European Union, Spain

State Aid and Autonomous Regions: The ECJ's Ruling in the *Basque Country* Case

The 2006 judgement of the European Court of Justice in the *Azores* case regarding the European Commission's interpretation of the "selective criterion" of the State aid rules of the EC Treaty opened the door for the ECJ's judgement in the *Basque Country* case in 2008. This article examines these two decisions of the ECJ. Before doing so, the article describes the financial regime of the Basque Country, which forms the background of the *Basque Country* judgement.

1. The Problem: The "Selective" Criterion of State Aid

According to the analysis of the European Commission in the "Notice on the application of the State aid rules to measures relating to direct business taxation"[1] (the Notice), a tax measure constitutes a fiscal aid under Art. 87(1) of the EC Treaty under the following four conditions:

- the measure confers on recipients an advantage which relieves them of charges that are normally borne from their budgets;
- the advantage is granted by the State or from State resources;
- the measure affects competition and trade between the Member States; and
- the measure is specific or selective in that it favours "certain undertakings or the production of certain goods".

The "selective" criterion is the one that raises the most difficult problems, including the one that is the subject of this article. A tax measure is selective or specific if it constitutes an exception to the general system. As examples of selective measures, the Notice mentioned those whose main effect is to promote one or more sectors of activity, on the one hand, and those that are restricted to certain functions of the enterprise, such as intragroup services, intermediation or coordination, on the other. Commentators have referred to these types of measures as "sectoral" and "horizontal" measures.[2] The third type of selective tax measures consists of those that are limited to a certain territory or region within a State ("regional" measures). This kind of measure poses the problem with which this article is concerned.

The Notice adopted a very rigid position concerning regional selectivity: "The Commission's decision-making practice so far shows that only measures whose scope extends to the entire territory of the State escape the specificity criterion laid down in Article 92(1) [now Art. 87(1)]". The Notice made an argument frequently put forward by the Commission before the European Court of Justice (ECJ): "The Treaty itself qualifies as aid measures which are intended to promote the economic development of a region. Article 92(3)(a) and (c) [now Art. 87(3)(a) and (c)] explicitly provides, in the case of this type of aid, for possible derogations from the general principle of incompatibility laid down in Article 92(1)."

It may be mentioned that the Notice reflected the European Union's new policy regarding harmful tax competition as a consequence of the adoption by the EU Council on 1 December 1997 of the proposals contained in the Commission communication to the Council entitled *Towards tax coordination in the European Union: A package to tackle harmful tax competition*,[3] the so-called "Monti package". Included in this package was the "Code of conduct for business taxation". The Code (Para. J) announced the publication of the Notice and mentioned that "[t]he Council notes that some of the tax measures covered by this code may fall within the scope of the provisions on State aid in Articles 92 to 94 of the Treaty [now Arts. 87 to 89]". The Council also noted that the Commission "commits itself to the strict application of the aid rules" and "intends to examine or re-examine existing tax arrangements and proposed new legislation by Member States case by case ...".

Thus, a connection was established between harmful tax competition and State aid.[4] This new stance led to the abandonment of the Commission's previous relatively tolerant attitude toward fiscal State aid, particularly regarding direct taxation, for which the Member States have exclusive competence, a change that Pinto called "dramatic". It has been pointed out, on the one hand, that this use of the State aid rules has the effect of converting soft law (the Code of conduct) into hard law, thus widening the power of the Commission.[5] On the other, it has also been pointed out that this use of the State aid rules is a means of carrying out harmonization in the field of direct taxation without being subject to the limitations

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1. 98/C 384/03, *Official Journal*, No. C 384, 10 December 1998.
2. See Martín Jiménez, A.J., "El concepto de ayuda de Estado y las normas tributarias: problemas de delimitación del ámbito de aplicación del art. 87.1 TCE", *Noticias de la Unión Europea*, No. 196 (2001), at 89; and Pinto, C., *Tax Competition and EU Law* (Kluwer Law International, 2003), at 140 et seq.
3. COM(97) 495.
4. Pinto, supra note 2, at 190. See also Palao Taboada, C., "Ayudas de Estado y Competencia Fiscal Dañina", *Forum Fiscal de Bizkaia*, No. 138 (2008), at 21.
5. Martín Jiménez, supra note 2, at 102.

imposed by the EC Treaty.[6] Some of the Commission's decisions against the tax measures of the Basque institutions were made in the context of this new policy.

The Commission's interpretation of the regional specificity criterion stated in the Notice would obviously make it impossible for any sub-central authority of an EU Member State to adopt tax measures within its territory that are more favourable than those applicable in the remaining State territory without falling afoul of the State aid provisions of the EC Treaty. This would, of course, severely restrict the fiscal autonomy of the regional authority. Here lies the core of our subject.

A crucial change in the interpretation of the "selective" criterion was brought about by the ECJ in its judgement of 6 September 2006 in *Portuguese Republic v. Commission of the European Communities*, C-88/03 (the *Azores* case). This ruling opened the door for the ECJ's judgement of 11 September 2008 in Joined Cases C-428/06 to C-434/06, referred to as the *Basque Country* judgement, which constitutes the basic reference point of this article. The article examines these two decisions (see 3. and 4.), but first it is necessary to describe concisely the financial regime of the Basque Country, which forms the background of the *Basque Country* judgement.

2. The Financial Regime of the Basque Country

2.1. Description of the regime

The Basque Country and Navarre have special financial regimes separate from the general tax system and from the financial systems of the remaining 15 Autonomous Communities or regions. The Canary Islands present some specialties, especially concerning indirect taxation (they are not included in the European VAT territory, in the first place), but they do not constitute a separate regime like those of the Basque Country and Navarre.

The regimes of the Basque Country and Navarre have a common origin in the 19th century, when these two territories were integrated into the general constitutional order of Spain, but retained certain "historical rights", a fundamental part of which is their special financial regime. Therefore, their basic principles are similar: both regions establish and collect their own taxes and pay a sum to the State in compensation for the services rendered by the State in their territory. According to the First Additional Provision of Spain's Constitution of 1978, "[t]he Constitution protects and respects the historic rights of the territories with traditional charts (*fueros*)."[7]

These "historical rights" belong to the Basque provinces of Álava, Guipúzcoa and Biscay and to Navarre, which was also a province in the unitary State before the present Constitution. The establishment by the latter of a quasi-federal State, by the creation of the Autonomous Communities, introduced some relevant differences between the two territories: while the old province of Navarre became an Autonomous Community on its own, the three Basque provinces were joined in the Autonomous Community of the Basque Country. Hence, Navarre has a simple internal structure: the political and administrative organs of the previous province were transformed into those of the regional government. In contrast, in the Basque Country, the organs of the new Autonomous Community coexist with those of the old provinces, which are called "Historic Territories" in the terminology of the Basque constitutional order. This creates a complicated pattern of institutional relationships between the region or Autonomous Community and the provinces or Historic Territories. These relationships are basically governed, first, by the Statute of Autonomy of the Basque Country, approved by Organic Law 3/1979 of December 18 of the *Cortes Generales* (Spanish Parliament), and second, by Law 27/1983 of November 25 of the Basque Parliament "on the relationships between the common Institutions of the Autonomous Community and the chartered organs of their Historic Territories", shortened to "Historic Territories Law".[8]

The organization of the Historic Territories, which on the grounds of the cited norms is set up autonomously, consists essentially of a deliberative organ called *Juntas Generales* (General Assembly) and a local government called *Diputación Foral* (Provincial Council). It is important for our purposes to indicate that the *Juntas Generales* produce legal norms called *normas forales*,[9] whose nature is a matter of dispute. Formally, they are administrative regulations and may therefore be challenged in the ordinary administrative courts, specifically in the Administrative Chamber of the High Court of the Basque Country. In substance, however, the specialties of the Basque constitutional order provide some grounds for assimilating them in many aspects to parliamentary laws.[10] One of these aspects is that the *normas forales* are the kind of laws by which the Historic Territories establish taxes within the framework of the Basque fiscal system, an action that requires a provision with the rank of parliamentary law.

