# Opinion Statement ECJ-TF 2/2015 on the Decision of the European Court of Justice in *European Commission v. United Kingdom* ("Final Losses") (Case C-172/13), Concerning the "*Marks & Spencer* Exception"

**This is an Opinion Statement prepared by the CFE ECJ Task Force concerning the decision given by the ECJ in *European Commission v. United Kingdom* ("Final Losses") (Case C-172/13), on 3 February 2015. This case is in some ways a follow-up to the ECJ's decision in *Marks & Spencer* (Case C-446/03) and comments on whether the legislative amendments introduced by the United Kingdom are sufficient to ensure compliance with EU law. After illustrating the case, arguments of the parties and decision of the Court, this Opinion Statement focuses on selected critical points from the Court's decision and Advocate General Kokott's Opinion.**[1]

## 1. Background and Issues

UK domestic tax law provides for a system of "group relief" that allows losses incurred by one company to be surrendered to, and offset against the profits of, another company of the same group arising in the same accounting period. Under these rules, group relief had initially been restricted to UK companies and UK permanent establishments (PEs). Non-UK losses could never be surrendered and offset against UK profits. Questioning the compatibility of this domestic regime with EU law, and more specifically with the freedom of establishment, Marks & Spencer challenged that exclusion and the issue was eventually referred to the ECJ.[2] In its decision in *Marks & Spencer* (Case C-446/03), the Court's Grand Chamber found a restriction of the freedom of establishment, but also viewed that restriction as justified unless there was no possibility to use the losses at issue in their home jurisdiction. The Court held that:[3]

> […] as Community law now stands, Articles 43 EC and 48 EC do not preclude provisions of a Member State which generally prevent a resident parent company from deducting from its taxable profits losses incurred in another Member State by a subsidiary established in that Member State although they allow it to deduct losses incurred by a resident subsidiary. However, it is contrary to Articles 43 EC and 48 EC to prevent the resident parent company from doing so where the non-resident subsidiary has exhausted the possibilities available in its State of residence of having the losses taken into account for the accounting period concerned by the claim for relief and also for previous accounting periods and where there are no possibilities for those losses to be taken into account in its State of residence for future periods either by the subsidiary itself or by a third party, in particular where the subsidiary has been sold to that third party.

This reasoning is known as the "*Marks & Spencer* exception"[4] or the "final losses" doctrine. In short, to ensure non-discriminatory application of group relief, the Court held that losses incurred by non-resident subsidiaries may be taken into account by a resident parent company, but only when it is possible in domestic situations and when it is no longer possible to take them into account in the State of the subsidiary. Debate continues as to whether this is also the case where the profit-making and loss-making company are not a parent and subsidiary, but have a different relationship within the group. Despite criticism and the scope being unclear,[5] the "final losses" doctrine became a constant theme in the Court's subsequent case law on foreign losses, for example, in *Lidl Belgium* (Case C-414/06),[6] *X Holding* (Case C-414/06),[7] *A Oy* (Case C-414/06)[8] and *K* (Case C-322/11).[9]

Following the decision in *Marks & Spencer*, the United Kingdom reacted by amending its Income and Corpora-

* The members of the Task Force include: Alfredo Garcia Prats, Daniel Gutmann, Volker Heydt, Eric Kemmeren, Georg Kofler (Chair), Michael Lang, Franck Le Mentec, João Félix Pinto Nogueira, Pasquale Pistone, Albert Rädler†, Stella Raventos-Calvo, Isabelle Richelle, Friedrich Roedler and Kelly Stricklin-Coutinho. Although the Opinion Statement was drafted by the ECJ Task Force, its content does not necessarily reflect the position of all members of the group. The Task Force wishes to thank George Gillham and Rupert Shiers for their valuable comments.

1. UK: Opinion of Advocate General Kokott, 23 October 2014, Case C-172/13, *European Commission v. United Kingdom*, ECJ Case Law IBFD.
2. UK: ECJ, 13 Dec. 2005, Case C-446/03, *Marks & Spencer plc v. David Halsey (Her Majesty's Inspector of Taxes)*, ECJ Case Law IBFD, referred to the ECJ by the UK High Court in UK: High Court, 16 July 2003, *Marks & Spencer v. Inland Revenue*, [2003] EWHC 1945 (Ch); the preceding decision in UK: Special Commissioners, 17 Dec. 2002, *Marks & Spencer plc v. David Halsey*, SPC00352, [2003] STC (SCD) 70 = [2003] EuLR 46, declined to find a violation of EU law.
3. *Marks & Spencer* (C-446/03), para. 59.
4. Found in *Marks & Spencer* (C-446/03), para. 55.
5. *See*, for example, AG Opinion in *Commission v. United Kingdom* (C-172/13), para. 36 et seq. (calling for the abandonment of the "*Marks & Spencer* exception").
6. DE: ECJ, 15 May 2008, Case C-414/06, *Lidl Belgium GmbH & Co. KG v. Finanzamt Heilbronnl*, ECJ Case Law IBFD.
7. NL: ECJ, 25 Feb. 2010, Case C-337/08, *X Holding BV v. Staatssecretaris van Financiën*, ECJ Case Law IBFD.
8. FI: ECJ, 21 Feb. 2013, Case C-123/11, *Veronsaajien oikeudenvalvontayksikkö and Valtiovarainministeriö v. Oy A*, ECJ Case Law IBFD.
9. FI: ECJ, 7 Nov. 2013, Case C-322/11, *K*, ECJ Case Law IBFD.

