OPINION OF ADVOCATE GENERAL KOKOTT

delivered on 8 May 2008 [1]

I — Introduction

1. The three Historical Territories of Biscay (Vizcaya), Álava (Araba) and Guipúzcoa (Gipuzkoa) are independent regional authorities and together form the Autonomous Community of the Basque Country. By virtue of traditional special rights (*fueros*) they have their own legislative powers in the field of tax law. Under those powers, they set the corporation tax rate for companies established in their territory at 32.5%. In contrast, a corporation tax rate of 35% is generally applicable in Spain. In addition, the Territories have introduced special rules governing the way certain investments are taken into account for tax purposes, which have no equivalent in Spanish tax law.

2. In the view of the neighbouring regions of La Rioja and Castilla y León and the trade union Unión General de Trabajadores de La Rioja (UGT-Rioja), those tax rules infringe higher-ranking national law and constitute unlawful State aid for the purposes of Articles 87 EC and 88 EC. They therefore brought an action before the Tribunal Superior de Justicia del País Vasco (High Court of Justice of the Basque Country), which has made the present seven references for preliminary rulings, [2] which are largely identical, to the Court of Justice.

3. Above all, it is unclear whether the tax measures adopted by the Historical Territories favour 'certain undertakings or the production of certain goods' compared with others and whether they are selective in nature. If the entire territory of Spain is chosen as the reference framework, the measure would be regionally selective. Only undertakings established in a certain part of Spain, namely the Historical Territories, would benefit from the tax rules in question.

4. However, in its judgment of 6 September 2006 in *Portugal* v *Commission* [3] in connection with tax rules in the Portuguese Region of the Azores (the '*Azores* judgment'), the Court made clear that the entire national territory of the Member State does not necessarily provide the reference framework for tax measures adopted by a regional or

1 — Original language: German.

2 — Case C-428/06 *Unión General de Trabajadores de La Rioja (UGT-Rioja)* v *Juntas Generales del Territorio Histórico de Vizcaya*.Case C-429/06 *Comunidad Autónoma de La Rioja* v *Juntas Generales del Territorio Histórico de Vizcaya*.Case C-430/06 *Comunidad Autónoma de La Rioja* v *Diputación Foral de Álava*.Case C-431/06 *Comunidad Autónoma de Lla Rioja* v *Diputación Foral de Guipúzcoa*.Case C-432/06 *Comunidad Autónoma de Castilla y León* v *Juntas Generales de Guipúzcoa and Diputación Foral de Guipúzcoa*.Case C-433/06 *Comunidad Autónoma de Castilla y León* v *Juntas Generales del Territorio Histórico de Álava and Diputación Foral de Álava*.Case C-434/06 *Comunidad Autónoma de Castilla y León* v *Diputación Foral de Vizcaya and Juntas Generales del Territorio Histórico de Vizcaya*.

3 — Case C-88/03 [2006] ECR I-7115.

local authority. If such an authority has sufficient autonomy, its territory alone may also form the relevant geographical reference framework. In that case, rules which favour all undertakings located in the territory in the same way are a general, non-selective measure which does not satisfy the definition of State aid.

5. The Court of Justice and the Court of First Instance have now dealt with or are still dealing with tax measures in the Historical Territories of Biscay, Álava and Guipúzcoa in more than 40 cases. [4] However, the rules contested in the present proceedings have not yet been the subject-matter of proceedings. The Commission and the Court of First Instance did not base their conclusion that the tax measures previously examined were selective solely on their territorial scope, but also on other conditions which restricted the circle of beneficiaries, such as the size of the undertakings or the fact that the undertaking was newly established. [5]

6. In the present cases, however, only the nature of the tax rules as regional measures is crucial. This gives the Court of Justice an opportunity to develop further the case-law it initiated in the *Azores* judgment. In particular, it must clarify what requirements are to be placed on the autonomy of regional and local authorities for their tax rules to be classified as independent measures which do not form part of the national framework.

II — Legal framework

A — *Spanish Constitution*

7. The following provisions of the Spanish Constitution are particularly relevant in the present context:

'*Article 2* — The Constitution is based on the indissoluble unity of the Spanish nation, the common and indivisible country of all Spaniards. It recognises and guarantees the right to autonomy of the nationalities and regions of which it is composed, and the solidarity among them all.

Article 31 — 1. Everyone shall contribute to sustain public expenditure according to his or her economic capacity through a fair tax system based on the principles of equality

4 — At present Joined Cases T-30/01 to T-32/01 and T-86/02 to T-88/02 and Joined Cases T-227/01 to T-229/01, T-265/01, T-266/01 and T-270/01 are still pending before the Court of First Instance.

5 — Joined Cases T-127/99, T-129/99 and T-148/99 *Diputación Foral de Álava and Others* v *Commission* [2002] ECR II-1275, paragraph 146; Joined Cases T-92/00 and T-103/00 *Diputación Foral de Álava and Others* v *Commission* [2002] ECR II-1385, paragraph 27; and Joined Cases T-346/99 to T-348/99 *Diputación Foral de Álava and Others* v *Commission* [2002] ECR II-4259, paragraph 52.

and progressive taxation, which shall not in any event be confiscatory in scope.

Article 139 — 1. All Spaniards have the same rights and obligations in any part of the State territory.

…'

2. No authority may adopt measures which directly or indirectly obstruct freedom of movement and establishment of persons or free movement of goods throughout the Spanish territory.

8. Title VIII of the Constitution is dedicated to the territorial organisation of the State and includes the following provisions:

Article 143 — 1. In the exercise of the right to autonomy recognised in Article 2 of the Constitution, bordering provinces with common historical, cultural and economic characteristics, the island territories, and provinces constituting a historical regional entity may accede to self-government and form Autonomous Communities in accordance with the provisions of this Title and the respective Statutes [of Autonomy].

'*Article 137* — The State is organised territorially into municipalities, provinces and the Autonomous Communities which may be constituted. All these entities shall enjoy autonomy for the management of their respective interests.

Article 138 — 1. The State shall guarantee the effective implementation of the principle of solidarity laid down in Article 2 of the Constitution by endeavouring to establish a fair and adequate economic balance between the different parts of the Spanish territory and taking into special consideration the circumstances pertaining to those which are islands.

…'

9. Article 148 and Article 149 contain lists of matters in which the Autonomous Communities may assume competences and areas in which the State retains exclusive competence. The possible duties of Autonomous Communities include the promotion of the economic development of the Autonomous Community within the scope of objectives set by national economic policy (Article 148(1)(13)).

2. The differences between the statutes of the individual Autonomous Communities may not in any event imply economic or social privileges.

10. Articles 156 to 158 contain more detailed provisions on finances:

'*Article 156* — 1. The Autonomous Communities shall enjoy financial autonomy for the development and exercise of their powers, in conformity with the principles of coordination with the State Treasury and solidarity among all Spaniards.

2. The Autonomous Communities may act as delegates or agents of the State for the collection, management and settlement of the latter's tax resources, in conformity with the law and the Statutes [of Autonomy].

Article 157 — 1. The resources of the Autonomous Communities shall consist of:

(a) taxes wholly or partially assigned to them by the State; surcharges on State taxes and other shares in State revenue;

(b) their own taxes, rates and special levies;

(c) transfers from an inter-territorial compensation fund and other allocations to be charged to the State budget;

(d) revenue accruing from their property and private law income;

(e) revenue from credit operations.

2. Under no circumstances may the Autonomous Communities adopt measures which impose taxes on property located outside their territory or which hinder the free movement of goods or services.

…

Article 158 — 1. An allocation may be made in the State budget to the Autonomous Communities in proportion to the amount of State services and activities for which they have assumed responsibility and to guarantee a minimum level of basic public services throughout the Spanish territory.

2. With the aim of correcting inter-territorial economic imbalances and implementing the principle of solidarity, a compensation fund shall be set up for investment expenditure, the resources of which shall be distributed by the Cortes Generales [Spanish Parliament] among the Autonomous Communities and the provinces, as the case may be.'

