in relation to that of the State in which the company has its seat is not such as to prevent the two categories of companies from being considered, all other things being equal, as being in a comparable situation as regards the method of determining the taxable base".

From a factual perspective two facts are similar between situations 1 and 6: the sales function and the client are located in Sweden. So both the origin of the need to incur liabilities (the clients to whom a loan is granted), and the actual performance of sales functions are in Sweden. As mentioned above in section 6.4.3, the fact that domestic and foreign banks have the same clients should be granted some importance in the factual comparability analysis, since banks can easily lend from abroad thanks to the European financial sector being largely subject to similar rules, and given that banks are both global and mobile. In contrast, as in situation 2, situation 6 is characterized by the credit function being performed abroad. However, as mentioned above the fact that the credit function is performed abroad does not need to automatically exclude the comparability between the two situations. In this case the existence of liabilities is at least partly linked to the granting of loans, which relies on the performance of the sales function and the conclusion of contracts with the client, both of which are present in Sweden. Consequently, there are arguments pointing both to the comparability and the lack of comparability of situations 1 and 6 from a factual perspective.

From a legal perspective, situations 1 and 6 are marked by an important difference, since the two banks are resident of different countries: Sweden (situation 1) and another country of the European Union (situation 6). Banks in situation 6 have no fiscal residence in Sweden, and no unlimited tax liability for corporate income tax purposes. The liabilities incurred by banks in situation 6 are normally recorded on the balance sheet of the foreign bank, and would probably not be mentioned on the balance sheet of the Swedish branch, since it is assumed in this situation that loans are being granted and managed from the foreign head office. This points to the lack of comparability from a legal perspective, if one is to follow a legal or accounting perspective. The *Paint Graphos* case may also point to the lack of legal comparability between situations 1 and 6, since the consequence of the foreign residence and the foreign registration of liabilities result in the lack of liabilities on a Swedish balance sheet.

On the other hand, one might argue on the basis of the *Gibraltar* case that the exclusion of liabilities from the tax base in situation 6 is a consequence of the choice made in the design of the risk tax to rely on where liabilities are formally incurred based on a legal or accounting perspective, while disregarding the origin of the liabilities. The *Gibraltar* case might support the view according to which one should not pay too much attention to legal incomparability when it is the consequence of the regulatory technique used in the design of the tax.[63] In addition, in situation 6 there is no impossibility to levy a risk tax on the foreign bank. The foreign bank has a branch in Sweden; although a branch

[63] See Joined cases C-106/09 P and C-107/09 P, *European Commission (C-106/09 P) and Kingdom of Spain (C-107/09 P) v Government of Gibraltar and United Kingdom of Great Britain and Northern Ireland*, paragraph 92, where the CJEU refused a conception of the selectivity criterion according to which "in order for a tax system to be classifiable as 'selective' it must be designed in accordance with a certain regulatory technique". Indeed, the Court found that "the consequence of this would be that national tax rules fall from the outset outside the scope of control of State aid merely because they were adopted under a different regulatory technique although they produce the same effects in law and/or in fact".

has a limited liability to corporate income tax, it could be used as a means to levy the risk tax on the foreign bank. Consequently, there are arguments pointing both to legal comparability, and legal incomparability of situations 1 and 6.

If situations 1 and 6 were comparable from a legal and factual perspective, the risk tax would be *prima facie* selective. It may still be justified by the nature or the logic of the tax system. I will first consider the argument according to which only domestic credit activities would trigger a risk of indirect costs. I have already mentioned the objection consisting in the more extrinsic nature of this argument, which is also valid when comparing situations 1 and 6. This argument would also be contradicted by the fact that foreign credit institutions may actually trigger higher risks of indirect costs for Sweden than Swedish banks, because of the high requirements applying in Sweden to ensure financial stability. I have also referred to the view expressed by the Swedish National Debt Office according to which the foreign residence of a bank may not remove all risks for the Swedish financial stability.[64] In other words, I do not find this justification valid.

The need to prevent double taxation would not either be a valid justification, since international double taxation does not occur as a consequence of the tax system of a single State: therefore, the internal logic of a tax system cannot mandate the elimination of international double taxation by a given State since the elimination of international double taxation reflects more an international policy ambition than the intrinsic need of a domestic tax system.