© IBFD

tion Taxes Act 1988 (ICTA 1988),[10] with effect from 1 April 2006 and provided administrative guidance on the new rules.[11] Those conditions were substantially kept in the Corporation Tax Act 2010 (CTA 2010).[12] The new regime allows for foreign losses to be offset against UK profits if the losses could not be taken into account in the jurisdiction where they were sustained (or broadly any other jurisdiction – this is discussed in section 3.) in the period they were incurred, or in previous or future accounting periods.[13] For future periods, the moment to assess whether or not they can be taken into account is "at the time immediately after the end" of the accounting period in which the losses were sustained[14] (procedurally, however, the claim for relief can be lodged at any time within two years of the end of the period, or longer if HMRC open an enquiry into the tax return of the company claiming the losses for offset).[15] Under the CTA 2010 rules, in order to qualify for group relief in the United Kingdom, a foreign loss has to satisfy four conditions: (1) the "equivalence condition" (i.e. the foreign loss has to be of the same nature as losses allowable under UK's group relief rules); (2) the "EEA tax loss condition" (i.e. the loss should be considered as a loss under the law of the EEA territory of residence of the foreign subsidiary); (3) the "qualifying loss condition" (i.e. the loss cannot be relieved in the EEA Member State of residence and cannot be relieved in another EEA Member State); and (4) the "precedence" condition (i.e. the loss cannot have been relieved in any territory of residence of an intermediate foreign company).[16] Accordingly, a loss determined under the rules of the State where it was incurred must be recalculated in accordance with UK principles[17] and only the lower of the two amounts (foreign calculation and UK calculation) will be considered.[18]

Although the United Kingdom amended its legislation after the Court's judgment in *Marks & Spencer*, this case was brought because the Commission took the position that "it continues to impose conditions on cross-border group loss relief which, in practice, make it very difficult to benefit from" such relief and that this infringes "the principle of non-discrimination and the freedom of establishment, set down in the Treaty".[19] The Commission's claims were twofold:[20]

(1) First, the Commission claimed that section 119 of the UK Corporate Tax Act 2010, which requires the assessment of the usability of losses for future years "at the time immediately after the end" of the accounting period when the losses were sustained, would make it "virtually impossible for a resident parent company to obtain cross-border group relief". The Commission argued that under UK rules, cross-border group relief may be granted in only two situations: (1) where no provision is made under the legislation of the state of residence of the non-resident subsidiary for losses to be carried forward and (2) where the non-resident subsidiary enters into liquidation before the end of the tax year in which the losses are sustained. Conversely, "[c]ross-border group relief is thus precluded in the normal commercial situation" (i.e. outside a liquidation) and, moreover, "relief is limited to losses sustained in a single tax period". Compliance with the *Marks & Spencer* principle would, however, require that the possibility of obtaining tax relief in the state of residence be assessed (1) at the time when the claim for group relief is made in the United Kingdom and (2) on the basis of the actual facts of the case, and not on the basis of some theoretical possibility (of subsequently taking into account losses sustained by the non-resident subsidiary) that exists only because the foreign subsidiary has not yet been placed in liquidation.

(2) Second, the Commission raised the obligations imposed on the United Kingdom by the ECJ's decision. The Commission noted that the new regime in the United Kingdom came into force only on 1 April 2006, and argued that UK law should have been given retroactive effect in order to allow cross-border group relief for losses incurred before 1 April 2006.