This system, called by the Basque Statute (Art. 41.1) "sistema foral tradicional de Concierto Económico o Convenios" (traditional "*foral*" system of Economic Agreement or Covenant), has two sides, an external one and an internal one. The external side concerns the relationship between the Basque Country and the central State, and the internal one concerns the relationship between the

6. Fantozzi, A., "The Applicability of State Aid Rules to Tax Competition Measures: A Process of 'De Facto' Harmonization in the Tax Field?", in Schön, W. (ed.), *Tax competition in Europe* (Amsterdam: European Association of Tax Law Professors/IBFD, 2003), at 131.

7. English translation posted on the web site of Congress (Parliament's law chamber). The Castilian noun "*fuero*", which the translator felt necessary to indicate in quotation marks, has a medieval origin and indicates, among other things, the charters of rights granted by the kings to cities or territories. Derived from *fuero* is the adjective "*foral*", habitually used in connection with the institutions and organs of the "Historic Territories".

8. The constitutionality of Law 27/1983 was challenged in the Constitutional Court, which rejected the claim in its judgement 76/1988 of April 26.

9. See note 7, supra.

10. See Jiménez Asensio, R., "El sistema de fuentes del Derecho de la Comunidad Autónoma del País Vasco como 'ordenamiento asimétrico'", 47(II) *Revista Vasca de Administración Pública* 127 (1997).

Autonomous Community of the Basque Country and the Historic Territories.[11]

The external side is governed by the Economic Agreement, which is agreed upon by a commission of representatives of the State and the Basque Country and is formally enacted by a law of the Spanish Parliament. The Economic Agreement presently in force was approved by Law 12/2002 of May 23, as amended. The main features of the system are the following:

First, the Historic Territories collect almost all the taxes in their territory (an important exception is customs duties).

Second, some of these taxes (in the first place, the income tax and the corporate tax) are governed by laws (*normas forales*) passed by the General Assemblies of the Historic Territories. The other taxes, basically indirect taxes (VAT and excise taxes), are governed by State law.

Third, the Agreement establishes the criteria (connecting factors in the terminology commonly used in private international law) for assigning the power to collect taxes and apply the corresponding rules to the State or the respective Historic Territory.

Fourth, the Agreement also establishes certain principles and rules in order to harmonize the Basque tax system with the State system.

Finally, the Basque Country contributes an amount called the "*cupo*" (quota) to the expenses of the State for the services which have not been assumed by the Basque government. The total quota consists of the contributions or quotas from the Historic Territories. Based on the principles established by the Agreement, the method for computing the quota is agreed upon for a five-year period by the same commission that approves the Economic Agreement. It also determines the amount for the first year and updates it in the subsequent years. The agreed methodology and the amount for the first year are then enacted by State law.[12]

Regarding the internal side of the system (relationships between the regional authorities and the Historic Territories), the Autonomous Community of the Basque Country has very limited taxing powers, and its principal source of finance is the contributions from the three Territories. According to the Basque Historic Territories Law, the total taxes collected by the three Territories is distributed between them and the regional Treasury by the Basque Public Finances Council, formed by one representative of each Historic Territory and three of the Basque government. The method of distribution is also determined by the Council for a five-year period and is enacted into law by the Basque Parliament. Thus, the internal side of the system closely resembles the external side. As De la Hucha put it,[13] the Historic Territories Law acts as an Economic Agreement between the Territories and the Autonomous Community.

On the other hand, Art. 14(3) of the Historic Territories Law provides that the rules passed by the Territories based on the power granted by the Economic Agreement "shall regulate in a uniform way the basic elements of the taxes", and it authorizes the Basque Parliament to enact norms for the harmonization, coordination and collaboration between the Historic Territories. On the basis of this authorization, the Basque Parliament passed Law 3/1989 of May 30, which, among other things, enumerates certain elements of the taxes for which the Territories have normative competence that must be harmonized, dictates some rules simplifying the compliance obligations of taxpayers and coordinating the activities of the provincial tax administrations, and sets up a Tax Coordination Organ. This Organ is formed by an equal number of representatives of the regional government and the Territories and, besides its other functions, it has to report on the draft legislation of the latter.[14]

Some additional information about the contribution of the Basque Country to the State (*cupo* or quota) is necessary in order to understand its role in assessing the economic autonomy of the region and the debate on this issue before the ECJ.[15] The quota is compensation for the State's expenditures for the services in the Basque Country not provided by the local institutions less the taxes paid to the State (not to the local authorities) by Basque residents. These amounts are determined indirectly as a percentage of the total State expenses for those services and the total amount of those taxes. This ratio is the relation of the income of the Basque Country to national income. It was set in the first post-constitutional Economic Agreement of 1981 at 6.24% and has remained unaltered ever since.[16]

Other major elements are also taken into account in computing the quota:

11. For a detailed and profound analysis of the Basque financial system, see De la Hucha Celador, F., *El regimen jurídico del Concierto Económico* (Bilbao: Ad Concordiam, 2006). The same author explained the system of Navarre in *El régimen jurídico del Convenio Económico de la Comunidad de Navarra* (San Sebastián: Fundación para el Estudio del Derecho Histórico y Autonómico de Vasconia, 2006). For a more summary description of the Basque system, see Sáinz Moreno, F., "El Régimen Foral Vasco y la articulación de sus competencias financieras", in *The Journal of Basque Studies* (Fresno, California: Basque American Foundation, 1992), at 17.

12. Law 29/2007 of October 25 approved the method for computing the quota for the period 2007-2011.

13. In *El régimen jurídico del Concierto Económico*, supra note 11, at 80.

14. See De la Hucha Celador, *El régimen jurídico del Concierto Económico*, supra note 11, at 82 et seq. (rather critical of the restrictions imposed by Law 3/1989 on the taxing powers of the Historic Territories).

15. For a clear explanation in English of the quota, see Armesto, D., "The ECJ's Judgment regarding the Tax Autonomy of the Basque Country", *European Taxation* 1 (2009), at 11, 16 et seq.