In contrast, the fiscal principle of territoriality might be a more convincing justification. According to this principle, a Member State has normally a right to limit its tax jurisdiction on foreign companies to domestic income. Indeed, non-residents are traditionally taxed on a territorial basis, for example in the areas of income tax, wealth tax, gift tax and death tax. By limiting its taxing rights to its territory, a host State does not tax in an extra-territorial manner, gives priority to the State of residence, and preserves its taxing rights on domestic income. This right has been recognized in the areas of direct taxation and the fundamental freedoms in the *Futura*[65] and *Centro Equestre*[66] cases, but was somewhat contradicted in the *Sofina*[67] case. Transposed to the risk tax, the fiscal principle of territoriality would enable the State where a branch is located to only tax the liabilities allocated to the branch, and disregard the foreign liabilities. However, the fiscal principle of territoriality might not be directly transposable to the area of fiscal State aid and the context of a risk tax on the liabilities of credit institutions. The case law of the CJEU does not explicitly support such a

[64] See https://www.riksgalden.se/en/press-and-publications/press-releases-and-news/news/2018/risks-stemming-from-nordea-will-not-decrease-following-change-of-domicile/ (accessed 5 January 2021).
[65] See Case C-250/95, *Futura Participations SA and Singer v Administration des contributions*, paragraph 22.
[66] See Case C-345/04, *Centro Equestre da Lezíria Grande Lda v Bundesamt für Finanzen*, paragraph 22.
[67] See Case C-575/17, *Sofina SA and Others v Ministre de l'Action et des Comptes publics*.

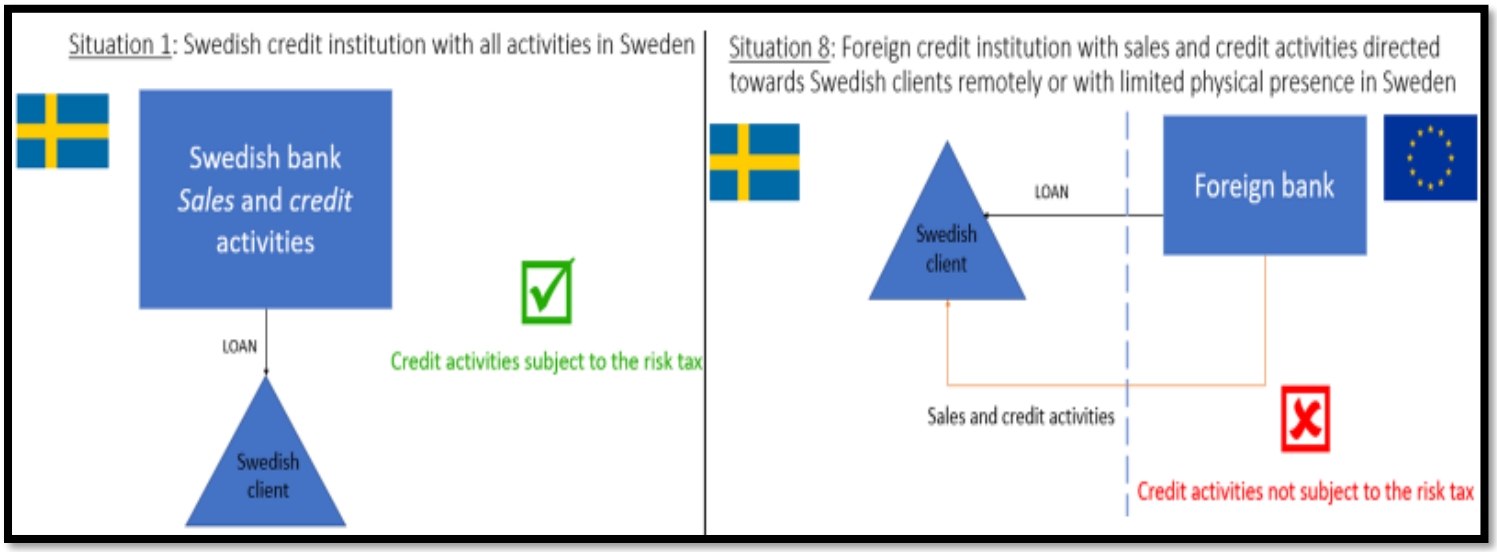
transposition, but it does not either preclude it. Therefore, the validity of this justification cannot be fully ascertained.