The United Kingdom rebutted the Commission's arguments.[21] It claimed that it followed closely the Court's guidance and that the "*Marks & Spencer* exception"[22] required assessment (of the possibility of loss carry-forward) to be made at the end of the period in which the losses arise. Moreover, the United Kingdom argued that the requirements of the domestic rules could be met in cases beyond those mentioned by the Commission, as domestic law did not require the subsidiary's liquidation before the end of the period for loss offset to be permitted. Rather, many factors could be taken into account at the end of the accounting period in order to ascertain the fulfilment of the condition, such as an intention to wind

10. With UK: Finance Act 2006, National Legislation IBFD.
11. *See* HMRC's guidance in CTM81500 – Groups: group relief: surrendering company not UK resident, available at http://www.hmrc.gov.uk/manuals/ctmanual/ctm81500.htm.
12. UK : Corporation Tax Act 2010, National Legislation IBFD.
13. *See* sections 188 and 119(3) CTA 2010.
14. Section 119(1) and (4) CTA 2010. *See also* the example in CTM8535: "If a company has made a loss in its EEA territory of residence but at the yearend it continues to exist, either trading or with other sources of income, into the next period and there is a possibility that relief may arise in a later period, against trading or other profits then the loss cannot be surrendered. If, as a matter of fact, no profits arose before the carry-forward of relief became time barred, this does not alter the position that the loss was carried forward and might have been given as relief. This is a distinct test applied to the situation existing at the time of loss and does not interact with the two-year limit for claims to group relief, which remains unchanged", available at http://www.hmrc.gov.uk/manuals/ctmanual/ctm81535.htm.
15. *See* UK: Finance Act 1998, schedule 18, paras. 14(1)(a) and 74(1)(a).
16. *See* section 113 CTA 2010; *see also* CTM81500 et seq. and in particular CTM81510, *supra* n. 11.
17. *See* CTM81560, *supra* n. 11.
18. *See* section 128 CTA 2010 and CTM81590, *supra* n. 11.
19. *See* Eur. Commn. Press Release IP/12/1017 (27 Sept. 2012), *Taxation: Commission refers UK to the European Court of Justice over cross-border loss relief*; *see also* IP/09/1461 (8 Oct. 2009), *Corporate taxation: Commission refers the United Kingdom to the European Court of Justice over improper implementation of an ECJ ruling on cross-border loss relief*.
20. UK: ECJ, 3 Feb. 2015, Case C-172/13, *European Commission v. United Kingdom of Great Britain and Northern Ireland*, paras. 14-16, ECJ Case Law IBFD.
21. Id., at paras. 17-18.
22. *Marks & Spencer* (C-446/03), para. 55.

 © IBFD

up a loss-making subsidiary or the initiation of a liquidation process soon after the end of the accounting period.

## 2. The Decision of the Court

The Court's Grand Chamber dismissed the infringement action brought by the Commission against the United Kingdom,[23] reiterating and refining its previous decision in *Marks & Spencer*. The Court basically reaffirmed that UK law, by creating a difference in a UK company's ability to offset losses between those incurred by resident and non-resident companies, hinders "the exercise by the group parent company of its freedom of establishment",[24] and that the measure should be tested against "three overriding reasons in the public interest, taken together", i.e. "the need to preserve the balanced allocation of powers of taxation between Member States, the need to prevent the double use of losses and the need to combat tax avoidance".[25] Also, as in *Marks & Spencer*, the Court noted that these three justifications should be taken together when testing proportionality, which in turn must be appropriate to achieving the objectives mentioned and not go beyond what is necessary to achieve them. And, as in *Marks & Spencer*, the Court ruled that domestic law would be disproportionate if the possibility of offsetting the losses by the parent company was "wholly precluded". Surrender and offset, however, has to be allowed (only) of "definitive losses".[26] This review of *Marks & Spencer* provided the framework for the analysis of the Commission's two claims.

As for the Commission's first claim (i.e. that loss deduction is "virtually impossible"), the Court noted that the Commission did not claim that domestic law absolutely prevents loss deduction; it only claimed that it makes it "virtually impossible". In the Commission's reading of UK law this is so because losses could only be deducted in two situations:

- when no possibility of use exists in the State where the losses were incurred (for example, absence of loss carry-forward); and
- when the subsidiary is already in liquidation at the close of the relevant period.

Following *K* (Case C-322/11),[27] the first situation was considered irrelevant by the Court, as such losses would not be "definitive losses" as the term was used in *Marks and Spencer*. As for the second situation (i.e. cases where loss carry-forward is allowed in the State of the subsidiary), the Court rejected the Commission's claim that deduction is only possible when the subsidiary is liquidated before the end of the accounting period as an incorrect interpretation of domestic law:[28]