16. According to Zubiri, I., *El sistema de Concierto Económico en el contexto de la Unión Europea* (Bilbao: Circulo de Empresarios Vascos, 2000), at 38, this percentage was an intermediate amount between the participation of the income of the Basque Country in Spain's total and its relative population. In Zubiri's opinion, the contribution was thus midway between progressivity (contribution in proportion to income) and neutrality (contribution in proportion to population). He pointed out that the relative income of the Basque Country in relation to national income has diminished so that the 6.24% is higher than the Basque relative income. See also Zubiri, I., "Los sistemas forales: características, resultados y su posible generalización", in Lago Peñas, S. (ed.), *La financiación del Estado de las Autonomías: perspectivas de futuro* (Madrid: Instituto de Estudios Fiscales, 2007), at 355, 374 et seq. The same point is made in Armesto, supra note 15, at 17.

- a deduction of part of the national budget deficit measured by applying the same 6.24%;[17]
- an adjustment for VAT, based on the consideration that part of the VAT collected by the State administration is borne by Basque consumers;[18] and
- an adjustment for excise taxes for the same reason.[19]

This brief description clearly shows that the amount of the quota is independent of the tax revenue collected by the Basque administration. If this were not the case, i.e. if the quota were determined by the amount of tax collected by the Basque authorities so that less revenue would entail a smaller quota, it would be equivalent to a compensation by the State of the consequence of the tax advantages granted by the Basque authorities to enterprises.[20]

2.2. Litigation on the tax measures of the Basque Country

Until now, the special tax regime of the Basque Country – this expression is used here in a general sense and includes the Historic Territories – has not had an easy life. The measures adopted in its framework have frequently been challenged by the State and, especially later, by the European Commission.

The State's challenges were based mostly on infringement of the Economic Agreement.[21] The State challenged certain *normas forales* of 1993 in the High Court of the Basque Country on the basis, among others, of violation of the State aid rules of the EC Treaty. The High Court decided to refer the case to the ECJ for a preliminary ruling, but the Spanish government withdrew the case before the ECJ issued a judgement because of the "fiscal peace" agreed to with the Basque authorities immediately before the 2000 general elections.[22] However, Advocate-General Saggio of the ECJ had already presented his opinion,[23] in which, concerning the specificity criterion of State aid, he maintained the same rigid position expressed earlier by the Commission in the "Notice on the application of State aid rules to measures relating to direct business taxation".[24] He considered the measures "selective in nature" because they were intended for companies situated in a particular region of the Member State in question. The defendants in the main proceedings (basically the *Juntas Generales* of the Historic Territories) and the Spanish government claimed a distinction between fiscal measures adopted by the State, whose scope is limited to a fixed area of its territory, and general measures adopted by a competent authority within the territory. The defendants argued that the rules on the allocation of competence for tax matters to the authorities of the Historic Territories were no different from the rules governing the allocation of competence between the sovereign tax authorities of two Member States. This argument anticipated the idea that lies at the heart of the *Azores* doctrine.

The Advocate-General rejected this reasoning. In his opinion, the fact that the measures at issue were adopted by regional authorities with exclusive competence under national law was merely a matter of form, which was not sufficient to justify the preferential treatment granted to companies falling within the scope of the provincial laws. If this were not the case, he argued, the State could easily avoid the application, in parts of its own territory, of the State aid rules of Community law simply by making changes to the internal allocation of competence for certain matters, thus raising the "general" nature, for that territory, of the measure in question. The Advocate-General also invoked the ECJ's case law according to which the words "in any form whatsoever" in Art. 92 (now Art. 87) mean that it is necessary to assess the effects of the aid, rather than the nature of the authority granting the aid or its powers, in light of the domestic rules.

The European Commission has repeatedly characterized the fiscal incentives granted by the Basque Country as State aid,[25] beginning in 1993 with regard to *normas forales* of 1988.[26] Subsequent measures in

17. The main rationale of this deduction is to allow the Basque Country to participate in the deferral of financing expenses through taxation; see Zubiri, *El sistema de Concierto* ..., id. at 37 (footnote 51); and Armesto, supra note 15, at 18.

18. This is the case in the first place with the VAT collected on imports by the customs services, computed as 6.875% of the total, an index of the relative consumption in the Basque Country. Added to this is 1.110% of the remaining estimated VAT revenue in the "common territory" (Spain less the Basque Country and Navarre). This 1.110% ratio is the difference between (a) the Basque consumption index and the percentage of the aggregate VAT base of the Basque Country and (b) the national total, estimated at 5.765%. These ratios were established by Law 29/2007 of October 25 which approved the method of computing the quota for the period 2007-2011. The effect of this adjustment is to convert the VAT at origin into a VAT at destination.

19. The ratios vary for the excises on alcohol, beer and hydrocarbons.

20. In the words of Armesto (supra note 15, at 16): "the Basque quota is not the State's share in the tax revenues collected in the Basque Country, but, rather, a contribution by the Basque Country to State expenditure. The proportion in which the Basque Country shares in such expenditure is not linked in any way to the level of taxes collected there, but is based on the relative weight of the Basque Country's economy in the Spanish economy as a whole. Neither is the contribution linked to the benefit that the Basque Country receives from State expenditure. In other words, the quota is not the "price" paid for the services received from the State, but is, rather, a contribution to the State expenditure, regardless of whether the expenditure benefits the Basque Country more or less than other territories."

21. On appeals against the rulings of the High Court of the Basque Country, see the judgements of the Supreme Court of 23 December 1996 (RJ 1996, 9590), 7 February 1998 (RJ 1998, 1111), 13 October 1998 (RJ 1998, 7912), 22 October 1998 (RJ 1998, 7929) and 20 November 1999 (RJ 1999, 9602). In all these appeals, the Supreme Court held in favour of the appellant State.

22. See the editorial article in the daily newspaper *El País* of 19 January 2000. The article mentioned that the armistice, as the article called it, entailed the withdrawal of nearly one hundred claims. It was in the context of this new political climate that the Economic Agreement of 2002 was negotiated and concluded.

23. Issued on 1 July 1999 in Joined Cases C-400/97, C-401/97 and C-402/97, *Administración del Estado v. Juntas Generales de Guipúzcoa and Others*.

24. See Para. 36 et seq. of the Advocate-General's opinion.

25. A fairly detailed account of the Commission's decisions characterizing the Basque measures as State aid and the ensuing judgements of the ECJ can be found in Moreno Fernández, J.I., "La autonomía de las regiones y el Derecho comunitario: los beneficios fiscales autonómicos como potenciales 'ayudas de Estado' contrarias al Mercado Común", in *Estudios en homenaje al profesor Pérez de Ayala* (Madrid: CEU/Dykinson, 2007), at 203, 218 et seq.

26. It is interesting to note that the Spanish State reacted to the Commission's decision with a legal provision granting non-residents a refund of the excess over the amounts they would have paid if they could have availed themselves of the Basque norms (8th Additional Provision of Law 42/1994 of December 30). In its judgement 96/2002 of April 25, the Constitutional Court ruled that such a provision infringed the constitutional principle of equality because it did not grant the same compensation to Spanish residents in the same situation.

1993[27] motivated new decisions of the Commission in 2001, in the wake of the new policy on the application of the rules mentioned above, declaring the measures to be State aid incompatible with the common market. Actions for the annulment of these decisions were brought before the Court of First Instance. The process repeated itself with new *normas forales* in subsequent years,[28] and some of the measures adopted by the Historic Territories were annulled by the Spanish courts.[29]

The last episode in this long struggle began with the adoption by the three Historic Territories in 2005 of provisions replacing those that had been annulled by the Supreme Court judgement of 9 December 2004. The new provisions, which simply reproduced those annulled,[30] were then challenged in the High Court of the Basque Country, which referred the case to the ECJ for a preliminary ruling. The judgement issued in this preliminary ruling constitutes the central subject of this article. Before commenting on that judgement, it is necessary to examine the preceding judgements in the *Azores* and *Gibraltar* cases.