B — *Statute of Autonomy*

11. The Autonomous Community of the Basque Country has its constitutional basis in the Statute of Autonomy of 1979, [6] under Article 40 of which it has its own autonomous treasury.

12. Furthermore, Article 41(1) of the Statute of Autonomy provides that public finance relations between the State and the Basque Country are regulated by the traditional system of the Concierto Económico (Economic Agreement) based on the *fueros*. Article 41(2) lays down the following principles for the Economic Agreements:

'(a) The competent institutions of the Historical Territories [Basque provinces in which the special right of *fueros* applies] may maintain, establish and regulate, within their own territory, the tax system, bearing in mind the general tax structure of the State, the rules contained in the Economic Agreement itself for coordination, fiscal harmonisation and cooperation with the State, and those which the Basque Parliament may adopt for the same purposes within the Autonomous Community….

(b) The levying, management, liquidation, collection and inspection of all taxes, except customs duties… shall be carried out, within each Historical Territory, by the respective Diputaciones Forales, without prejudice to cooperation with the State and its inspection service.

(c) The competent institutions of the Historical Territories shall adopt the relevant agreements, with the object of applying within their respective territories whatever exceptional or provisional tax rules the State may decide to enforce in the common territory. Such rules shall remain in force for the same length of time as indicated for those State rules.

(d) The Basque Country's contribution to the State shall consist of an overall quota, made up of the individual quotas of each of its territories, as a contribution towards all State burdens that are not assumed by the Autonomous Community.

6 — Adopted by Ley Orgánica de las Cortes Generales Españolas (Spanish Parliament) No 3/1979 of 18 December 1979. Available in an English translation at http://www.lehendakaritza.ejgv.euskadi.net/r48-2312/en/contenidos/informacion/estatuto_guernica/en_455/estatu_com_i.html.

(e) In order to determine the quotas for each Historical Territory which makes up the abovementioned overall quota, a Joint Committee shall be set up, consisting, on the one hand, of one representative of each Diputación Foral and the same number of representatives of the Basque Government and, on the other, of an equal number of representatives of the State Administration. The quota thus set shall be adopted by law at intervals to be determined in the Economic Agreement, without prejudice to its annual adjustment by a procedure likewise to be established in the [Economic] Agreement.

(f) The system of [Economic] Agreements shall be applied in accordance with the principle of solidarity to which Articles 138 and 156 of the Constitution refer.'

C — *Economic Agreement*

13. The Economic Agreement between the Autonomous Community of the Basque Country and Spain of 2002,[7] which applies in the present cases, replaces the previous agreement of 1981. Articles 2 to 4 of the Economic Agreement lay down principles which must be observed by the Historical Territories in the organisation of the tax system:

'Article 2. General principles

1. The tax system established by the Historical Territories shall comply with the following principles:

(1) Respect for the principle of solidarity in the terms laid down in the Constitution and in the Statute of Autonomy.

(2) Compliance with the general tax structure of the State.

(3) Coordination, fiscal harmonisation and cooperation with the State, in accordance with the rules laid down in the present Economic Agreement.

(4) Coordination, fiscal harmonisation and mutual cooperation between the institutions of the Historical Territories pursuant to the provisions enacted by the Basque Parliament for those purposes.

7 — Adopted by Law No 12/2002 of 23 May 2002 (Ley por la que se aprueba el Concierto Económico con la Comunidad Autónoma del País Vasco, BOE No 124 of 24 May 2002). Available at www.ogasun.ejgv.euskadi.net/r51-341/es/contenidos/informacion/concierto_quinquenal/es_4177/adjuntos/CAST.pdf.

(5) Submission to the international treaties or agreements signed and ratified by the Spanish State or to those of which it is a party.

In particular, it shall comply with the provisions laid down in the international agreements signed by Spain for the avoidance of double taxation and the fiscal harmonisation rules of the European Union, and shall be responsible for making the refunds to be made as a result of the application of those agreements and rules.

2. The rules laid down herein shall be interpreted in accordance with the provisions of the Tax Code [Ley General Tributaria] for the interpretation of tax law.

Article 3. Fiscal harmonisation

In drafting their tax legislation, the Historical Territories shall:

(a) respect the Tax Code in matters of terminology and concepts, without prejudice to the special circumstances laid down in the present Economic Agreement;

(b) maintain an overall effective fiscal pressure equivalent to that in force in the rest of the State;

(c) respect and guarantee freedom of movement and of establishment of persons and free movement of goods, capital and services throughout the territory of Spain, without giving rise to discrimination or a restriction of the possibilities of commercial competition or to distortion in the allocation of resources;

(d) use the same system for classifying livestock, mining, industrial, commercial, service, professional and artistic activities as is used in the common territory, without prejudice to further classifications of those activities that might be made.

Article 4. Principle of cooperation

1. The competent institutions of the Historical Territories shall inform the State Administration, giving due advance notice, of any draft tax legislation.

Similarly, the State Administration shall inform the aforementioned institutions of any such drafts.

2. The State shall develop mechanisms for allowing the institutions of the Basque Country to participate in any international agreements affecting the application of the present Economic Agreement.

3. The State and the Historical Territories, in the exercise of functions within their powers regarding the administration, inspection and collection of taxes, shall, without delay and in due form, exchange any information and records deemed necessary with a view to levying them more efficiently.

In particular, both Administrations shall:

(a) provide each other, through their data-processing centres, with any information they may require. To this end, the necessary technical connections between them shall be set up. A jointly coordinated fiscal data-processing system plan shall be drawn up on a yearly basis.

(b) The inspection services shall draw up joint inspection plans for coordinated selective objectives, sectors and procedures, and for taxable persons who have changed their place of residence, undertakings declaring under the tax transparency system and companies subject to corporation tax proportionate to turnover.'

14. Article 14(1) governs the division of fiscal sovereignty with regard to corporation tax as follows:

'Corporation tax is agreed to be a coordinated tax subject to autonomous legislation by the Basque authorities for taxable persons having their fiscal domicile in the Basque Country.

Without prejudice to the above paragraph, taxable persons whose turnover in the previous tax year exceeded EUR 6 million, and who performed 75% or more of their total operations in that tax year in the common territory, shall be subject to the law of that territory.

Autonomous law shall also apply to taxable persons with their fiscal domicile in the common territory whose turnover in the previous tax year exceeded EUR 6 million and whose entire operations were performed in the Basque Country.'

15. Articles 48 to 60 of the Economic Agreement govern the financial relations between the State and the Basque Country. Articles 48 to 50 state:

'Article 48. General principles

The financial relations between the State and the Basque Country shall be governed by the following principles:

1. Fiscal and financial autonomy of the institutions of the Basque Country in the regulation and implementation of their powers.

2. Respect for the principle of solidarity in the terms laid down in the Constitution and the Statute of Autonomy.

3. Coordination and cooperation with the State in matters of budgetary stability.

4. Contribution by the Basque Country to State burdens not assumed by the Autonomous Community, in the form determined by the present Economic Agreement.

5. The faculties of financial supervision developed by the State at any time in matters concerning local or regional authorities shall be enjoyed by the competent institutions of the Basque Country, without this being construed to mean, in any way, that the Basque local or regional authorities have a lower level of autonomy than that enjoyed by those under the common regime.

Article 49. Quota

The Basque Country's contribution to the State shall consist in an overall quota, comprising the quotas from each of the Historical Territories as the Basque Country's share of all the State burdens not assumed by the Autonomous Community of the Basque Country.

Article 50. Frequency and adjustment of the quota

1. Every five years, by means of a law passed by the Cortes Generales [Spanish Parliament], subject to the prior approval of the Joint Committee on the Economic Agreement, the methodology to be used in setting the quota for the following five-year period shall be determined in accordance with the general principles laid down herein, and the quota for the first year of the five-year period shall be approved.

2. In each of the years following the first, the Joint Committee on the Economic Agreement shall adjust the quota by applying the methodology approved in the law referred to in the preceding paragraph.

3. The principles underlying the methodology for determining the quota and contained herein may be amended in the Law on the quota, when circumstances and the experience acquired in its application make this advisable.'