> As regards the second situation referred to, it should be noted, first, that the Commission has not established the truth of its assertion that Section 119(4) of the CTA 2010 requires the non-resident subsidiary to be put into liquidation before the end of the accounting period in which the losses are sustained in order for its resident parent company to be able to obtain cross-border group relief. […] Under Section 119(4) of the CTA 2010, in fact, the assessment as to whether the losses sustained by a non-resident subsidiary may be characterised as definitive, as described in paragraph 55 of the judgment in Marks & Spencer (EU:C:2005:763), must be made by reference to the situation obtaining 'immediately after the end' of the accounting period in which the losses were sustained. It is thus clear from the wording of that provision that it does not, on any view, impose any requirement for the subsidiary concerned to be wound up before the end of the accounting period in which the losses are sustained. […] Secondly, it should be borne in mind that losses sustained by a non-resident subsidiary may be characterised as definitive, as described in paragraph 55 of the judgment in Marks & Spencer (EU:C:2005:763), only if that subsidiary no longer has any income in its Member State of residence. So long as that subsidiary continues to be in receipt of even minimal income, there is a possibility that the losses sustained may yet be offset by future profits made in the Member State in which it is resident […]. […] Referring to a specific example of a resident parent company which obtained cross-border group relief, the United Kingdom confirmed that it is possible to show that losses sustained by a non-resident subsidiary may be characterised as definitive, as described in paragraph 55 of the judgment in Marks & Spencer (EU:C:2005:763), where, immediately after the end of the accounting period in which the losses have been sustained, that subsidiary ceased trading and sold or disposed of all its income producing assets.

As for the Commission's second claim (i.e. that the UK legislation does not permit surrender and offset for periods before 1 April 2006), the Court dismissed this claim by stating that the Commission failed to provide evidence of situations in which relief for losses sustained before that date was denied.

## 3. Comments

The decision in *European Commission v. United Kingdom* is another landmark in the long line of ECJ decisions on cross-border utilization of losses. Since late 2005, with *Marks & Spencer* (itself a case that dealt with losses incurred in the mid 1990s[29] by companies that ceased operations in the early 2000s),[30] the Court has been dealing with its legacy (and problems of implementation), for example, in *Lidl Belgium*,[31] *X Holding*,[32] *A Oy*[33] and *K*,[34] adding increasing complexity and detail to the "*Marks & Spencer* exception". Ten years ago, this exception for "final losses" seemed to apply, in particular, with regard to the Member States' "need to prevent the double use of losses" (because there is no remaining risk of such double utilization if a loss becomes "final" in one jurisdiction).[35]

23. *Commission v. United Kingdom* (C-172/13).
24. *See Commission v. United Kingdom* (C-172/13), para. 23.
25. Id., at para. 24.
26. Id., at paras. 26 and 27.
27. *K* (C-322/11), paras. 75-79.
28. *Commission v. United Kingdom* (C-172/13), paras. 34-38.
29. *Marks & Spencer* (C-446/03), para. 20.
30. Id., at para. 21.
31. *Lidl Belgium* (C-414/06).
32. *X Holding* (C-337/08).
33. *A Oy* (C-123/11).
34. *K* (C-322/11).
35. *See also*, for example, FI: Opinion of Advocate General Kokott, 19 July 2012, Case C-123/11, *Veronsaajien oikeudenvalvontayksikkö and Valtiovarainministeriö v. Oy A*, para. 48, ECJ Case Law IBFD, noting that the "final losses" doctrine "can be understood only against the background of the justifications considered in *Marks & Spencer*. The Court based the justification in that case not only on the objective of preserving the allocation of taxation powers among Member States but also, inter alia, on the right of the Member States to prevent losses from being used twice. […] There will be no fear of losses being used twice where the losses of a foreign subsidiary can no longer be used in its State of residence. Consequently a national provision which refuses to allow the parent company

Indeed, as is also clear from subsequent litigation in the United Kingdom (up to the UK Supreme Court),[36] "[t]he judgment in *Marks & Spencer* has not, however, brought about *quieta*, as it has consistently remained unclear with regard to its effects".[37] Hence, even a decade after *Marks & Spencer*, uncertainty regarding its exact meaning remains. It is hence welcome that the Court in *European Commission v. United Kingdom* has given further guidance on the "final losses" doctrine. Moreover, the fact that this decision – just as *Marks & Spencer* – was given by a Grand Chamber certainly increases the authority of the ruling.[38] Some questions, however, remain unanswered.

The operative part of the decision is notably short. It is composed of a mere 25 paragraphs.[39] The controversial character of some *obiter dicta* and the need to seek consensus may have dictated the streamlined nature of the decision. Nonetheless, it should be recognized that the Court's decision was based on the well-known approach to comparability and justification. Most importantly, the Court has not followed Advocate General Kokott's plea to abandon the "*Marks & Spencer* exception"[40] (which would mean that the home State would not even be required to take into account foreign "final losses");[41] instead, it clearly upheld the "final losses" doctrine.