3. The *Azores* Doctrine

3.1. The *Azores* case

The *Azores* judgement marks a decisive turn in the ECJ's case law on the territorial specificity criterion. The change was actually anticipated in Advocate-General Geelhoed's opinion in this case, delivered on 20 October 2005, in which (Para. 2) he identified the question at issue from the very beginning: "In what circumstances do variations in the national rate adopted solely for a designated geographical area of a Member State fall under the definition of State aid?" The controversial measure was a reduction in the income tax rates of initially 15% and later 20% and a reduction in the 30% corporate tax rate. The European Commission found that the measure constituted State aid on the ground of the (until then) settled doctrine on the specificity criterion. Portugal brought an action of annulment in the ECJ against the Commission.

In his opinion (Para. 48 et seq.), the Advocate-General answered the question by first distinguishing between three different scenarios:

(1) where the central government unilaterally decides that the national rate should be reduced in a defined geographical area, a measure that would be clearly selective;
(2) where all local authorities at a particular level have the autonomous power to set the tax rate for their geographical jurisdiction, a situation that is frequently called "symmetrical autonomy". The adoption of a lower rate by one authority would not be selective since there would be no national rate or general tax system against which to compare it; and
(3) where only one or more, but not all, local authorities of a given level have the power to establish for their territory a lower rate than the national rate ("asymmetrical autonomy").

In the last scenario, which is the relevant one when dealing with, as in the *Basque Country* case, special regional tax systems, the Advocate-General considered that "the crucial question is whether the lower tax rate results from a decision taken by a local authority that is truly autonomous from the central government of the Member State". He then explained that "truly autonomous" means "institutionally, procedurally and economically autonomous":

- institutional autonomy is a "constitutional, political and administrative status separate from that of the central government";
- procedural autonomy means that the local authority takes the decision "pursuant to a procedure where the central government does not have any power to intervene directly in the procedure of setting the tax

27. One of the measures was an exemption from the corporate tax for a period up to ten years, known as "fiscal holidays".

28. The *Daewoo* and *Ramondín* cases are noteworthy. The incentives granted by the Historic Territory of Álava determined that these companies (Daewoo and Ramondín Cápsulas, S.A.) established themselves in the latter's territory, Ramondín having moved from the neighbouring Autonomous Community of La Rioja. The actions for annulment of the Commission's decisions against the aids were dismissed by the Court of First Instance in two judgements of 6 March 2002: Joined Cases T-127/99, T-129/99 and T-148/99 (*Daewoo*) and Joined Cases T-92/00 and T-103/00 (*Ramondín*). The ECJ dismissed the appeals in two judgements of 11 November 2004, Joined Cases C-183/02 P and C-187/02 P (*Daewoo*) and Joined Cases C-186/02 P and C-188/02 P (*Ramondín*). However, the specific nature of the aid in these cases was not based on the territorial scope of the incentives.

29. Of special relevance is the Supreme Court judgement of 9 December 2004 (RJ 2005, 130), issued on an appeal against a judgement of the High Court of the Basque Country. The Supreme Court endorsed the Commission's restrictive territorial "selective" criterion and held many of the challenged measures to be State aid. On these grounds, the Court annulled them for the reason that the Commission had not been informed of them, thus violating Art. 88(3) of the EC Treaty. This ruling has been heavily criticized for the Court's interpretation of the concept of State aid and the Court's failure to refer the case to the ECJ for a preliminary ruling. See Falcón y Tella, R., "En torno a la STS 9 diciembre 2004 relativa a las normas forales de 1996 (I): los efectos de la declaración de nulidad y el papel del Tribunal Supremo en el control de las ayudas de Estado", *Quincena Fiscal*, 2/2005 at 5, and "(II): régimen de ayudas y libertad de establecimiento", *Quincena Fiscal*, 3-4/2005 at 5; Merino Jara, I., "Las ayudas de Estado y el Concierto Económico", *Jurisprudencia Tributaria Aranzadi*, 2004/III at 477 (electronic version reference BIB 2005, 566); Armesto Macías, D. and P.M. Herrera Molina, "¿Es ayuda de Estado un tipo de gravamen regional inferior al vigente en el resto del territorio? De la polémica doctrina del Tribunal Supremo a la fascinante opinión del Abogado General en el caso Azores y su relevancia para el País Vasco", *Quincena Fiscal*, 13/2006 at 33, 35; and Orena Domínguez, A., "Espaldarazo al Concierto Económico (Sentencia de 6 de septiembre de 2006 del Tribunal de Justicia de la Unión Europea, asunto C-88/03)", *Nueva fiscalidad*, 9/2006 at 106, 115 et seq.

Advocate-General Kokott's opinion in the *Basque Country* case (Para. 101) made a slight reference to this judgement saying in its favour that the Supreme Court was obviously unable to take into consideration the ECJ's judgement in *Azores*. As a matter of fact, the Supreme Court later modified its stance in view of the *Azores* doctrine. The High Court of the Basque Country had ordered a stay of the tax measures of the Historic Territories on the ground that they were presumably null in view of the Supreme Court's doctrine in its judgement of 9 December 2004 (applying the "*fumus boni iuris*" or "appearance of good right" doctrine). The Supreme Court revoked these orders, referring expressly to the change in the ECJ's case law represented by the *Azores* judgement: Supreme Court rulings of 12 July 2007 (RJ 2007, 4840) and 27 May 2008 (RJ 2008, 3494). The latter ruling also mentioned Advocate-General Kokott's opinion. See Burlada Echeveste, J.L. and I.M. Burlada Echeveste, "Ayudas de Estado y concierto económico: ¿el Tribunal Supremo rectifica su postura tras el asunto *Azores*?", *Quincena Fiscal*, 4/2008 at 9.

30. Hence, the request for a stay of the new provisions (mentioned in note 29, supra) accepted by the High Court of the Basque Country but revoked by the Supreme Court. Interestingly, in Merino Jara, supra note 29, at 495, the author suggested that the Historic Territories should enact provisions similar or even identical to those annulled, inform the Commission and see its position.

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"; and

- economic autonomy implies in sum that the lower tax rate is not financed by the central government so that the economic consequences of the reduction are borne by the region itself.

All three aspects of autonomy must be present; if one of them is absent, the lower tax rate would be selective for State aid purposes.

The fundamental lines of a new understanding of the specificity criterion were thus drawn. In its judgement of 6 September 2006, the ECJ fully endorsed the Advocate-General's construction and, after affirming that "the 'normal' rate is the rate in force in the geographical area constituting the reference framework", the ECJ set out the fundamental grounds of its new doctrine in Paras. 57 and 58:

> In that connection, the reference framework need not necessarily be defined within the limits of the Member State concerned, so that a measure conferring an advantage in only one part of the national territory is not selective on that ground alone for the purposes of Article 87(1) EC.
>
> It is 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, it is that body and not the central government which plays a fundamental role in the definition of the political and economic environment in which undertakings operate. In such a case it is the area in which the infra-State body responsible for the measure exercises its powers, and not the country as a whole, that constitutes the relevant context for the assessment of whether a measure adopted by such a body favours certain undertakings in comparison with others in a comparable legal and factual situation, having regard to the objective pursued by the measure or the legal system concerned.