16. Under Articles 63 and 64 the compatibility of tax legislation with the Economic Agreement may be assessed prior to its publication by a Coordination and Evaluation Committee composed of an equal number of representatives. At the request of one of its members, the committee considers objections to rules and attempts to reach an amicable solution.

D — *Law on the quota in the five-year period 2002 to 2006*

17. By Law No 13/2002, [8] the methodology for determining the quota for the Basque Country for 2002 to 2006 was adopted. It provides inter alia as follows:

'Article 3. Determination of the quota for the base year

The net quota for the base year of the five-year period from 2002 to 2006 shall be determined by applying the attribution rate to the total amount of the burdens not assumed by the Autonomous Community and by making the relevant adjustments and compensations, as provided for in the following articles.

Article 4. State burdens not assumed by the Autonomous Community

1. State burdens not assumed by the Autonomous Community are those which correspond to competences the exercise of which has not actually been assumed by the Autonomous Community.

2. In order to determine the total amount of such burdens, the entire budget allocation which, at State level, corresponds to the areas of competences assumed by the Autonomous Community from the date of entry into force of the transfer established in the corresponding Royal Decrees shall be deducted from the total State budget expenditure. …

8 — Law No 13/2002 of 23 May 2002 (Ley por la que se aprueba la metodología de señalamiento del cupo del País Vasco para el quinquenio 2002-2006, BOE No 124 of 24 May 2002). Available at www.ogasun.ejgv.euskadi.net/r51-341/es/contenidos/informacion/concierto_quinquenal/es_4177/adjuntos/CAST.pdf.

Article 5. Adjustments

1. Without prejudice to the provisions of Articles 14 and 15 below, the figures resulting from the attribution referred to in Article 4(4) shall be adjusted to improve the accuracy of the estimated income from direct taxes attributable to the Basque Country and to the rest of the State territory pursuant to Article 55 of the Economic Agreement. …

Article 6. Compensation

1. From the quota corresponding to each Historical Territory the following items shall be deducted:

(a) the attributable portion of non-transferred taxes;

(b) the attributable portion of budgetary income not from taxes;

(c) the attributable portion of the deficit figuring in the general State budget. …

Article 7. Attribution rate

The attribution rate referred to in Articles 4 and 6 above, set essentially in accordance with the income of the Historical Territories in proportion to that of the State, shall be 6.24% for the current five-year period.'

18. Other provisions of the Law govern the adjustments to the quota which must be made in subsequent years with reference to the base year 2002.

E — *Basque legislation*

19. The financial and tax system set up by the provisions reproduced above is supplemented by Law of the Basque Country No 27/1983 of 25 November 1983. That law fixes the proportion of the tax revenue which the Historical Territories must transfer to the Basque Country after deduction of the quota payable to the State.

20. In addition, a body for tax coordination within the Basque Country was set up by Law of the Basque Country No 3/1989 of 30 May 1989. That body produces reports on the draft tax legislation proposed by the Historical Territories.

F — *The contested rules of the Historical Territories*

21. Cases C-428/06, C-429/06 and C-434/06 concern Norma Foral No 7/2005 of the Juntas Generales of Biscay of 23 June 2005, Article 2 of which amends Norma Foral No 3/1996 of 26 June 1996 on corporation tax (del Impuesto sobre Sociedades): [9]

— Article 2(4) amends Article 29 of Norma Foral No 3/1996 to the effect that the tax rate is set at 32.5%;

— Article 2(6) amends Article 37 of Norma Foral No 3/1996 and provides that investments made in new tangible fixed assets of certain kinds intended for the economic operation of the undertaking may be deducted at a rate of 10% from the corporation tax liability;

— Article 2(7) amends Article 39 of Norma Foral No 3/1996. Under that provision, taxable persons may deduct from the corporation tax liability a sum equal to 10% of the accounting income for the financial year as a reserve for production investments and/or as a reserve for environmental conservation and improvement activities.

22. The corporation tax rate applicable in Biscay thus departs from the rate of 35% which applies generally in Spain. [10] The tax deductions under Articles 37 and 39 of Norma Foral No 3/1996 have no equivalent in Spanish corporation tax law.

23. The subject of Cases C-430/06 and C-433/06 is Decreto Foral Normativo de Urgencia Fiscal No 2/2005 of the Consejo de Diputados of **Álava** of 24 May 2005, paragraphs 4 and 5 of whose sole article amend Articles 29 and 37 of Norma Foral No 24/1996 of 5 July 1996 on corporation tax. The rules are similar to the contested provisions for Biscay.

24. Lastly, Cases C-431/06 and C-432/06 relate to Decreto Foral No 32/2005 of the Diputación Foral de **Guipúzcoa** of 24 May 2005, which amends Articles 29 and 37 of Norma Foral No 7/1996 of 4 July 1996 on corporation tax. The rules are similar to the contested provisions of the other Historical Territories.

9 — The applicants in the main proceedings in Cases C-428/06 and C-429/06 claimed that Article 2(4), (6) and (7) of the Norma Foral should be annulled, whilst only Article 2(4) and (6) is at issue in Case C-434/06.

10 — See Article 28(1) of the Law on corporation tax revised by Real Decreto-Legislativo No 4/2004 of 5 March 2004.

III — Facts of the case and questions referred for a preliminary ruling

25. Even before the provisions at issue in these proceedings were adopted, similar rules existed for the three Historical Territories. By judgment of 9 December 2004, however, the Tribunal Supremo (Supreme Court) annulled those predecessor provisions (Cassation proceedings No 7893/1999). [11] The court examined the Normas Forales with particular reference to the constitutional principles of autonomy, equal treatment, the unity of the State and solidarity, as well as competition and freedom of establishment. In its judgment, it stated that the abovementioned principles did not preclude taxation in the Historical Territories which departed from the general tax system. Account also had to be taken of their constitutionally guaranteed autonomy. On the other hand, where the differences constituted State aid for the purposes of Article 87(1) EC this went beyond the limits of what was constitutionally lawful.

26. Having regard to the case-law of the Court of Justice and of the Court of First Instance, the Tribunal Supremo then analysed the individual provisions and concluded inter alia that the reduced tax rate, the rules on the deduction of certain investments in tangible fixed assets and the special reserves constituted aid. It annulled those and several other provisions because they had not been notified to the Commission pursuant to Article 88(3) EC, without making reference to the Court of Justice for a preliminary ruling.

27. After the Historical Territories had adopted the rules with the same content which are contested in these proceedings, the neighbouring regions of La Rioja and Castilla y León and UGT-Rioja then challenged them before the Tribunal Superior de Justicia del País Vasco. Because the *Azores* judgment had been delivered by the Court of Justice in the meantime, [12] that court considered it necessary to request a preliminary ruling and, by orders of 20 September 2006, referred the following question in Cases C-428/06, C-429/06 and C-434/06:

'Must Article 87(1) EC be construed as meaning that, by providing for a rate of tax lower than the basic rate set in Spanish State legislation and for deductions from the amount of tax payable which do not exist in State tax legislation, provisions in the field of taxation adopted by the Juntas Generales del Territorio Histórico de Vizcaya amending Articles 29(1)(a), 37 and 39 of the Provincial Law on Company Tax, which take effect in the jurisdiction of that infra-State autonomous body, must be regarded as selective and as covered by the definition of State aid

11 — Annex 8 to the Commission's written statement.

12 — Cited in footnote 3.

enshrined in Article 87(1) EC and, accordingly, must be notified to the Commission pursuant to Article 88(3) EC?'

IV — Legal assessment

A — *Admissibility of the reference for a preliminary ruling*

28. The questions referred in the other cases relate to the parallel provisions of the Historical Territories of Álava (C-430/06 and C-433/06) and Guipúzcoa (C-431/06 and C-432/06), but are otherwise identical.