Besides upholding *Marks & Spencer* in principle, the Court further clarifies the exception in several respects:

(1) First, a lack of a loss carry-forward in the subsidiary's state does not lead to losses being available for offset, i.e. "losses sustained by a non-resident subsidiary cannot be characterised as definitive, as described in paragraph 55 of the judgment in *Marks & Spencer* (EU:C:2005:763), by dint of the fact that the Member State in which the subsidiary is resident precludes all possibility of losses being carried forward".[42] This position was already taken by the Court in *K*,[43] which concerned "adverse consequences arising from particularities" of domestic law of the source state, i.e. the rather unusual rule that domestic law allows for no carry-forward at all. The present decision seems to imply, however, that, more generally, in cases of mere legal restrictions on loss-utilization in the subsidiary's state (for example, a lack of a loss carry-forward, anti-abuse provisions, etc.) "the Member State in which the parent company is resident may not allow cross-border group relief without thereby infringing Article 49 TFEU".[44]

(2) Second, the Court confirms and develops its decision in *A Oy* (Case C-123/11)[45] by finding that losses may only be considered as definitive "if that subsidiary no longer has any income in its Member State of residence".[46] More concretely, "[s]o long as that subsidiary continues to be in receipt of even minimal income, there is a possibility that the losses sustained may yet be offset by future profits made in the Member State in which it is resident".[47] Examples mentioned in *A Oy* by the Member States (and obviously acknowledged by the Court) include (very minimal) income from assigning existing leases, capital gains on assets and liabilities.[48] Hence, ceasing trading alone is not sufficient in itself to satisfy the *Marks & Spencer* exception if some income is still being generated (for example, when the company's assets are liquidated).[49] The Court's wording does not make it entirely clear if this is a "black-or-white" test or if a more nuanced proportionality test is required (i.e. it seems to be unclear whether, if there are losses of 100 and a possibility of future trading profits of 10, 90 should be available for surrender). As a side note, in the area of losses of foreign PEs, Advocate General Wathelet recently accepted that losses of a wound-up PE that "stick" with the taxpayer and could (theoretically) be used as carry-forwards if that taxpayer were to resume an activity in the source State are not "final".[50]

(3) Third, one view of the Court accepts that the assessment of "finality" of losses, i.e. the determination that there is no possibility for the losses being taken into account, is to be made "immediately after the accounting period".[51] As UK legislation requires such assessment "immediately after" (and not "before the end")

to use the loss even in such a case goes further than is necessary in order to prevent losses from being used twice".

36. UK: Supreme Court, 22 May 2013, *Commissioners for Her Majesty's Revenue and Customs v. Marks and Spencer plc*, [2013] UKSC 30 and UK: Supreme Court, 19 February 2014, *Commissioners for Her Majesty's Revenue and Customs v. Marks and Spencer plc*, [2014] UKSC 11.
37. AG Opinion in *Commission v. United Kingdom* (C-172/13), para. 42.
38. According to the Statute of the Court, it shall sit in a 13-Judge Grand Chamber "when a Member State or an institution of the Union that is a party to the proceedings so requests" (*see* article 16(3) of Protocol (no. 3) on the Statute of the Court of Justice of the European Union).
39. *See* the "Findings of the Court" in *Commission v. United Kingdom* (C-172/13), paras. 21-45.
40. Advocate General Kokott supported her plea not only by reference to the shortcomings of *Marks & Spencer*, also in light of the Court's subsequent jurisprudence (for example, *A Oy* (C-123/11) and *K* (C-322/11), but also with three main arguments, i.e. that overruling *Marks & Spencer* would (1) resolve contradictions in relation to the Court's other case law on tax matters; (2) be in line with legal certainty; and (3) not infringe the ability-to-pay principle. *See* AG Opinion in *Commission v. United Kingdom* (C-172/13), para. 36 et seq. *See also* the fundamental criticism of the *Marks & Spencer* line of case law in the AG Opinion in *A Oy* (C-123/11), paras. 47-54.
41. Advocate General Kokott rejected a system of loss-utilization with recapture as a possible alternative: "A system of relief for losses incurred by non-resident subsidiaries which was practicable for the internal market could only connect their current relief with the incorporation of future profits, as has already been discussed in *Marks & Spencer*. Such a solution would offer the parent company both the cash flow advantage and the advantage of relief in respect of the total loss. However, this solution would result in a broad degree of equal treatment of losses incurred by non-resident and resident subsidiaries. It would thus undermine the principle in established case-law that a Member State is required to take into account a loss from foreign activity only if it also taxes that activity". *See* AG Opinion in *Commission v. United Kingdom* (C-172/13), para. 49.
42. *Commission v. United Kingdom* (C-172/13), para. 33.
43. *K* (C-322/11), paras. 75-79.
44. *See Commission v. United Kingdom* (C-172/13), para. 33.
45. *A Oy* (C-123/11).
46. *See Commission v. United Kingdom* (C-172/13), para. 36.
47. Id., referring to *A Oy* (C-123/11), paras. 53 and 54.
48. *A Oy* (C-123/11), para. 53.
49. According to the Court's decision in *A Oy*, a mere cease in trade of a subsidiary that is put into liquidation is not sufficient, per se, to conclude that the loss is definitive; *see A Oy* (C-123/11), paras. 51 and 54 and AG Opinion in *Commission v. United Kingdom* (C-172/13), para. 40.
50. DE: Opinion of Advocate General Wathelet, 3 Sept. 2015, Case C-388/14, *Timac Agro Deutschland*, para. 67 at note 45.
51. *See Commission v. United Kingdom* (C-172/13), paras. 34-24.