The ECJ firmly rejected the Commission's argument derived from Arts. 87(3)(a) and (c) by affirming (in Para. 60) that "it cannot be inferred from that that a measure is selective, for the purposes of Article 87(1) EC, on the sole ground that it is applicable only in a limited geographical area of a Member State". In its judgement (Paras. 62 to 68), the ECJ fully endorsed Advocate-General Geelhoed's construction according to which the local authority's autonomy in the three aspects he distinguished is the relevant criterion as to which is the reference framework in order decide whether a measure is selective. In the specific case, the ECJ found that the Azores Region did not meet the required autonomy standard and ruled that the measure was selective; the ECJ therefore dismissed the action.

The *Azores* judgement made a crack in the seemingly insurmountable obstacle in the prevailing interpretation of the regional selectivity criterion. Thus, it is no wonder that the judgement was received with relief in Spain, especially in the Basque Country, where that interpretation of the State aid rules was, with reason, seen as a threat to its special regime, coming this time not from the central State but from the farther and even more powerful institutions of the European Union. It was generally thought that the Basque Country met the requirements of the *Azores* doctrine,[31] although certain commentators foresaw some of the problems posed by the application of the new doctrine to the particular situation of this region.[32]

3.2. The *Gibraltar* case

A new occasion for applying the *Azores* doctrine presented itself in the *Gibraltar* case, which originated with the Commission's decision declaring that a tax reform enacted by the Gibraltar authorities was both regionally and materially selective, and hence constituted State aid. The government of Gibraltar filed an application for annulment of the decision in the Court of First Instance, which rendered its judgement on 18 December 2008 in *Government of Gibraltar v. Commission of the European Communities*, Cases T-211/04 and T-215/04. The Commission raised a question before the application of the *Azores* autonomy requirements. The Commission contended (Paras. 69 ad 70):

> that the requirement, referred to in paragraph 66 of the judgment on the tax regime in the Azores, that the region "occupies a fundamental role in the definition of the political and economic environment in which the undertakings present on the territory within its competence operate" implies a fourth condition for the purposes of determining the appropriate reference framework, preliminary to and separate from the three tests listed in paragraph 67 of that judgment.
>
> This fourth condition requires the region in question to enjoy a degree of autonomy over the political and economic environment in which undertakings established in its territory operate that is comparable to the influence exercised by the central government of a Member State whose constitution does not provide for regional autonomy. The Commission explains that the rationale behind this requirement, in the light of the Treaty rules on State aid, is that in order to establish whether certain undertakings benefit from a given advantage it is necessary to compare their situation with that of other undertakings operating in the same political and economic environment.

31. See Orena Domínguez, supra note 29, at 106 et seq. Others were more cautious; see Merino Jara, I., "A vueltas con las ayudas de Estado de carácter fiscal", *Forum Fiscal de Bizkaia* (January 2008), at 23 (electronic version reference 085.002); and Calderón Carrero, J.M. and V. Ruiz Almendral, "Autonomía financiera de las Comunidades Autónomas vs. Derecho Comunitario", *Repertorio de Jurisprudencia Aranzadi*, 24/2006 (electronic version reference BIB 2006, 1718).

32. In Armesto Macías and Herrera Molina, supra note 29, at 33 et seq., the authors argued that it seemed incoherent that a small Member State like Cyprus, Estonia or Lithuania can adopt tax rates much lower than the Community average, but that a region with the required legislative competence cannot; the authors asked themselves whether it was a juridical incoherence, a product of the lack of fiscal harmonization, or a political incoherence that resulted in the different positions, with regard Community law, on the fiscal sovereignty of the Member States and the taxing power of sub-central governments. In the latter case, the incoherence could be resolved, in the authors' opinion, by weighing the degree of tax autonomy of the region; according to the authors (at 37), this was the solution proposed by Advocate-General Geelhoed. The authors pointed out (at 38) the "excessive complexity in practice" of the Advocate-General's proposal, and they foresaw with perspicacity some of the problems encountered by the ECJ in applying the *Azores* doctrine to the Basque Country. In Ruiz Almendral, V., "¿Vuelta a la casilla de salida? El concierto económico vasco a la luz del Ordenamiento comunitario", 28 *Revista española de Derecho europeo* 499 (2008), at 508, the author pointed out that, while the *Azores* doctrine is a deserving attempt to use the autonomy criterion to temper the Commission's interpretation of selectivity, the doctrine probably creates bigger problems than it solves, as shown by its application to the Basque Country situation.

It might be pointed out that this "fourth condition theory" is not totally contradictory to the autonomy concept of the *Azores* doctrine. In fact, the ECJ referred to the region's "fundamental role in the definition of the political and economic environment in which undertakings operate" as a sort of motivation of this concept. However, by establishing this additional condition, the Commission pushed the latter's rationale to the extreme so that, if this theory were accepted, hardly any region that was not fully independent would meet this standard. Thus, the fourth condition appears to be the Commission's old regional "selective" concept in new clothes. Therefore, the Court of First Instance rejected the contention (Para. 87): "There is no support for that argument in the judgment on the tax regime in the Azores or in the Opinion of Advocate-General Geelhoed in the same case (points 54 and 55)."

The Court of First Instance also rejected the Spanish government's argument that another fourth condition had to be added to the three conditions of autonomy required by the *Azores* doctrine (Para. 75):

> Under this fourth condition, the tax measure in question would not be selective if it were circumscribed by a number of harmonisation criteria which are similar to those that apply, by virtue of Community law, to tax measures adopted by the Member State to which the infra-State body belongs and which aim to protect the free movement of persons, capital, goods and services and to prevent distortion of the single market.

The Court concluded (Para. 88) that "[b]esides its vagueness so far as concerns identification of the harmonization criteria referred to and their content, this argument is not supported by the judgment on the tax regime in the Azores ...".

Having circumscribed the "selective" analysis to the three *Azores* conditions, the Court of First Instance held (Para. 115) that the Gibraltar authorities met all of them and consequently declared that the reference framework was the territory of Gibraltar.

As regards material selectivity, the Court found (Paras. 170 and 177) the Commission's reasoning to be flawed insofar as it failed to identify the "normal" regime, as would be necessary in the Court's opinion, in order to establish that certain elements of the system constituted derogations. Hence, the Court held (Para. 184) that the Commission did not sufficiently rebut the definition of the "normal" regime put forward by the Gibraltar authorities and did not establish the existence of selective advantages produced by the tax reform. The Court annulled the Commission's decision.

The *Gibraltar* ruling raises the following question: Can a tiny territory, like the territory of Gibraltar, of an authority that is not a Member State be considered an adequate geographical reference framework for a tax regime which, even if internally not selective, is designed to attract foreign companies? Arguably, the judgement of the Court of First Instance pushed the boundaries of the *Azores* doctrine a little too far.