29. By order of the President of the Court of Justice of 30 November 2006, the cases were joined.

30. In the proceedings before the Court of Justice, the Unión General de Trabajadores de La Rioja (UGT-Rioja), the Comunidad Autónoma de La Rioja, the Comunidad Autónoma de Castilla y León, the Diputación Foral de Guipúzcoa, Confederación Empresarial Vasca (Confebask), the Spanish, Italian and United Kingdom Governments, and the Commission of the European Communities submitted observations. In addition, the Juntas Generales del Territorio Histórico de Vizcaya, the Diputación Foral de Álava, the Diputación Foral de Vizcaya and the Cámara de Comercio, Industria y Navegación de Bilbao submitted joint observations.

31. UGT-Rioja and the Comunidad Autónoma de La Rioja had originally alleged that the reference for a preliminary ruling was inadmissible. UGT-Rioja had argued that Norma Foral No 7/2005 of the Juntas Generales of Biscay had already been annulled or its application had been suspended. The Comunidad Autónoma de La Rioja had claimed that the contested rules of all three Territories had been annulled by an order of the Tribunal Superior de Justicia del País Vasco of 14 November 2005 (confirmed by an order of 17 March 2006) in application of the judgment of the Tribunal Supremo of 9 December 2004.

32. However, both parties withdrew their pleas of inadmissibility shortly before the hearing. The information on the status of those judicial proceedings, which the parties provided in response to a question from the Court of Justice at the hearing, did not give a clear picture. The interim measures adopted appear to have been partially suspended, whilst the corresponding orders relating to some Normas Forales are probably not final.

33. It must be stated first of all that the withdrawal of the pleas of inadmissibility is irrelevant because the Court of Justice would also have to establish inadmissibility of its own motion. In this connection, the fact that the contested rules may have been annulled or suspended could give rise to doubts as to the need for the reference for a preliminary ruling.

34. It is settled case-law, however, that, in the context of the cooperation between the Court of Justice and the national courts provided for by Article 234 EC, it is solely for the national court before which the dispute has been brought, and which must assume responsibility for the subsequent judicial decision, to determine in the light of the particular circumstances of the case the need for a preliminary ruling in order to enable it to deliver judgment. [13]

35. Where questions submitted by national courts concern the interpretation of a provision of Community law, the Court of Justice is thus bound, in principle, to give a ruling unless it is obvious that the request for a preliminary ruling is in reality designed to induce the Court to give a ruling by means of a fictitious dispute, or to deliver advisory opinions on general or hypothetical questions, or that the interpretation of Community law requested bears no relation to the actual facts of the main action or its purpose, or that the Court does not have before it the factual or legal material necessary to give a useful answer to the questions submitted to it. [14]

36. In the main proceedings, which are still pending, the applicants are challenging the rules of the Historical Territories. In this connection, the referring court asks a question concerning the interpretation of Article 87 EC. There is no evidence to suggest that the legal disputes have been settled or have become hypothetical in nature because the provisions have already been annulled in other proceedings. In any case, the Tribunal Superior de Justicia del País Vasco, whose assessment takes precedence, has referred the matter to the Court even though, according to the parties, the validity of the provisions was apparently called into question in interlocutory proceedings by that very court. It is for the referring court and not the Court of Justice to assess, on the basis of national procedural law, the effects of the decisions adopted in that context. [15]

37. Moreover, Confebask does not consider the references to be necessary because the answer is already clear beyond doubt from the *Azores* judgment. The Court could also give its decision by an order under Article 104(3) of its Rules of Procedure. However, this is not a plea of inadmissibility strictly speaking. In the case of proceedings

13 — Case C-415/93 *Bosman* [1995] ECR I-4921, paragraph 59; Case C-28/95 *Leur-Bloem* [1997] ECR I-4161, paragraph 24; and Case C-275/06 *Promusicae* [2008] ECR I-271, paragraph 36.

14 — Case C-275/06 *Promusicae* (cited in footnote 13), paragraph 37.

15 — See Joined Cases C-482/01 and C-493/01 *Orfanopoulos and Oliveri* [2004] ECR I-5257, paragraph 42; Case C-28/04 *Tod's* [2005] ECR I-5781, paragraph 14; and Case C-246/04 *Turn- und Sportunion Waldburg* [2006] ECR I-589, paragraph 21.

under Article 104(3) of the Rules of Procedure the request is not inadmissible but can be answered only in a simplified procedure. However, there are no grounds to suggest that this is the case because the answer to the question referred is not obvious from the case-law and the answer also leaves room for reasonable doubt.

38. The reference for a preliminary ruling is therefore admissible.

B — *The question referred*

39. The referring court essentially seeks to ascertain under what conditions tax measures adopted by local authorities which are more favourable than the tax rules applicable in the rest of the Member State are selective in nature and therefore constitute State aid for the purposes of Article 87(1) EC, which must be notified to the Commission under Article 88(3) EC.

40. Before I examine more closely, in the light of the facts in the main proceedings, the circumstances under which tax rules may be regarded as selective, I would like to recall the main features of the *Azores* judgment.

1. The *Azores* judgment

41. In the *Azores* judgment, the Court considered in detail for the first time the 'regional selectivity' of tax rules. The starting point is the settled case-law on the condition of selectivity. It is clear from that case-law that Article 87(1) EC requires assessment of whether, under a particular statutory scheme, a State measure is such as to 'favour certain undertakings or the production of certain goods' in comparison with other undertakings which are in a legal and factual situation that is comparable in the light of the objective pursued by the measure in question. [16]

42. In principle, taxes are not an advantage, but a charge. However, tax measures may be aid in certain cases where the State levies lower taxes than normal or levies no tax at all. Because the concept of State aid is broader than the concept of subsidy, it also covers the mitigation of charges which are normally included in the budget of an undertaking. [17] In order to assess the nature of a tax measure as aid, 'normal' taxation from which the contested regime departs in a selective

16 — *Azores* judgment (cited in footnote 3), paragraph 54, with reference to Case C-143/99 *Adria-Wien Pipeline and Wietersdorfer & Peggauer Zementwerke* [2001] ECR I-8365, paragraph 41; Case C-308/01 *GIL Insurance and Others* [2004] ECR I-4777, paragraph 68; and Case C-172/03 *Heiser* [2005] ECR I-1627, paragraph 40.

17 — Case 30/59 *De Gezamenlijke Steenkolenmijnen in Limburg* v *High Authority* [1961] ECR 1, 19; Case C-387/92 *Banco Exterior de España* [1994] ECR I-877, paragraph 13; and Case C-200/97 *Ecotrade* [1998] ECR I-7907, paragraph 34.

manner is needed. [18] Differences in taxation are justified where the differentiation arises from the nature or the overall structure of the tax system. [19]

43. The main innovation of the *Azores* judgment is that the Court did not consider that the Member State as a whole had to be the reference framework. Instead, it also considered it possible that for tax rules adopted by a local or regional authority its territory alone forms the reference framework if that authority is sufficiently autonomous in relation to the central government of the Member State. [20]

44. In its earlier case-law on aid from local and regional authorities, the Court had stressed above all that such aid is attributable to the State. [21] Following on from that, in its previous decision-making practice the Commission has regarded rules which were not applicable to the national territory as a whole as selective measures even if they were adopted by local or regional authorities. [22]

45. In determining the reference framework for assessing a reduced tax rate in part of a Member State, the Court distinguished three situations in the *Azores* judgment, following the line taken in the Opinion of Advocate General Geelhoed: [23]

— The central government unilaterally decides that the applicable national tax rate should be reduced within a defined geographical area (*situation 1*).

— Fiscal sovereignty is transferred by the central State to all local authorities at a certain level which have the autonomous power to decide, within the limit of the powers conferred on them, the tax rates applicable in the territory within their competence (*situation 2*).

18 — *Azores* judgment (cited in footnote 3), paragraph 56.

19 — *Azores* judgment (cited in footnote 3), paragraph 52, with reference to Case 173/73 *Italy* v *Commission* [1974] ECR 709, paragraph 33, and Case C-148/04 *Unicredito Italiano* [2005] ECR I-11137, paragraph 51.

20 — *Azores* judgment (cited in footnote 3), paragraph 58.