 © IBFD

of the accounting period, the UK noted (and the Court acknowledged) that this requirement does not necessitate that the subsidiary be (completely) wound up.[52] "Final losses" can, therefore, also exist "where, immediately after the end of the accounting period in which the losses have been sustained, that subsidiary ceased trading and sold or disposed of all its income producing assets".[53] In assessing, at the end of the accounting period in which the losses were sustained, whether losses are "final", "[e]vidence of an intention to wind up a loss-making subsidiary and initiation of the liquidation process soon after the end of the accounting period would be factors to be taken into account".[54] On this view, the "finality" of losses needs to be determined immediately after the period in which the losses were incurred and not as, for example, the UK Supreme Court[55] and other domestic courts[56] have thought – at any later time even if it was clear by then that the loss would not be used in any period after it arose. Hence, if (immediately after the end of the accounting period) there is still some hope of using a subsidiary's losses (for example, through future profits), no relief in the parent's state need be granted, even if it subsequently becomes clear that no such future profits materialized (and, for example, the subsidiary was later liquidated). It is notable, however, that the Court referred twice to the decision of the UK Supreme Court but did not contradict its conclusion on this point.[57]

(4) Fourth, and closely related, if the Court has accepted the timing of assessment under UK law ("immediately after the accounting period"), it might have accepted a (rather surprising) further limitation of the "*Marks & Spencer* exception": the Commission had pointed out that, under the UK rules, "only the loss in respect of a single accounting period may therefore be transferred",[58] and it indeed seems to be the UK's position[59] that only losses sustained in the accounting period that has just ended (and, under certain circumstances, those incurred in the accounting period that immediately follows)[60] can become "final" and qualify for loss relief, but not losses from any previous years, whether effectively relieved in the subsidiary's state or not.[61] If, for the sake of argument, we assume that the Court has fully accepted this conclusion, the "*Marks & Spencer* exception" clearly loses much of its practical importance (because "final losses" are only losses of one taxable period and do not include unused carry-forwards from previous periods) and may put more focus on tax planning by creating strange incentives (for example, to completely wind down or take over the trading activities and all assets of the subsidiary to enable loss utilization). Such a narrow understanding, however, would certainly be a surprise for those domestic courts that have applied the "*Marks & Spencer* exception" to accumulated foreign "final" losses of several years (and not only to the losses of the last taxable year).[62]

It is not entirely clear if all of the above conclusions and their potentially far-reaching effects on the utilization of "final" losses can indeed be inferred from the Court's decision, given that the outcome of an infringement proceeding does not necessarily mean that a Member State's law is in full compliance with EU law. It could also merely indicate that the Commission has failed to prove a violation of EU law. Hence, *European Commission v. United Kingdom* may have limited effect, or it may mean that the "*Marks & Spencer* exception" has been reduced to apply in a very limited number of situations. If there is still hope for future profits, the possibility of using the losses against those profits by carry-forward seems to prevent those losses from being final: even minimal income of a subsidiary creates "a possibility that the losses sustained may yet be offset by future profits made in the Member State in which it is resident".[63] Also, within the framework of a liquidation (and if carry-forward is admissible), it seems that losses of the subsidiary will not be "final" if, for example:

- there are judicial or administrative claims in progress (regardless of whether those claims have been brought by or against the subsidiary);
- there are situations in which an impairment is deemed to be needed, but the loss is not realized (for example, if the subsidiary has a claim against a doubtful debtor

