MEMIRA HOLDING AND *HOLMEN*: WHAT ARE FINAL LOSSES?

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The Court of Justice of the European Union (CJEU) recently heard two cases concerning the use of "final losses": *Skatteverket v Memira Holding AB ("Memira Holding")* [2] and *Skatteverket v Holmen AB ("Holmen").* [3] Both cases involved advance rulings in Sweden that were referred to the CJEU for preliminary rulings on matters concerning EU law, in particular, the freedom of establishment.

In both cases, the CJEU delivered judgments concerning the interpretation of paragraph 55 of the *Marks & Spencer* judgment,[4] which concerned situations where cross-border losses could be used by a United Kingdom parent company.

Memira Holding

In *Skatteverket v Memira Holding AB ("Memira Holding")* the Court of Justice of the European Union ("CJEU" or "the Court") determined that for the purposes of assessing the finality of losses in the context of a merger involving a non-resident, loss-making subsidiary, the parent company had to demonstrate that it was impossible for it to deduct those losses by ensuring, in particular by means of a sale to a third party, that the losses are taken into account by a third party for future tax periods.

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2 *Skatteverket v Memira Holding AB ("Memira Holding"),* C-607/17, ECLI:EU:C:2019:510.

3 *Skatteverket v Holmen AB ("Holmen"),* C-608/17, ECLI:EU:C:2019:511.

4 *Marks & Spencer plc v David Halsey (Her Majesty's Inspector of Taxes) ("Marks & Spencer"),* C-446/03, ECLI:EU:C:2005:763.For in-depth analysis of this case, see Tom O'Shea, *Marks and Spencer v Halsey (HM Inspector of Taxes):* restriction, justification and proportionality, EC Tax Review 2006 p.66-82.

Background

Memira Holding AB is a Swedish company with a subsidiary in Germany that was loss-making. This subsidiary ceased activity in Germany and Memira Holding is considering a merger by absorbing its German subsidiary. This would occur without a liquidation of the German subsidiary and without Memira Holding carrying on further activities in Germany after the merger takes place. Under German law, Memira Holding was unable to deduct the losses incurred in Germany since it was not possible to transfer the losses to another company in a merger situation. Consequently, Memira Holding applied to the Swedish Revenue Law Commission (Skatteerättdnämnden) for a preliminary decision (advance ruling) on whether, if it implemented the proposed merger, it was entitled to deduct the losses of its German subsidiary under freedom of establishment. The Revenue Law Commission rejected this claim. On appeal to the Supreme Administrative Court (Högsta förvaltningsdomstolen), the proceedings were stayed while some questions were referred to the CJEU for a preliminary ruling on EU law matters.

Final Losses

The Court noted that the question referred by the Swedish court concerned an interpretation of the concept of "final losses" (or the "no possibilities test") contained in paragraph 55 of its judgment in *Marks & Spencer*. The issue was whether the cross-border losses in the *Memira Holding* merger situation fell within the scope of paragraph 55 of the *Marks & Spencer* judgment.

The Court highlighted that paragraph 55 of the *Marks & Spencer* judgment specifically referred to situations involving a sale or a transfer of the losses to a third party. The Court indicated, in paragraph 25 of *Memira Holding*, that –

> "even if all the other impossibilities referred to in paragraph 55 of the judgment in *Marks & Spencer* have been met, the losses would not be characterised as final if there is a possibility of deducting those losses economically by transferring them to a third party".

Consequently, the Court held, in paragraph 27 of *Memira Holding*, that –

> "in a situation such as that envisaged by Memira, it is for Memira to demonstrate that the possibility referred to in the previous paragraph is precluded, with the mere fact that the subsidiary's State of establishment does not allow the transfer of losses in the event of a merger cannot, in itself, be sufficient to regard the losses of the subsidiary as being final".

The Court explained that if such evidence is adduced and the other conditions set out in paragraph 55 of the judgment in *Marks & Spencer* are met, the tax authorities are required to find that the losses of the non-resident subsidiary are final. This means that it is disproportionate to not allow the parent company to take such cross-border losses into account for tax purposes.