4. The *Basque Country* Case

4.1. Reference for a preliminary ruling

As mentioned above, the three Historic Territories enacted tax provisions in 2005 which were similar to those that had been annulled by the Supreme Court. The adopted measures were in essence the following:

- a general corporate tax rate of 32.5%, which was lower than the 35% rate of the State corporate tax;
- a tax credit of 10% of the investment in new tangible fixed assets; and
- a tax credit of 10% of the accounting income assigned to a reserve for production investments and/or to a reserve for environmental conservation and improvement or energy savings.

The new provisions were challenged in the High Court of the Basque Country by the neighbouring regions of La Rioja and Castilla y León and by a trade union (*Unión General de Trabajadores* (UGT)) of La Rioja. The High Court considered it necessary to request a preliminary ruling from the ECJ in view of the *Azores* judgement, which so clearly departed from the previous stance of both the Commission and the ECJ and which, as mentioned above, the Supreme Court had applied. The questions referred to the ECJ by *autos* (orders) of the Basque Court on 20 September 2006 had the following identical text, save for the reference to the specific legislation of each Territory:[33]

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

The referring orders expressed the High Court's concerns in applying the *Azores* doctrine to the *Basque Country* case. These concerns lie beneath the formulation of the question posed to the ECJ and are discussed in the latter's judgement.

The referring Court had "little doubt" that the Basque Country and its Historic Territories met the "institutional autonomy" criterion. Regarding the "procedural autonomy" criterion, the Court expressed some doubt in view of the existence of procedures of a conciliatory and reciprocal nature which tend to guarantee that draft legislation is not contrary to the Economic Agreement. The Court also mentioned certain negative limits to the Basque legislation established by the Agreement which refer (a) to an overall effective fiscal burden equivalent to that in the rest of the State, (b) to the freedoms of movement and of establishment, and (c) to the exclusion of discriminatory effects. Compliance with these limits is subject to judicial review.

33. English translation quoted in Para. 32 of the *Basque Country* judgement.

With regard to the "economic autonomy" criterion, the referring Court stated that there were no specific legal provisions in the system to the effect that a hypothetical fiscal deficit caused by lower revenue was to be borne or subsidized by the State. The Court's "only doubt" pertained to the existence of matters in the exclusive competence of the State which exerted economic influence over the Basque Country, such as (among others) the monetary system (now actually controlled by the European Central Bank), the coordination of the general planning of economic activity, and the economic regulation of social security and public works of general interest. Given these limitations, the existence of a different economic framework in the Basque Country was conditioned by the requirements derived from the unity of the market and of the economic order.

4.2. Advocate-General Kokott's opinion

At the outset of her analysis of the application of the *Azores* judgement to the measures adopted by the Historic Territories, Advocate-General Kokott pointed out the different procedural situation of the two cases. The *Azores* judgement was given in an action for annulment of a decision by the Commission under Art. 230(1) of the EC Treaty. "The Court therefore has to give a final decision itself on whether the Commission proved that the contested measure was State aid." The *Basque Country* case, however, was a preliminary ruling proceeding under Art. 234 of the EC Treaty, in which the ECJ's task was limited to interpreting Art. 87(1) of the EC Treaty. "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.[34]

The Advocate-General then referred to the Commission's opinion that, in the *Azores* judgement, the ECJ required a two-stage examination for assessing the autonomy of the local authority: it must first be examined whether the authority "plays a fundamental role in the definition of the political and economic environment in which undertakings operate", and only when this has been established is it relevant whether the three criteria relating to autonomy have been satisfied. In the Advocate-General's view (Para. 69), in the *Azores* judgement, it was clear "that the Court is concerned with autonomy in adopting the specific measures and not general freedom to act in economic policy". As mentioned above, this position, referred to as the "fourth condition theory", was rejected by the Court of First Instance in its *Gibraltar* judgement.

The Advocate-General then asked the question whether the correct connecting factor was the individual Historic Territories or the Autonomous Community of the Basque Country,[35] that is, whether it was the former or the latter that had to be compared with the central State. The extent of this doubt was manifest considering the complex system of institutional relationships within the Basque Country described above. As the Advocate-General pointed out, while it was the Historic Territories that adopted the tax rules, coordination within the Basque Country clearly resulted in the *normas forales* of all three Territories being largely identical.

In her opinion, a distinction had to be drawn between two scenarios: (a) where the coordination is independent of the provisions laid down by the central State, and (b) where the coordination is based on such provisions. In the first case, in the Advocate-General's formulation,

> 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.

In the second case, the autonomy of the Historic 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."

Examining the three aspects of autonomy set out in the *Azores* judgement, the Advocate-General concentrated on procedural autonomy and on economic or financial autonomy; institutional autonomy was out of the question. Instead of procedural autonomy, she preferred the expression "organizational autonomy" and distinguished between "procedural and substantive organizational autonomy".[36] "Procedural organizational 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".[37] In the Advocate-General's opinion, procedural organizational autonomy is not affected where the central State and local authority inform and consult one another about legislative plans, at least when the local authority remains free to adhere to its plans even in the case of an unfavourable opinion from the central government. The Advocate-General thought that the requisite was met in the Basque Country regime, notwithstanding the final assessment by the referring court.

Substantive organizational autonomy exists, in the Advocate-General's opinion, when "the local legislator is able to decide freely on the structure of tax rules". "However", she immediately added, "the legislator does not have full freedom in any democratic, constitutional order. Rather, the legislator is always bound by constitutional provisions .... Community law also imposes limits

34. Advocate-General Kokott's opinion, Paras. 59 and 60.
35. Id., Para. 72 et seq.
36. Id., Para. 79. The original German uses the terms "*Gestaltugsautonomie*" for the general criterion, which can be translated as "configuration autonomy", and "*formelle*" and "*materielle Gestaltungsautonomie*" for its two aspects.
37. Id., Para. 85.

on national legislation." This also applied to the constitutional limits that the Historic Territories had to observe as long as they did 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".[38]

The Advocate-General then examined those constitutional limits and suggested some tests as to whether substantive organizational autonomy exists, like the possibility for the regions to enter into fiscal competition with one another, notwithstanding the solidarity principle, the extent to which the tax regime of the Historic Territories can be regarded as a system independent of the central State system, and whether material parameters such as the tax rate and the basis for assessment may be fixed in derogation from central law. It was, however, for the referring court to decide whether or not these criteria were met. The existence of judicial review of the provisions adopted by the Historic Territories did not constitute a restriction on the autonomy, provided it did not extend to the expediency of those provisions.

With regard to financial autonomy,[39] the Advocate-General formulated some relevant statements. First, in order to determine whether this criterion is met, it is necessary in complex situations to undertake a comprehensive assessment of the financial relations between the central State and its subdivisions. Financial autonomy is not always to be rejected where, following this general examination, there is, on balance, a financial transfer from the central State to the regional authority; this conclusion requires the existence of a connection between the financial transfer and the local tax legislation. In order to establish such a connection, two requirements must be satisfied: first, the level of the local tax revenue must be included as a parameter in determining any financial transfer; and second, a reduction in tax revenue must also lead to a corresponding compensatory adjustment in the transfer of funds.