52. Id., para. 35.
53. *See* the UK's position as restated in *Commission v. United Kingdom* (C-172/13), para. 37.
54. *See*, for that understanding of UK legislation, *Commission v. United Kingdom* (C-172/13), para. 18.
55. *Commissioners for Her Majesty's Revenue and Customs v. Marks and Spencer plc* (2013).
56. *See*, for example, DE: BFH, 9 June 2010, I R 107/09, Tax Treaty Case Law IBFD; DE: BFH, 9 Nov. 2010, I R 16/10; and DE: Fiscal Court Hamburg, 6 Aug. 2014, 2 K 355/12.
57. *See* the references to *Commissioners for Her Majesty's Revenue and Customs v. Marks and Spencer plc* (2013) in *Commission v. United Kingdom* (C-172/13), paras. 7 and 42.
58. *See* AG Opinion in *Commission v. United Kingdom* (C-172/13), para. 15 and *Commission v. United Kingdom* (C-172/13), para. 15.
59. *See* section 119(1) and (4) CTA 2010**,** and also the example in CTM8535, *supra* n. 14.
60. As the United Kingdom has contended, "final losses" can also exist "where, immediately after the end of the accounting period in which the losses have been sustained, that subsidiary ceased trading and sold or disposed of all its income producing assets" (*see* the UK's position as restated in *Commission v. United Kingdom* (C-172/13), para. 37). This implies that loss relief is possible not only in "respect of a single accounting period" (as the Commission had claimed), but also for losses from *two* accounting periods, i.e. (1) for the losses incurred in the accounting period *before* the subsidiary ceased trading and sold or disposed of all its income producing assets and (2) for the losses incurred *in* the accounting period in which the subsidiary ceased trading and sold or disposed of all its income producing assets. One might then pose the question if the losses of even more accounting periods may be eligible for relief, for example, because disposing of assets takes more than one accounting period.
61. Imagine the following example: Company X, an EU subsidiary of a UK parent, was active for three years, having only losses (that cannot be carried backwards or otherwise compensated in the state where they are located). In year 1 there were losses of 20,000 (calculated under both tax systems), in year 2, 30,000 and in year 3, 60,000 (and in this year, the company is liquidated in November). Under UK rules it seems that only the losses of year 3, i.e. 60,000, could potentially be relieved in the United Kingdom as "final losses", leaving 50,000 of loss carry-forwards from years 1 and 2 unrelieved.
62. *See*, concerning "final" PE losses, for example, I R 107/09 (9 June 2010) (2000-2001 tax years); DE: BFH, 5 Feb. 2014, I R 48/11 (1997-1998 tax years); and 2 K 355/12 (6 Aug. 2014) (2004-2008 tax years).
63. *See Commission v. United Kingdom* (C-172/13), para. 36, referring to *A Oy* (C-123/11), paras. 53 and 54.

for which the impairment was recorded, but there is at least a theoretical possibility of recovering such an amount);
- assets with unrealized gains are kept at the end of the accounting period; or
- mere theoretical possibilities of income exist. Also, it remains unclear whether procedural rules may have an impact on the concept of "final" losses, for example, with regard to the statute of limitations.[64]

That said, this rather narrow understanding of the "*Marks & Spencer* exception" is in contrast to the whole rationale of a group as pictured by the court, i.e. granting the group a cash-flow advantage "by speeding up the relief of the losses of loss-making companies by allowing them to be set off immediately against the profits of other group companies".[65]

Another open issue is the quantification of "final" losses, i.e. which State's tax rules are used to determine the amount of losses. This question was briefly addressed by the Court in *A Oy*, where it stressed that such a "calculation must not lead to unequal treatment compared with the calculation which would have been made in a similar case for the taking over of the losses of a resident subsidiary".[66] Notwithstanding, the Court, in that case, also noted that such a "question cannot, however, be addressed in an abstract and hypothetical manner, but must be analysed where necessary on a case-by-case basis".[67] Unfortunately, the Court in the present case of *European Commission v. United Kingdom* did not have to address the UK requirement that "final" losses be recomputed in accordance with UK rules and only the lower of the two amounts (foreign computed loss versus domestic computed loss) is to be taken into account at the UK level.[68] While, according to the logic of the UK Supreme Court's decision, this requirement would appear to breach the fundamental freedoms,[69] the authors wonder whether the distinction made under UK law is in line with *Marks & Spencer*. Additional case law is necessary to clarify this issue.

Finally, one may recall *Biehl II* (Case C-151/94),[70] where the Court stated that "incompatibility of provisions of national law with provisions of the Treaty, even those directly applicable, can be definitively eliminated only by means of binding domestic provisions having the same legal force as those which require to be amended", i.e. that legislative actions and not mere administrative practices are required for the proper fulfilment of a Member State's obligations under the Treaty. In the present case, the Court did not elaborate on whether the domestic law amendments were to have retroactive effect, but, rather, dismissed the Commission's second plea: it focused on the burden of proof and pointed out that the Commission "has not established the existence of situations in which cross-border group relief for losses sustained before 1 April 2006 was not granted" and even left open the possibility that a UK Supreme Court decision "according to which losses sustained before that date are not excluded from cross-border group relief, [would] satisfy[y] the need for legal certainty as regards the possibility of obtaining cross-border group relief for losses sustained before that date".[71] From this it might (wrongly) be concluded that the absence of legislative amendments taking effect *ex tunc* (or a delay in taking legislative action at all) is not necessarily perceived as a breach of EU law. The problem of a lack of legislative action (or delay) by Member States is, however, sometimes closely related to the uncertainty surrounding the Court's case law: The *Marks & Spencer* legacy shows the problem surrounding the "final loss exception" (not to speak of legislative implementation), and in some areas it even seems that the Court later relaxes its case law (and hence rewards those Member States who have not taken any legislative action at all). Moreover, in some instances, the Court hands down broad and open-ended decisions and leaves it to the domestic court to decide the issue (recently, for example, in *A Oy*[72]or *C.G. Sopora* (Case C-512/13).[73] While it is certainly true that the Court may only interpret EU law (and not provide normative solutions or rule on domestic law), one may wonder if instead of broad decisions, more precise guidance could be provided by the Court, thus preventing doctrinal debates and continuous litigation.