Finally, two justifications mentioned in the State aid notice might be relevant in this case: the need to take into account "specific accounting requirements", and "administrative manageability".[68] Since it is assumed in situation 6 that the liabilities are recorded on the balance sheet of the foreign bank and do not appear on the balance sheet of the Swedish branch, there would be no objective way to determine the tax base of the branch if part of the liabilities were to be attributed it. A fiction might be possible, but it might be legally uncertain, and might increase the risk of international double taxation if this method is not recognized by the State of residence of the foreign credit institution. Consequently, these justifications might be valid.

To conclude, there is no clear answer as to the possibility to justify the difference in treatment between situations 1 and 6. After comparing situations 1 and 6, I will finally compare situations 1 and 8.

6.4.5 Comparability and justification analyses for situations 1 and 8

To be able to easily compare situations 1 and 8, two pictures summarising these situations are presented below:



In situation 8 it is assumed that a foreign credit institution has no branch in Sweden, yet lends money to Swedish clients. This situation is not purely theoretical; it is a reality, probably helped by the progress of digitalization. Situation 8 has a factual difference with situation 6, namely the fact that the sales functions are performed remotely, or with limited physical presence in Sweden. This tends to decrease the factual comparability with situation 1. Legally, the foreign bank in situation 8 has no branch in

[68] See Commission Notice on the notion of State aid as referred to in Article 107(1) of the Treaty on the Functioning of the European Union, C/2016/2946, paragraph139.

Sweden, which decreases legal comparability. Ultimately, whether or not the situations are comparable in the light of the objective to tax liabilities will ultimately depend on the perspective taken as to the existence of liabilities:[69] under a legal and accounting perspective, the objective to tax liabilities cannot be met, because of the lack of a branch. If one does not rely on a legal or accounting perspective, but rather considers the origin of the liabilities, a higher degree of comparability may exist, since part of the liabilities of the foreign bank may not exist without lending money to a Swedish client, and performing certain sales functions directed towards this client. The *Gibraltar* case may support this view, on the basis that the lack of domestic liabilities in situation 8 is the consequence of the choice made to rely on the existence of a permanent establishment for corporate income tax purposes to potentially be in the scope of the tax, and on legal as well as accounting considerations to potentially attribute liabilities to such a permanent establishment. However, the *Gibraltar* case is sometimes seen as an exception, and the CJEU has not often found situations to be comparable in the area of fiscal State aid on the basis of such a way of reasoning. Therefore, it is unlikely that situations 1 and 8 are deemed factually and legally comparable in the light of the objective to tax the liabilities of credit institutions. This would mean that the difference in treatment between situations 1 and 8 is not selective. If situations 1 and 8 nevertheless were comparable, the two justifications mentioned above concerning "specific accounting requirements" and "administrative manageability"[70] would, in my opinion, be even more valid to justify the advantage given in situation 8, since no branch exists in Sweden and thus no liabilities can in an objective manner be deemed to exist in Sweden.

7 Conclusion

To conclude, the territorial scope of the suggested risk tax presents complex challenges from a State aid perspective. Because of the complexity and the diversity of situations where the risk tax may or may not apply, I have not been able to analyse all issues in the most thorough manner. Therefore, this legal opinion does not contain definitive conclusions as to the compatibility with the State aid rules and the internal market of the territorial scope of the suggested risk tax. However, certain tensions with the State aid rules have been identified, thereby justifying further analysis, and the notification of the envisaged risk tax to the European Commission in accordance with Article 108(3) of the TFEU.

From a general perspective, it is assumed in the memorandum that only domestic credit activities may trigger risks of indirect costs for the Swedish State in case of financial

[69] For example, under an accounting-based perspective the liabilities might appear on the balance sheet of the legal entity that actually takes up a loan. Under an income tax-based perspective, countries that follow the recommendations of the OECD (the so-called authorised OECD approach) would tend to allocate the liabilities to the entity where the significant people functions relevant for the management of loans are actually located. The proposal for a risk tax on certain credit institutions does not contain very precise guidance with respect to this issue.

[70] See Commission Notice on the notion of State aid as referred to in Article 107(1) of the Treaty on the Functioning of the European Union, C/2016/2946, paragraph139.

crisis, hence the exclusion of liabilities connected to foreign credit activities. However, this assumption may not be fully correct. As a result, there may be an inconsistency between the aim and the design of the tax.