In the *Basque Country* case, the principal object of scrutiny was, of course, the quota. The Advocate-General stated her "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 tax revenue". Again, it was for the national court to make the final assessment.

If the *Azores* judgement was received with relief in the Basque Country, Advocate-General Kokott's opinion caused sheer delight, for it constituted a reassuring omen of the forthcoming ruling by the ECJ.[40] As a matter of fact, the ECJ basically confirmed her opinion.

4.3. The ECJ's judgement

Having examined in some detail the precedents of the *Basque Country* judgement of 11 September 2008, it is only necessary now to highlight its most relevant statements.

The ECJ completely ratified the doctrine on selectivity of a tax measure for purposes of the State aid rules initially set out in the *Azores* judgement of 6 September 2006,[41] which has become well-established case law. The ECJ also firmly dismissed the Commission's "fourth condition theory":

> Contrary to the Commission's contention, paragraphs 58 and 66 of the judgment in *Portugal v. Commission* do not lay down any precondition for the operation of the three criteria set out in paragraph 67 of that judgment.[42] ... [W]here an infra-State body is sufficiently autonomous, in other words, when it has autonomy from the institutional, procedural and economic points of view, it plays a fundamental role in the definition of the political and economic environment in which the undertakings operate. That fundamental role is the consequence of the autonomy and not a precondition for that autonomy.[43]

> It follows that the only conditions which must be satisfied in order for the territory falling within the competence of an infra-State body to be the relevant framework in order to assess whether a decision adopted by that body is selective in nature are the conditions of institutional autonomy, procedural autonomy and economic and financial autonomy as set out in paragraph 67 of *Portugal v. Commission*.[44]

Regarding the question of which infra-State body is to be taken into consideration, the ECJ pointed out that there is little doubt that, considered as such, the Historic Territories do not enjoy sufficient autonomy (Para. 67):

> The existence of political and fiscal autonomy requires that the infra-State body assume responsibility for the political and financial consequences of a tax reduction measure. That cannot be the case where the body is not responsible for the management of a budget, in other words, where it does not have control of both revenue and expenditure. It appears that that is the situation in which the Historical Territories find themselves, as they are competent only in tax matters and the other areas of competence belong to the Autonomous Community of the Basque Country.

The ECJ did not, however, find it "indispensable" to take into consideration only the Historic Territories or, alternatively, only the Autonomous Community of the Basque Country. For historical reasons, the areas of competence exercised in the geographical territory corresponding to both the Historic Territories and the Autonomous Community are organized in such a way that competence for tax matters is vested in the Territories and competence for economic matters is vested in the Autonomous Community. In order to prevent this leading to incoherent situations, this sharing of areas of competence necessitates close collaboration between the

38. Id., Para. 89.
39. Id., Para. 106 et seq.
40. See Alonso Arce, I., "La Abogada General del Tribunal de Luxemburgo respalda el Concierto", *Forum Fiscal de Bizkaia* (June 2008), at 15 (electronic version reference 085.207) (the issues of this journal are numbered only from the August 2008 issue, which is No. 135); Alonso Arce, I., "La autonomía total de los Territorios Históricos según la Abogada General del Tribunal de Luxemburgo", *Forum Fiscal de Bizkaia* (July 2008), at 17 (electronic version reference 085.246); and Manzano Silva, M.E., "Concierto Económico y ayudas estatales (Las conclusiones de la Abogada General Sra. Juliane Kokott del 8 de mayo de 2008)", *Quincena Fiscal*, 15-16/2008 at 15.
41. *Basque Country* judgement, Para. 46 et seq.
42. Id., Para. 53.
43. Id., Para. 55.
44. Id., Para. 60.

different bodies.[45] On these grounds, the ECJ came to the conclusion that:

> it is both to the Historical Territories and to the Autonomous Community of the Basque Country that reference must be made for the purpose of determining whether the infra-State body made up of those Historical Territories and that Community enjoys sufficient autonomy to constitute the reference framework in the light of which the selectivity of a measure adopted by one of those Historical Territories should be assessed.[46]

The ECJ upheld the Advocate-General's opinion concerning the relevance for the autonomy of the Historic Territories of judicial review of the provisions enacted by them by confirming that it is not the existence of that review that is relevant, but the criterion the court uses when carrying out that review.[47] Thus, an infra-State body does not lack autonomy for the sole reason that the acts which it adopts are subject to judicial review.[48]

Applying the autonomy criteria, the ECJ summarily accepted the institutional autonomy of the Basque Country and focused on procedural and financial autonomy. Concerning the first, the ECJ dismissed the arguments based on the coordination mechanisms and on the principles that had to be observed by the legislation of the Historic Territories (Para. 107):

> [T]he essential criterion for the purpose of determining whether procedural autonomy exists is not the extent of the competence which the infra-State body is recognised as having, but the possibility for that body, as a result of that competence, to adopt a decision independently, in other words, without the central government being able directly to intervene as regards its content.

It fell to the national court, however, to determine whether the procedural autonomy criterion was satisfied in the cases in the main proceedings.[49]

The ECJ's analysis of whether the financial autonomy criterion was met by the Basque Country focused mainly on the quota, as was to be expected. The ECJ pointed out that the 6.24% attribution rate, although determined on the basis of economic data, was set during what were essentially political negotiations between the State and the Autonomous Community of the Basque Country. But the ECJ acknowledged (Para. 127) that "a decision to reduce the tax rate thus does not necessarily have an impact on the level of that rate". Regarding the Commission's contention that the rate was undervalued and that consequently the Historic Territories contributed less than they should to State burdens, the ECJ replied that it did not fall within its jurisdiction to decide whether the quota was correctly calculated. The ECJ added that an undervaluation of the attribution rate could constitute only an indicator that the Historic Territories lacked economic autonomy, but "there must be compensation, namely, a causal relationship between the tax measure adopted by the foral authorities and the amounts assumed by the Spanish State".[50] The ECJ deferred to the national court the determination of whether "the setting of the attribution rate and, more generally, the calculation of the quota may have the effect of causing the Spanish State to compensate the consequences of a tax measure adopted by the foral authorities".[51]

The ECJ also considered other financial relationships and transfers between the State and the Basque Country and upheld the Advocate-General's opinion that the mere existence of these transfers was not enough to demonstrate the lack of financial autonomy since they may take place for reasons unconnected with the tax measures.[52] The ECJ closed its arguments insisting on the limits of its jurisdiction:

> In any event, it is not for this Court to declare whether the foral laws at issue in the main proceedings constitute State aid within the meaning of Article 87(1) EC. Such a classification implies that the Court proceeds to determine, interpret and apply the relevant national law and to examine the facts, tasks which fall within the jurisdiction of the national court, whilst this Court has sole jurisdiction to interpret the concept of State aid within the meaning of Article 87(1) EC in order to provide the national court with the criteria which will enable it to decide the cases before it.
>
> It must thus be held that, on the basis of the elements examined and all the other elements which the national court considers relevant, it is for that court to determine whether the Historical Territories assume the political and financial consequences of a tax measure adopted within the limits of the powers conferred on them.[53]

One last caveat added by the ECJ was that the determination of whether the autonomy criteria were satisfied:

> may be carried out only after prior review in order to ensure that the Historical Territories and the Autonomous Community of the Basque Country respect the limits of their areas of competence since the rules on, in particular, financial transfers have been drawn up on the basis of those areas of competence as defined.
>
> The finding of infringement of the limits of those areas of competence could call into question the results of the analysis carried out on the basis of Article 87(1) EC, since the reference framework for assessing whether the law of general application in the infra-State body is selective is no longer necessarily constituted by the Historical Territories and the Autonomous Community of the Basque Country, but could, where appropriate, be extended to the whole Spanish territory.[54]

Which hypotheses the ECJ had in mind are not entirely clear. This rather obscure passage can be understood as meaning that, in order to assess the region's autonomy, the powers exercised in reality by the local authority must be taken into account, not the (formal) legal attribution of competences.