21 — Case 248/84 *Germany* v *Commission* [1987] ECR 4013, paragraph 17; see also the Opinion of Advocate General Saggio in Joined Cases C-400/97 to C-402/97 *Juntas Generales de Guipúzcoa and Others* [2000] ECR I-1073, point 31. The Court of Justice also essentially adheres to this view in the *Azores* judgment (see paragraph 55 of that judgment, cited in footnote 3).

22 — See Commission Decision 2003/442/EC of 11 December 2002 on the part of the scheme adapting the national tax system to the specific characteristics of the Autonomous Region of the Azores which concerns reductions in the rates of income and corporation tax (OJ 2003 L 150, p. 52, paragraphs 26 to 32), which was contested in the *Azores* judgment, and Commission Decision 2005/261/EC of 30 March 2004 on the aid scheme which the United Kingdom is planning to implement as regards the Government of Gibraltar corporation tax reform (OJ 2005 L 85, p. 1, paragraphs 102 to 109), against which actions for annulment have been brought by Gibraltar and the United Kingdom before the Court of First Instance (Cases T-211/04 and T-215/04).

23 — Opinion in Case C-88/03 *Portugal* v *Commission* [2006] ECR I-7115, points 50 to 54.

— A regional or local authority adopts, in the exercise of sufficiently autonomous powers in relation to the central power which other authorities do not hold (asymmetry), a tax rate lower than the national rate which is applicable only to undertakings present in the territory within its competence (*situation 3*).

46. In *situation 1*, the measure is undoubtedly selective. Because here the national level establishes both the general standard and the regional difference, only the State as a whole can be taken as the reference framework.

47. In *situation 2*, there is no 'normal taxation' applying to the national territory as a whole from which the rules of the individual local or regional authorities depart in an advantageous manner. The relevant local rules therefore stand in isolation and are not selective. [24]

48. This is similar to the relationship between the different Member States' tax rules. Since direct taxation falls within the competence of the Member States, [25] corporation tax rates are not harmonised, but differ considerably from one Member State to the next. Whilst the tax rate in Bulgaria and in Cyrus is only 10%, the EU average is around 25%. [26] Even though the different tax rates certainly influence competition, particularly low rates which apply to all the undertakings in a Member State do not constitute aid because there is no general system in the Community.

49. *Situation 3* is characterised by an asymmetrical division of competences. In some areas, the local or regional authorities have certain rule-making powers which are held by the central authorities in the rest of the national territory. The crucial factor is the level of autonomy enjoyed by the local and regional authorities in their legislative activity.

50. If the central State actually determines the content of the local rules and/or bears the relevant economic consequences, there is no real autonomy. The local rules are

24 — See the Opinion in the *Azores* case (cited in footnote 23), point 53. See also the notice of the Commission (1998 Commission notice on the application of the State aid rules to measures relating to direct business taxation (OJ 1998 C 384, p. 3), paragraph 16, and the report on the implementation of that notice of 9 February 2004, C[2004] 434, paragraph 33). In legal literature, the German system of trade tax, where the municipalities set the tax rate, is therefore regarded as selective (Stein, R.M., *Bestimmtheit von Regionalbeihilfen*, 2007, p. 167 et seq.).

25 — See, inter alia, Case C-446/03 *Marks & Spencer* [2005] ECR I-10837, paragraph 29; Case C-196/04 *Cadbury Schweppes and Cadbury Schweppes Overseas* [2006] ECR I-7995, paragraph 40; and Case C-374/04 *Test Claimants in Class IV of the ACT Group Litigation* [2006] ECR I-11673, paragraph 36.

26 — The figures are taken from the Eurostat study, *Taxation trends in the European Union*, 2007, p. 32, Tables 1-6, available at www.ec.europa.eu/taxation_customs/resources/documents/taxation/gen_info/economic_analysis/tax_structures/Structures2007.pdf.

attributable to the central State. Its general rules form the benchmark for assessing whether the local rules accord a selective advantage. If the territory of the authority were used as the reference framework solely because the rules were adopted formally by the local or regional authority, the Member States could easily circumvent the prohibition of State aid. They would merely have to transfer the competences for adopting the relevant rules formally to the local or regional authorities. [27]

— The rule-making regional or local authority has, from a constitutional point of view, a political and administrative status separate from that of the central government — *institutional autonomy*.

— The rules must have been adopted without the central government being able to intervene directly as regards their content — *procedural autonomy*.

51. If, on the other hand, the contested measure adopted by the local authority were adopted in the exercise of sufficiently autonomous powers, *situation 3* is comparable with *situation 2*. The rules of several legislators acting on the basis of their own competence — here the central State and the local and regional authorities — do not have a common reference framework.

— The financial consequences of a reduction of the national tax rate for undertakings in the region concerned must not be offset by aid or subsidies from other regions or central government — *financial autonomy*.

2. Application of the findings from the *Azores* judgment to the measures adopted by the Historical Territories

52. Like Advocate General Geelhoed, [28] the Court has linked the question whether sufficient autonomy exists to three criteria which must be met cumulatively:

53. As in the case of the *Azores*, it seems reasonable to assume an asymmetrical division of competences along the lines of *situation 3* in the case of the Historical Territories. In Spain too, tax legislation falls within the competence of the central State in principle. Unlike the other local and regional authorities, only the Historical Territories have their

27 — See the Opinion of Advocate General Saggio in *Juntas Generales de Guipúzcoa and Others* (cited in footnote 21), point 37.

28 — See the Opinion in the *Azores* case (cited in footnote 23), point 54.

own powers in this field.[29] The question whether the tax rules at issue in the main proceedings should be related to the provisions which apply in the rest of Spain or are to be regarded as independent rules therefore depends on the autonomy of the Territories in the exercise of their powers.

(a) Preliminary observations

54. First of all, I would like to mention that under Article 6(3) EU the European Union must respect the national identities of its Member States. This means that the Union cannot encroach on the constitutional order of a Member State, whether it is centralist or federal, and does not in principle have any influence on the division of competences within a Member State. The revision of that provision by the Treaty of Lisbon expressly mentions respect for the constitutional structures of the Member States by the Union.[30]

55. The Court has consistently held, however, that a Member State cannot plead provisions, practices or situations prevailing in its domestic legal order, including those resulting from the constitutional organisation of that State, to justify the failure to observe obligations arising under Community law.[31]

56. In the *Azores* judgment, the Court struck a reasonable balance between these two principles. On the one hand, it respects the autonomy which the Constitution of the Member State in question grants to its local and regional authorities. If the limited territorial application of local tax rules alone were to give grounds for the selectivity of a measure, the autonomy which the national Constitution accords the local or regional authority would be very questionable. Any local rules which are more favourable than the tax law of the central State, meet the other requirements to satisfy the definition of aid and exceed the *de minimis* threshold would require approval by the Commission. This would be granted only if a ground for justification holds, such as the promotion of economically underdeveloped areas under Article 87(3)(a) EC.

57. On the other hand, the requirements relating to the autonomy of the local legislator ensure that the Member States cannot hide behind their constitutional order and circumvent the prohibition on aid under Article 87 EC through a purely formal transfer of legislative powers.

29 — In addition to Biscay, Álava and Guipúzcoa, the Autonomous Community of Navarre also has similar fiscal sovereignty on the basis of historical special rights (*fueros*).

30 — The first sentence of Article 3a(2) EU (after renumbering Article 4 EU) as amended by the Treaty of Lisbon amending the Treaty on European Union and the Treaty establishing the European Community, signed at Lisbon on 13 December 2007 (OJ 2007 C 306, p. 1), states:'The Union shall respect the equality of Member States before the Treaties as well as their national identities, inherent in their fundamental structures, political and constitutional, inclusive of regional and local self-government.'

31 — See, in particular, Case C-212/06 ***Government of the*** *French Community and Walloon Government* [2008] ECR I-1683, paragraph 58, with further references.