Further, the exemption from tax in situation 2 appears as particularly problematic from a State aid perspective. In this case, the degree of comparability with situation 1 is relatively high, the potential justifications of a difference in treatment not particularly strong, and there is a possibility that the advantage given in situation 2 goes beyond what is necessary to achieve the legitimate objective pursued by the risk tax. The *World Duty Free Group* case tends also to support the view that the risk tax may be compared to an aid to certain export activities (exempted from the tax), as opposed to domestic activities (in the scope of the tax). The degree of factual comparability would be even higher in situation 3 (Swedish credit institution with foreign branch from which some credit activities are being carried out, while all sales activities remain in Sweden); a difference in treatment with situation 1 would thus be less motivated.

The difference in treatment between situations 1 and 6 appears more acceptable from a State aid perspective, and even more so for situations 1 and 8. However, since several of the issues emphasised in this opinion do not receive precise answers in the case law of the Union courts, it cannot be concluded with all certainty to the potential compatibility, or incompatibility of the territorial scope of the suggested risk tax with the State aid rules and the internal market. It therefore appears justified to notify the measure to the European Commission, as suggested in the memorandum drafted by the Swedish Ministry of Finance.

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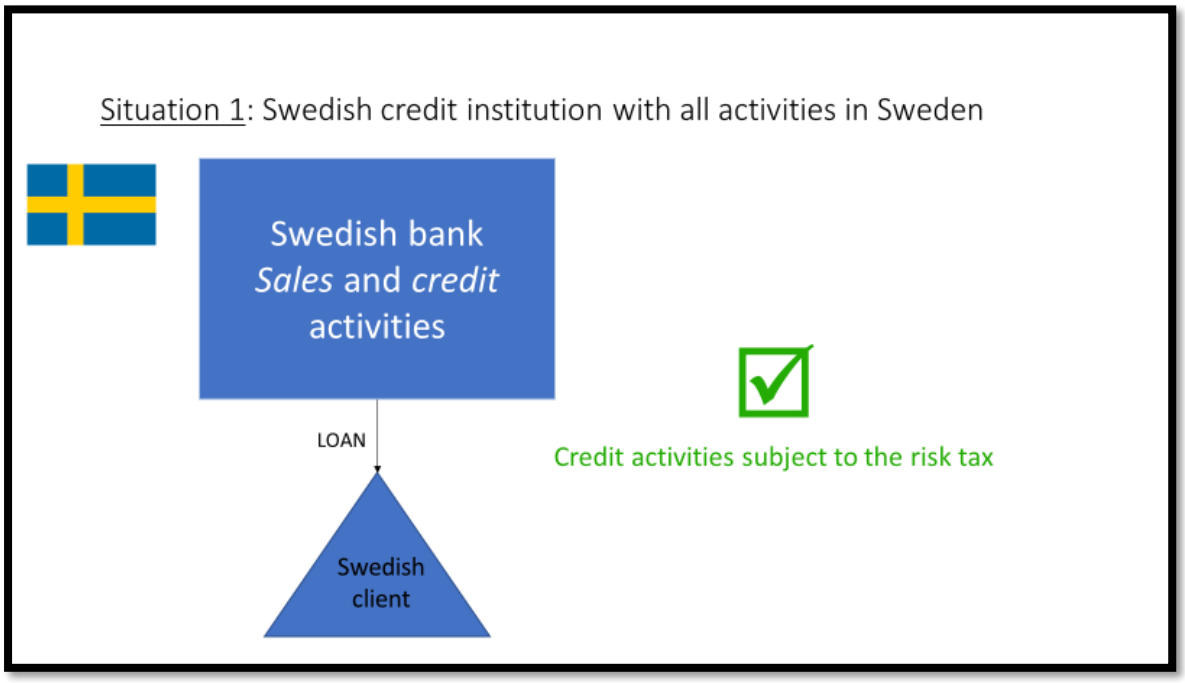
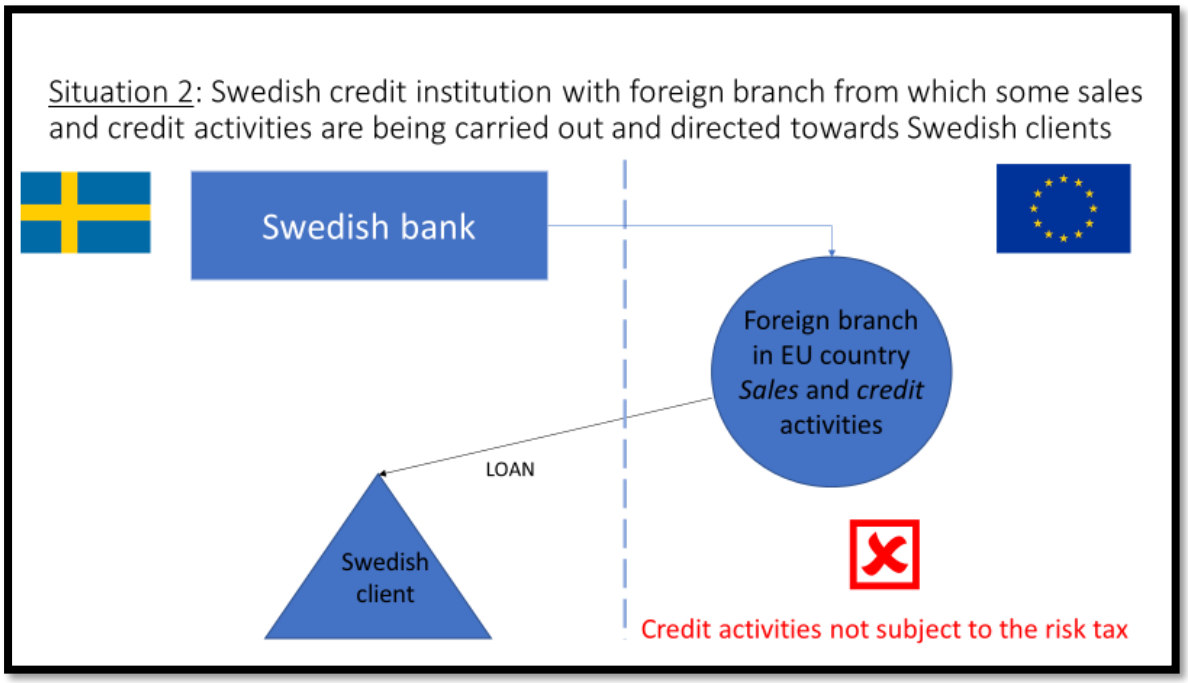
Prof. Dr. Jérôme Monsenego
Stockholm, 1 February 2021