## 4. The Statement

The Confédération Fiscale Européenne welcomes the additional explanation on the concept of "definitive losses" established in *Marks & Spencer*. Furthermore, it notes that,

64. It may be questioned, for example, if one is obliged to wait (1) for the end of the period defined by the (tax) statute of limitation for the loss to be considered final (as the company may be attributed new profits, for example, in the framework of a transfer pricing adjustment), or (2) even for the end of all periods for administrative and judicial appeals (and if so, only the ordinary or also the extraordinary ones).
65. *See Commission v. United Kingdom* (C-172/13), para. 22 and AG Opinion in *Commission v. United Kingdom* (C-172/13), para. 20. The Court has, however, not considered the "second and more significant" advantage of group relief as pointed out by Advocate General Kokott: "Where, on balance across all the accounting periods for its activity, the subsidiary makes only a loss ('total loss'), group relief goes beyond being a mere cash flow advantage. In this case, on the basis of the loss relief, the parent company does not pay any tax on its income to the amount of the total loss incurred by its subsidiary, and this is definitive. The same situation exists where the subsidiary does not collapse economically, but its loss carry-forward is limited by law and, for that reason, losses incurred by it are not subject to tax relief". *See* AG Opinion in *Commission v. United Kingdom* (C-172/13), para. 21.
66. *A Oy* (C-123/11), para. 59.
67. *A Oy* (C-123/11), para. 60.
68. *See* section 128 CTA 2010 and CTM81590, *supra* n. 11, which explains that "[t]he amount of loss to be relieved is the foreign loss recomputed in accordance with UK principles. However, where the amount recomputed under UK rules exceeds the eligible foreign loss the amount available for surrender by way of group relief cannot exceed the quantum of eligible foreign loss. Such differences will arise, for example, because of timing differences in the recognition of income or expenditure so will either be amounts that have already been relieved or could be relieved in future." *See also* HMRC's guidance in CTM81625, *Groups: group relief: surrendering company not UK resident: examples: comparison of UK and EEA loss*, *supra* n. 11.
69. *See Commissioners for Her Majesty's Revenue and Customs v. Marks and Spencer plc* (2014) (conversion to UK rules of unutilized losses as determined under domestic rules), paras. 49-53.
70. LU: ECJ, 26 Oct. 1995, Case C-151/94, *Commission v. Luxembourg ("Biehl II")*, para. 18.
71. *See Commission v. United Kingdom* (C-172/13), para. 43.
72. *A Oy* (C-123/11).
73. NL: ECJ, 24 Feb. 2015, Case C-512/13, *C.G.Sopora*, ECJ Case Law IBFD.

 © IBFD

in respect of certain factual and legal patterns, it remains doubtful whether and when the exception applies.

The Confédération Fiscale Européenne notes that, in practice, one view is that this exception will be applicable in only very limited circumstances. The "new" understanding of definitive losses and the need to assess usability "immediately after the end of the accounting period" would necessarily lead to the offsetting of losses only being allowed in a limited number of cases. This restriction may lead companies to liquidate their subsidiaries for tax purposes. This hampers economic efficiency and, therefore, the development of the internal market. The latter would require immediate offsetting of foreign losses in the State of the parent company, coupled with an efficient recapture rule.

Hence, the Confédération Fiscale Européenne welcomes the Commission's efforts to re-launch the project on a CCCTB and its plans to propose that, "until full CCCTB consolidation is introduced, group entities should be able to offset profits and losses they make in different Member States".[74] Such cross-border loss relief would be temporary (with recapture once the group entity is profit-making again) and would remove a major tax obstacle in the internal market for businesses.

74. *See* Chapter 3.1 of the Commission's Communication, *A Fair and Efficient Corporate Tax System in the European Union: 5 Key Areas for Action*, COM(2015) 302 final (17 June 2015).