58. Account must be taken of this balance in applying the findings in the *Azores* judgment to the present cases.

59. However, two factors distinguish the present cases from the *Azores* case. First of all, there is a different procedural situation. The *Azores* judgment was given in an action for annulment brought by Portugal pursuant to the first paragraph of Article 230 EC against a Commission decision. The Court therefore had to give a final decision itself on whether the Commission proved that the contested measure constituted State aid.

60. In the present preliminary ruling proceedings under Article 234 EC, on the other hand, the Court's task is limited to interpreting Article 87(1) EC. Even though the Court considers the specific situation in the main proceedings, the referring court is still responsible for assessing whether the contested rules of the Historical Territories are to be classified as selective measures and thus as State aid. [32] The question referred, which asks the Court of Justice to assess the specific measures, must therefore be construed as I have formulated it in point 39 of this Opinion.

61. Secondly, it should be borne in mind that the Azores were given the power to reduce the national tax rate in order to compensate for structural disadvantages for the region's undertakings as a result of insularity. [33] So that the tax rate reduction did not also weaken the region financially, the central State compensated for the resulting shortfalls in tax revenue. The Court concluded that financial responsibility for the regional tax rules is borne not by the region itself, but ultimately by the central State, and therefore took the basic State tax level as the reference framework for assessing the selectivity of the regional tax rate. [34]

62. It is not clear that the tax rules of the Historical Territories of the Basque Country are intended to compensate for similar geographical or other structural disadvantages. Rather, the tax regime, which is more favourable than the general rules, seeks to create special incentives to attract businesses. At the same time, however, it is not in the logic of the system — unlike in the *Azores* case — for the central State to compensate for shortfalls in revenue which the Historical Territories suffer as a result of the tax advantages.

32 — See also the case-law cited in footnote 13.

33 — The Commission also recognised this in principle and considered the tax reduction to be partially justified on the basis of Article 87(3)(a) EC. It merely objected that the reduced tax rate also applied to the financial sector, which is not affected by insularity in the same way (see the *Azores* judgment (cited in footnote 3), paragraph 27 et seq.).

34 — *Azores* judgment (cited in footnote 3), paragraph 71 et seq.

63. Lastly, it must be assumed that the contested rules actually apply in the same way to all economic operators subject to the fiscal sovereignty of the Historical Territories. In this connection the Commission claims that on the one hand the Historical Territories also tax revenue obtained outside their territory and on the other they do not tax income earned within the Territories.

64. This is because under the first sentence of Article 14(1) of the Economic Agreement the division of fiscal sovereignty between the central State and the Basque Country is linked first and foremost to the domicile of the undertaking. Within certain limits, revenue which is not earned at the domicile is nevertheless subject to taxation on the basis of domicile status. However, there is no provision for general limited tax liability for permanent establishments at their place of establishment linked with a crediting of tax or exemption of that revenue at the undertaking's main place of business. In this respect, the division of fiscal sovereignty departs from the rules common in international tax law. However, it does not follow that taxation in the Basque Country is selective. Rather, it applies in the same way to all undertakings subject to its tax regime in accordance with the division of fiscal sovereignty.

(b) Substantive scope of political and financial autonomy

65. In the view of the Commission, in the *Azores* judgment the Court requires a two-stage examination for assessing the autonomy of the local authority. First of all, it must be examined whether the authority 'plays a fundamental role in the definition of the political and economic environment in which undertakings operate'.[35] Only when this has been established is it relevant whether the three criteria relating to autonomy in paragraph 67 of the judgment have been satisfied.

66. The Commission argues that the Historical Territories actually have only very limited powers to define the environment for businesses. Under Article 41 of the Statute of Autonomy, they may regulate tax law. However, they do not really influence the use of tax revenue. The revenue is largely transferred to the Autonomous Community of the Basque Country and to the State. Consequently, there is not sufficient autonomy for that reason.

67. The Commission is right to state that the competitive situation of undertakings is influenced not only by the tax regime, but by many other local factors, such as the availability of skilled labour, the structure of labour law and of social security, or infrastructure. However, this does not necessarily

35 — *Azores* judgment (cited in footnote 3), paragraph 58.

mean that 'sufficient autonomy' can be taken to exist only where an infra-State body possesses such extensive powers that it is able to influence all these factors.

68. Even the Member States no longer possess full autonomy in economic policy. They must conduct their economic policies in accordance with the principles laid down in Article 98 EC and must coordinate those policies within the Council under Article 99 EC. Many rules which are relevant in terms of location have been harmonised at Community level, such as rules in the field of labour law, environmental protection, public procurement law and protection of intellectual property. In some areas, such as agriculture, external trade and transport, national policy is also overlaid by a Community policy.

69. On closer examination of the relevant passage of the *Azores* judgment, which the Commission reproduces only in abridged form, it also becomes clear that the Court is concerned with autonomy in adopting the specific measures and not general freedom to act in economic policy. Thus, it considers it possible that 'an infra-State body enjoys a legal and factual status which makes it sufficiently autonomous in relation to the central government of a Member State, with the result that, *by the measures it adopts*, [36] it is that body and not the central government which plays a fundamental role in the definition of the political and economic environment …'. [37] The Court is obviously referring to the tax rules at issue in the *Azores* case.

70. If the Commission were correct in its interpretation of the *Azores* judgment, it would be incomprehensible why the Court did not reject autonomy in that case too because the regional competences were restricted to adjusting the tax rate. Instead, it examined in detail whether in the exercise of that competence the region acted autonomously from an institutional, procedural and financial point of view.

71. The Commission's argument must therefore be rejected.

(c) The correct connecting factor: the individual Historical Territories or the Autonomous Community of the Basque Country?

72. In assessing the selectivity of the contested measures and examining the autonomy of the respective local and regional authorities, the question arises, first of all,

36 — My emphasis.

37 — *Azores* judgment (cited in footnote 3), paragraph 58.

whether the Autonomous Community of the Basque Country as a whole or the three Historical Territories are to be compared with the central State.

73. Under Article 41(1) of the Statute of Autonomy it is for the Historical Territories to adopt tax rules, which, as has just been stated, is the significant factor. The provisions laid down in Articles 2 to 4 of the Economic Agreement are addressed to them. They exchange information on tax legislation directly with the central State's Treasury and send their own representatives to the Coordination and Evaluation Committee under Articles 63 and 64 of the Economic Agreement. This is an argument in favour of examining the autonomy of the individual Historical Territories.

74. It is evident, however, that coordination within the Basque Country clearly results in the Normas Forales of all three Territories being largely identical. There might therefore be doubts as to the legislative independence of the individual Territories. In that connection, a distinction must be drawn between two scenarios:

— The Historical Territories are compelled, in fact or in law, by the coordination within the Basque Country to adopt uniform rules; coordination is independent of provisions laid down by the central State.

— The Territories are bound, in the context of coordination, by provisions of the Autonomous Community, which are in turn based on provisions laid down by the central State.

75. In the first case, fiscal sovereignty is exercised jointly by all three Territories and possibly also by the Autonomous Community. In this case, legislative coordination within the Basque Country would possibly restrict the autonomy of the Territories in relation to one another, but not the (joint) autonomy in relation to the central State. However, only the relationship between the central State and the local or regional authorities is relevant in assessing the selectivity of tax rules which apply in the same way to all undertakings under that authority. It would therefore be necessary to examine whether the Territories, acting jointly, or the Territories and the Autonomous Community together possess sufficient autonomy vis-à-vis the central State.

76. In the second scenario, on the other hand, the autonomy of the Historical Territories would be called into question indirectly by the provisions of the central State. It is for the referring court to clarify whether either of the two scenarios exists and to draw the necessary consequences.

77. Lastly, it would also be conceivable that the Autonomous Community of the Basque Country can influence the tax legislation of the Historical Territories in such a way

that more favourable conditions apply in one part of the Basque Country than in the other parts. In that case, a selective measure might exist where the reference framework was provided not by the central State, but by the Basque Country. However, there is no evidence in support of such an assumption in the information available to the Court.

(d) The application of the individual criteria

78. The institutional autonomy of the Historical Territories and their organs is beyond doubt for the referring court and all the parties to the proceedings before the Court of Justice. There is therefore no need for further consideration of that criterion. The objections raised by the applicant in the main proceedings, and by the Commission, are directed only at the procedural and financial autonomy of the Historical Territories.