5. Reception of the Judgement in Spain

5.1. Judgements of the High Court of the Basque Country

In the meantime, the High Court of the Basque Country, which had requested the preliminary ruling from the ECJ, decided the main proceedings by no fewer than 18

45. Id., Paras. 68 to 70.
46. Id., Para. 75. See also Para. 86.
47. Id., Para. 79.
48. Id., Para. 83.
49. Id., Para. 110.
50. Id., Para. 129.
51. Id., Para. 131.
52. Id., Para. 135.
53. Id., Paras. 139 and 140.
54. Id., Paras. 142 and 143.

judgements on 22 December 2008.[55] The High Court quite rightly understood that its task was to rule, in light of the interpretation criteria provided by the ECJ, on the original claims submitted to it, whose object and scope were not altered by the request for a preliminary ruling. As the High Court put it: "What the ECJ provides is a method of interpretation, not a questionnaire to be answered by the referring organ". The Court added that the ECJ did not address orders to the national court requesting it to research new facts, which would give rise to a new procedure different from the one already finished and awaiting judgement.

The High Court then ruled on the application of the three autonomy criteria. Regarding procedural autonomy, the Court pointed out that, although the ECJ's findings did not impair its own competence to apply the national law and EU law, no aspects other than those considered by the ECJ were in sight; thus, the analysis of this criterion had to be considered exhausted. This also showed that the questioning of this aspect by the claimants lacked any foundation.

As for economic autonomy, the Court considered that the ECJ's judgement dispelled its doubts arising from the State's competence for general economic matters. The Court also noted the ECJ's rejection of the Commission's contention that playing a fundamental economic role is a precondition of autonomy.

The High Court paid special attention to the *cupo* or quota. After a detailed description of its mechanism, the Court concluded that the amount of the quota bore no relationship to the tax revenue of the Historic Territories. Regarding the (6.24%) attribution rate, the Court pointed out that, even if it was undervalued at a given time, no consistent causal relationship could be established with the tax measures at issue.

As expected, the High Court of the Basque Country dismissed the claims.

5.2. Commentators' opinions

The reaction of Basque commentators to the ECJ's judgement was one of victory: the rights of the Basque Country had finally been recognized at the highest judicial level and were now safe from further challenges;[56] the ECJ had proved them right.[57] The defeated party was, in the first place, the European Commission and its concept of "fiscal uniformity",[58] but also the Supreme Court of Spain. In Alonso Arce's opinion, this Court's judgement of 9 December 2004 had performed a "Copernican turn" on the principles on which the analysis of the legislative autonomy of the Historic Territories was founded. Until then, the question had been whether they had respected the limits imposed by the Economic Agreement, but the Supreme Court's judgement ruled that the *normas forales* infringed the State aid rules of the EC Treaty and were therefore contrary to national law. As Alonso Arce put it, the State aid rules thus "became the excuse external to the Economic Agreement to annul the Normas Forales enacted in the exercise of the autonomy that it recognized". What the ECJ's judgement now said is that Community law was violated only insofar the *normas forales* exceeded the limits of the Agreement because the Basque regime as such was not contrary to EU law.

Alonso Arce also emphasized the ECJ's finding that it is both the Historic Territories and the Autonomous Community of the Basque Country that constitute the reference for the purpose of assessing autonomy. In his opinion, this confirmed that the Basque Economic Agreement regime is unitary and implies a bilateral relationship between the Basque institutions as a whole and the State. With respect to the State aid rules, this entails that the Historic Territories themselves constitute three symmetrically autonomous systems. Consequently, there could be a different corporate tax in each of the Territories, and this would be compatible with Community law.[59]

Basque commentators expressed an aspiration that, if fulfilled, would crown the recognition of the Basque Country's fiscal autonomy and its attempt to achieve "fiscal uniformity". What they aspire to is that the competence of the Constitutional Court be established to rule on actions against the *normas forales*, i.e. that these actions be brought in the Constitutional Court and not in the High Court of the Basque Country, as happens at present. This would acknowledge the status of *normas forales* as being equivalent to parliamentary laws. The expression used to refer to this process is "to armour" those *normas*.[60]

From the different perspective of the "common territory" is shown the importance of the ECJ's judgement not only for the Basque Country but also for Navarre, which has a similar fiscal regime, as well as for the remaining Autonomous Communities subject to the general financial relationships with the State, which possess certain legislative competence for State taxes.[61]

55. Nos. 875/08 to 879/08 and 882/08 to 894/08. Seventeen of them are the same except for minor differences owing to certain variations in the claimants' arguments. The 18th judgement (No. 892/08) dismissed the claim on the ground of a formal defect in the challenged provision.

56. In Orena Domínguez, A., "Las normas forales tienen cabida en Europa: Sentencia del Tribunal de Justicia de las Comunidades Europeas de 11-9-2008 (TJCE 2008, 201)", *Quincena Fiscal*, 18/2008 at 67, 75, the author expressed his hope that the ECJ's judgement would put an end to the fiscal battle and would give place to a climate of legal security for Basque taxpayers.

57. "And Luxembourg has proved us right ..." is the translation of the title of the article by Alonso Arce, I., "Y Luxemburgo nos dio la razón ...", *Forum Fiscal de Bizkaia* (2008), No. 137 (Part I) at 11, and No. 138 (Part II) at 11 (electronic version references 085.373 and 085.414).

58. See Alonso Arce, "La Abogada General ...", supra note 40, at 24.

59. This idea is elaborated in Alonso Arce, I., "Autonomía normativa interna de los Territorios Históricos en materia de Impuesto sobre Sociedades", *Forum Fiscal de Bizkaia*, No. 139 (2009) at 19 (electronic version reference 095.001).

60. Alonso Arce, "La Abogada General ...", supra note 40, at 24; Orena Domínguez, supra note 56, at 75; Etxeberria Monasterio, J.L., "En defensa del 'Blindaje' de las Normas Forales Tributarias", *Forum Fiscal de Bizkaia* (June 2008), at 25 (electronic version reference 085.208).

61. See Falcón y Tella, R., "Las normas forales y la prohibición de ayudas de Estado: inexistencia de selectividad regional (STJCE 11 septiembre 2008 (TJCE 2008, 201), UGT Rioja y otros contra Juntas Generales)", *Quincena Fiscal*, 20/2008 at 9, pointing out that, although Navarre has set up tax incentives often identical to the Basque incentives, they were practically unnoticed by the European Commission and by the neighbouring Autonomous Communities. See also Ruiz Almendral, supra note 33, at 525.