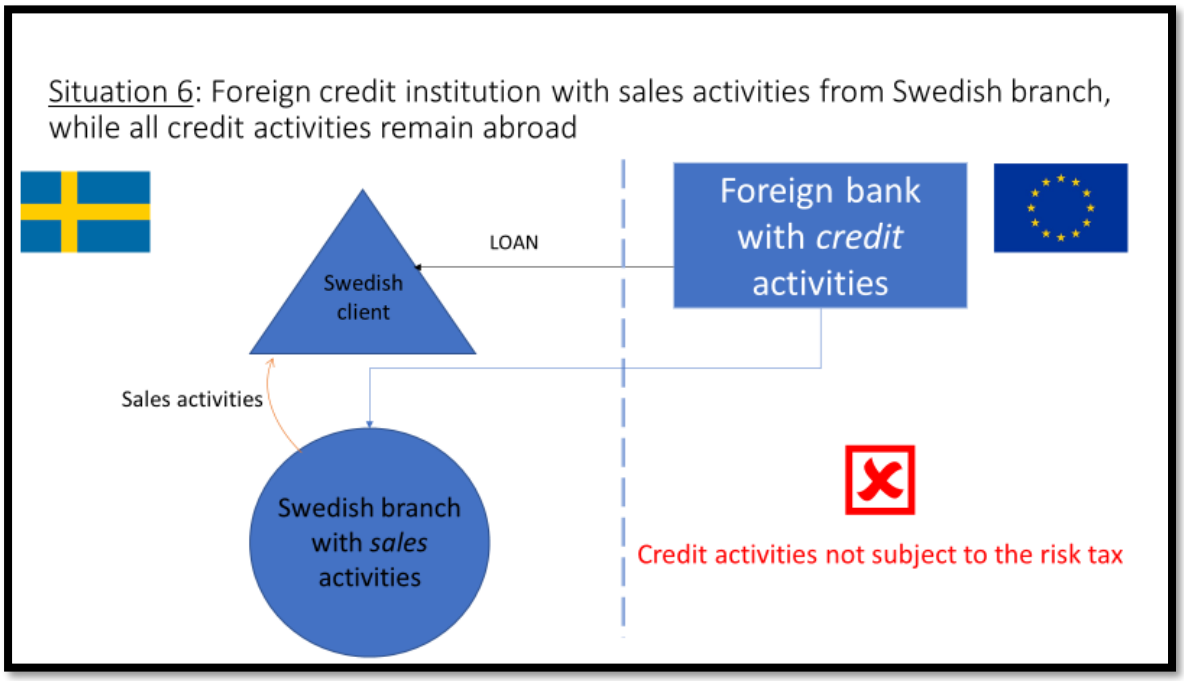
Appendix 1


Situation 1: Swedish credit institution with all activities in Sweden
Swedish bank
Sales and credit
activities
LOAN
Swedish
client
Credit activities subject to the risk tax

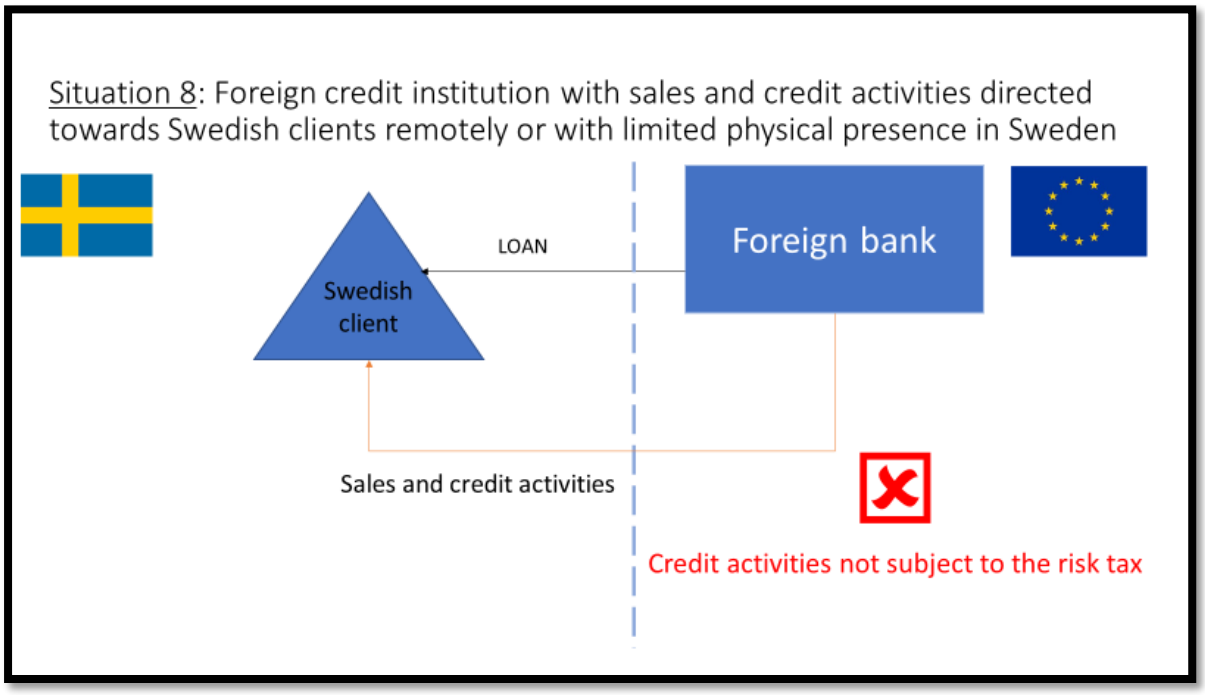
Appendix 2


Situation 2: Swedish credit institution with foreign branch from which some sales and credit activities are being carried out and directed towards Swedish clients
Swedish bank
Foreign branch in EU country *Sales* and *credit* activities
LOAN
Swedish client
Credit activities not subject to the risk tax

Appendix 3


Situation 6: Foreign credit institution with sales activities from Swedish branch, while all credit activities remain abroad
LOAN
Swedish client
Foreign bank with *credit* activities
Sales activities
Swedish branch with *sales* activities
Credit activities not subject to the risk tax

Appendix 4


Situation 8: Foreign credit institution with sales and credit activities directed towards Swedish clients remotely or with limited physical presence in Sweden
LOAN
Swedish client
Foreign bank
Sales and credit activities
Credit activities not subject to the risk tax