79. The Commission rightly identifies two aspects in connection with procedural autonomy. The first aspect, which could also be called procedural economy in the strict sense, concerns the local authority's freedom to adopt the tax rules in a procedure in which the central State has no influence or at least no decisive influence. The second aspect relates to the substantive discretion enjoyed by the local authority under the national legal order. In order better to illustrate this second aspect, I would like to use hereinafter, rather than the expression procedural autonomy, the expression *organisational autonomy*, in fact procedural and substantive organisational autonomy.

(i) Organisational autonomy

80. As the Court found in paragraph 67 of the *Azores* judgment, the local rules must be adopted 'without the central government being able to directly intervene as regards its content'.

81. However, in this connection it refers to point 54 of the Opinion in which the Advocate General employed a broader approach: 'The decision must be taken by the local authority pursuant to a procedure where the central government does not have any power to intervene directly in the procedure of setting the tax rate, *and without any obligation on the part of the local authority to take the interest of the central State into account in setting the tax rate.*' [38]

82. Lastly, paragraph 68 of the judgment states that that sufficient political and fiscal independence of central government presupposes that the local authority has powers to adopt measures reducing the tax rate,

38 — My emphasis.

regardless of any considerations related to the conduct of the central State.

— Procedural organisational autonomy

85. Procedural organisational autonomy exists where the central State is not able to intervene directly in the procedure leading to the adoption of the tax rules, for example by approving the rules, lodging a veto against the adoption of the rules, or assuming competence for their adoption.

83. In view of these formulations, the parties disagree on the extent to which autonomy is called into question by the fact that the Historical Territories are bound in adopting their tax legislation by certain legal provisions. Compliance with those provisions is subject to judicial review, at last instance by the Tribunal Supremo, a central State court. Certain parties also see this as a restriction of the autonomy enjoyed by the Historical Territories.

86. On the other hand, procedural organisational autonomy is not affected where the central State and the local authority inform and consult one another about legislative plans, as the United Kingdom rightly argues. This is true at least where the local authority remains free to adhere to its plans, even in the case of an unfavourable opinion from the central government.

84. The constitutional provisions, including the provisions in the Statute of Autonomy and in the Economic Agreement, restrict the substantive discretion of the Historical Territories. I will therefore examine this aspect in connection with substantive organisational autonomy. In that context, I would also like to consider the ex post review of the tax rules by the courts. Because it does not have a direct effect on decision-making during the legislative procedure, it does not affect organisational autonomy in the formal sense, but safeguards the limits of substantive organisational autonomy.

87. Without wishing to prejudge the final assessment by the referring court, the central government does not appear to have any final right of decision under the provisions of the Constitution, the Statute of Autonomy or the Economic Agreement. Article 4 of the Economic Agreement does provide for coordination and cooperation between the tax authorities, which is given an institutional framework by the Coordination and Evaluation Committee under Articles 63 and 64 of the Economic Agreement. Nevertheless, the coordination and cooperation does not appear to bind the Historical Territories to the provisions of the central State against their will.

— Substantive organisational autonomy

88. Substantive organisational autonomy means that the local legislator is able to decide freely on the structure of the tax rules. However, the legislator does not have full freedom in any democratic, constitutional order. Rather, the legislator is always bound by constitutional provisions, in particular by observance of fundamental and human rights. Community law also imposes limits on national legislation.

89. Consequently, the fact that the Historical Territories must observe constitutional limits in adopting tax legislation does not automatically preclude substantive organisational autonomy. However, those provisions may not restrict the freedom to act to such an extent that in practice the Territories can no longer pursue their own finance policy aims in adopting tax legislation.

90. In this connection, mention should be made, first of all, of Article 2 of the Constitution, which guarantees the right to autonomy of the Spanish nationalities and regions, but at the same time requires solidarity among them. The principle of solidarity is also enshrined in Articles 138 and 156 of the Constitution. Is the autonomy so extensive that the regions can enter into fiscal competition with one another or is that contrary to the principle of solidarity? This question lies at the heart of the entire dispute, and must be answered not by the Court of Justice, but by the national courts.

91. Article 31 of the Constitution provides for taxation according to economic capacity through a fair tax system based on the principles of equality and progressive taxation. If it is inferred that there may be only one tax system in Spain to which all taxable persons contribute according to their economic capacity, then the local legislator could not introduce lower tax rates. This means that the level of the tax burden does not depend solely on the economic capacity of the taxable persons, but also on their domicile. However, it is also possible that Article 31 does not preclude the existence of more than one tax system in Spain, *within which* each of the abovementioned principles must be implemented.

92. As regards the Constitution, mention should also be made of Article 139, which requires the equal treatment of all citizens and prohibits measures which directly or indirectly hinder freedom of movement and of establishment of persons. Article 3(c) of the Economic Agreement also adds that the tax rules of the Territories may not give rise to discrimination or restrict commercial competition.

93. Different tax rates or differences in tax deductibility may influence taxable persons in deciding on their location. In its case-law

on the fundamental freedoms, however, the Court has stated that the EC Treaty offers no guarantee to a taxable person that transferring his activities to another Member State will be neutral as regards taxation. [39] Given the disparities in the legislation of the Member States in this area, such a transfer may be to the worker's advantage in terms of taxation or not, according to circumstance. This statement is based on the fact that there is no Community-wide uniform system of taxation. [40] The question whether this finding can be applied to the circumstances within Spain therefore also depends on the extent to which the tax regime of the Historical Territories can be regarded as a system independent of the central State system.

94. Further commitments follow from Article 41(2)(a) of the Statute of Autonomy, which requires the Territories to have regard to the general tax structure of the State, and the rules contained in the Economic Agreement governing coordination, fiscal harmonisation and cooperation with the State.

95. Article 2(2) and Article 3(a) of the Economic Agreement clarify that the Territories must have regard to the general taxation structure of the State and respect the Ley General Tributaria in matters of terminology and concepts. However, observance of uniform taxation structures and concepts does not necessarily preclude pursuit of the Territories' own finance policy aims. The crucial factor is whether material parameters such as the tax rate and the basis for assessment may be fixed in derogation from central law.

96. A further restriction lies in the requirement to maintain for taxable persons an overall effective fiscal pressure equivalent to that in force in the rest of the State (Article 3(b) of the Economic Agreement). However, that provision allows the Historical Territories the possibility of shifting the balance between income taxation of natural persons or others, on the one hand, and corporation tax, on the other, without any change in the average per capita tax burden. It would also be conceivable for the reduction in the corporation tax rate to be compensated by an extension of the basis for assessment.

97. In summary, I consider that it is for the referring court to establish whether the Historical Territories have their own organisational discretion in adopting tax legislation in accordance with the provisions of the Constitution, the Statute of Autonomy and the Economic Agreement, which allows them to pursue their own finance policy aims. That would be the case if they could define relevant parameters such as the tax rate or the basis for assessment in marked derogation from the central tax legislation.

39 — Case C-387/01 *Weigel* [2004] ECR I-4981, paragraph 55.

40 — See point 45 above, situation 2.

98. Certain parties argue that it is clear from the case-law of the Spanish higher courts that no such discretion exists. I am not able to give a definitive assessment of this, but would like briefly to examine the two judgments which are primarily cited in this connection.

99. In so far as reference is made in this connection to Judgment 96/2002 of the Tribunal Constitucional (Constitutional Court) of 25 April 2002, [41] it should be noted that that decision did not directly concern the legislative competences of the Historical Territories. Instead, it related to rules of the central State which introduced advantages similar to the provincial tax rules. Advantages were accorded to undertakings which, because of their domicile in another Member State, were subject to the fiscal sovereignty of the central State and could not therefore benefit from tax advantages under the Normas Forales for setting up a permanent establishment in the Historical Territories. Under the contested rules of the central State, they were reimbursed tax in so far as it exceeded the amount which would have been payable pursuant to provincial tax law.

100. The Constitutional Court held that this difference in treatment of two categories of undertaking — undertakings established in another Member State and undertakings established in Spain, but outside the Basque Country — which are in the same position as regards setting up a permanent establishment in the Basque Country, was incompatible with the Constitution. [42] However, this difference in treatment occurred within the same legal order. On the other hand, it clearly did not compare the situation of economic operators established in the Territories and subject to provincial tax law with the situation of undertakings established in the rest of the State, which are subject to general tax rules.

101. Nor does the judgment of the Tribunal Supremo of 9 December 2004 [43] give a final answer to the question whether the national provisions allow the Historical Territories sufficient substantive organisational autonomy. Apparently, the court considered the limit of their discretion to be where the provincial tax rules crossed the threshold into State aid. It was obviously unable to take into consideration the Court of Justice's *Azores* judgment, which was delivered at a later date.

102. In the light of the principles developed in that judgment, there are two possible interpretations of the decision by the Tribunal Supremo. Either it assumed implicitly that in the absence of sufficient autonomy on the part of the Historical Territories the State tax system alone could be used as the reference

41 — Annex 7 to the Commission's written statement.

42 — Ultimately, it thus found discrimination against nationals to be unlawful.

43 — See point 25 above.

framework for assessing the selectivity of the provincial tax rules or it wished to make the extent of the autonomy dependent on the Community law concept of aid.

103. Taking into account the *Azores* judgment, however, the latter approach would lead to a circular argument. The Court conversely links the existence of aid to the lack of autonomy on the part of the local tax legislator under national law. In order to avoid such a circular argument, ascertaining the powers of the local tax legislator is to be regarded as a precondition for the application of the concept of aid under Article 87(1) EC. The Court of Justice cannot take from the national courts the necessary task of interpreting national law.

104. Lastly, it is necessary to consider the argument that the Historical Territories lack sufficient autonomy because their rules are subject to judicial review, at last instance by a central State court.

105. If the national rules place limits on the discretion enjoyed by the local tax legislator, it is not unusual in a State based on the rule of law for the observance of those limits to be subject to judicial review. Provided the examination extends only to that and not to the expediency of the local tax laws, the judicial review does not constitute an additional restriction of the autonomy of the local or regional authority. This is not affected by the fact that at last instance a court at the level of the central State is competent. It is also irrelevant that legal recourse to ordinary courts is possible in order to challenge the local rules as secondary regulations, whilst regional and central laws can be challenged only before the Constitutional Court.

(e) Financial autonomy

106. A local authority possesses financial autonomy if it must itself bear the financial consequences of its tax rules and it does not receive any compensation from the central State for shortfalls in tax revenue stemming from derogations from the central rules by local rules.

107. The application of that criterion raises considerable practical difficulties if the reduction of the tax rate or the grant of other advantages does not — as in the case of the *Azores* — represent an element of a kind of indirect regional assistance by the central State. There is then no internal logic between the tax reduction and compensatory financial transfers between the central State and the local or regional authority. Rather, in cases like the main proceedings, there is a need for

a comprehensive assessment of the financial relations between the central State and its subdivisions.

108. That examination is made even more difficult by the fact that in addition to the general budget of the State, the regions and other local or regional authorities overlapping special State funds exist, in particular social security schemes, where there may be further financial transfers between different geographical areas and State levels.

109. Financial autonomy on the part of the infra-State structure is not always to be rejected where following this general examination there is, on balance, a financial transfer from the central State to the local or regional authority. Such a financial transfer can take place for a variety of reasons which have no connection with the local or regional tax rules.

110. In order to establish a connection between such financial transfers and the local tax legislation, at least two requirements must therefore be satisfied. First of all, the level of the local tax revenue must be included as a parameter in determining any financial transfer. Secondly, a reduction in tax revenue must also lead to a corresponding compensatory adjustment in the transfer of funds between the State levels.

111. For the further examination, it must be assumed that the lower tax rate and the special deductions provided for by the provincial tax rules in derogation from the central State provisions result in shortfalls in tax revenue at least in a certain assessment period. The claim made by the Historical Territories that their tax policy actually increases tax revenue in the longer term because more undertakings become established there must be disregarded. If such a defence were accepted in examining aid, the prohibition on aid would be practically redundant. State aid is often granted with the aim of promoting positive economic development among the favoured undertakings, with the result that the 'investment' is ultimately profitable for the State by creating jobs, easing the burden on social security schemes and returning tax revenue. [44]

112. The main instrument in financial relations between the central State and the Autonomous Community of the Basque Country, and indirectly also the Historical

44 — In this connection, the Commission argues in particular that the relevant factor under the case-law is the effect of aid on an individual undertaking and not the aims pursued (see Case C-56/93 *Belgium* v *Commission* [1996] ECR I-723, paragraph 79; Case C-241/94 *France* v *Commission* [1996] ECR I-4551, paragraph 20; and Case C-75/97 *Belgium* v *Commission* [1999] ECR I-3671, paragraph 25).

Territories, to which the national court and the parties in the proceedings before the Court of Justice refer, is the quota (*cupo*).

113. The quota system has its basis in Article 42(2)(d) to (f) of the Statute of Autonomy, Article 48 et seq. of the Economic Agreement and the Law on the quota in the five-year period 2002 to 2006. Ultimately, the majority of the tax revenue is transferred by the Historical Territories to the Autonomous Community of the Basque Country and the central State. That transfer is necessary because a large part of the tax revenue goes to the Historical Territories, whilst the majority of the State contributions are made by the central State and the Autonomous Community.

114. In very simple terms, the level of the overall quota of the Basque Country, made up of the individual quotas of each of its Historical Territories and paid to the State budget, is determined in the following steps. The expenditure for the functions of the State which the regions do not themselves perform is calculated, it being assumed notionally that all Spanish regions perform functions to the same extent as the Basque Country. A coefficient is then applied, which is intended to correspond to the share of the revenue of the Historical Territories compared with the State as a whole. Since 1981 that coefficient has remained unchanged at 6.24%. Various adjustments and corrections not directly connected with the level of the tax revenue are then made. This produces a sum which the Basque Country must pay to the State. In the base year 2002, it amounted to around EUR 1 000 million and may be subject to further adjustments in subsequent years.

115. It is difficult to assess the extent to which the tax revenue of the Historical Territories and changes thereto on the basis of the contested rules influence the level of the financial transfer from them or from the Autonomous Community of the Basque Country to the State. On the whole, the explanations given by the parties in their written statements and in response to a question asked by the Court at the hearing give the impression that the definition of the quota represents something of a political compromise and is not a direct consequence of the change to certain economic parameters, including the level of the tax revenue. This is clearly shown by the fact that the attribution coefficient, which is actually intended to create a link to the proportionate amount of tax revenue of the Historical Territories, has not been changed for more than 25 years, even though tax revenue has certainly been subject to fluctuations.

116. In any case, the Spanish Government takes the view that changes to the tax revenue of the Historical Territories do not influence the amount of the quota. If the referring court were to come to the same conclusion and no other compensatory mechanisms were to intervene, there would be sufficient financial autonomy on the part of the Historical Territories.

V — Conclusion

117. The question referred by the Tribunal Superior de Justicia del País Vasco must therefore be answered as follows:

Article 87(1) EC must be construed as meaning that the tax rules adopted by a local authority in a Member State, which apply in the same way to all undertakings subject to its fiscal sovereignty and which are more favourable than the general tax rules of that Member State, do not constitute an advantage for certain undertakings and the production of certain goods where the local authority has sufficient autonomy in the exercise of its legislative powers in the field of tax law. Such autonomy requires that:

— the local authority has institutional independence,

— the central State cannot have decisive influence in the procedure leading to the adoption of the local tax rules (procedural organisational autonomy),

— the local authority has sufficiently wide discretion in organising its tax rules, which allow it to pursue independent finance policy aims (substantive organisational autonomy) and

— the local authority itself bears financial responsibility for shortfalls in tax revenue stemming from the rules which are more favourable than the general tax legislation (financial autonomy).