Holmen

In *Holmen*, a Swedish parent company ("Holmen") held, via a subsidiary, several Spanish sub-subsidiaries. One of these sub-subsidiaries had accumulated significant losses and Holmen planned to liquidate that sub-subsidiary. Holmen applied for a preliminary ruling from Revenue Law Commission in Sweden to determine whether, when the liquidation was complete, it would be entitled to use the cross-border final losses in Sweden. The losses were not deductible in Spain because in the year of liquidation such losses could not be transferred. Moreover, under the Swedish rules, the losses could not be used because there was a requirement that the subsidiary sustaining the final losses had to be directly owned.

The Revenue Law Commission rejected the claim for cross-border loss relief. Accordingly, the matter was appealed to the Supreme Administrative Court which referred a number of questions to the CJEU for a preliminary ruling.

First Question

The first question concerned the concept of "final losses" and asked whether it applied in a non-resident sub-subsidiary situation. The Court noted that the Swedish rules made the application of group relief conditional on a direct link between the parent company and the loss-making, non-resident subsidiary that sustained the losses.

The Court indicated that such a condition could be justified in certain circumstances by the need to preserve a balanced allocation of taxing rights between the Member States and to prevent the risk of losses being used twice and to prevent tax avoidance. The question remaining was whether such rules complied with the principle of proportionality.

Proportionality: Two alternative scenarios

The Court observed that there were two alternatives. The first one concerned a situation where the intermediate subsidiary (or subsidiaries) between the parent company and the sub-subsidiary sustaining the losses were not established in the same Member State.

The Court indicated that, in such circumstances, the group could choose in which Member State the final losses are used. This might jeopardise the balanced allocation of taxing rights between the Member States and risk the double (or multiple) use of losses. Therefore, the Court held that it was not disproportionate for a Member State to insist on a direct link, even if the other conditions contained in paragraph 55 of the *Marks & Spencer* judgment were met.

The Court also pointed out that the Member State of the subsidiary, that directly owned the loss-making sub-subsidiary, could be the subject of a claim for cross-border loss relief for the losses of that sub-subsidiary.

The second alternative concerned the situation where the intermediate subsidiary (or subsidiaries) between the parent company and its loss-making sub-subsidiary were established in the same Member State.

The Court observed that this appears to have been the situation in *Holmen* because the intermediate subsidiary and the sub-subsidiary with the losses were both established in Spain.

The Court stressed that in such a case it would be disproportionate for a Member State to impose a requirement of a direct link between the parent company and the sub-subsidiary sustaining the cross-border losses.

Second Question

The second question (which was actually the third question asked by the Swedish referring court) concerned the significance of the fact that the subsidiary's State of establishment (Spain) did not permit the losses of one company to be transferred to another company liable for corporation tax in the year of liquidation, but allowed those losses to be carried forward to other accounting periods of the same company.

The Court stressed, in paragraphs 37-39 of *Holmen*, that –

> "in a situation such as those envisaged by Holmen, and even if all the other impossibilities mentioned in paragraph 55 of the judgment in *Marks & Spencer* have been met where applicable, the losses would not be characterised as final if there is a possibility of deducting those losses economically by transferring them to a third party before the completion of the liquidation ...
>
> it cannot be excluded from the outset that a third party may take into account for tax purposes the losses of the subsidiary in that subsidiary's State of establishment, for example following a sale of that subsidiary for a price including the tax advantage represented by the deductibility of losses for the future …
>
> unless Holmen can demonstrate that the possibility referred to in the previous paragraph is precluded, the mere fact that the subsidiary's State of establishment does not allow the transfer of losses in the year of liquidation cannot, in itself, be

> sufficient for the losses of the subsidiary or of the sub-subsidiary to be regarded as being final".

Third Question

Finally, the Court dealt with the third question (which was an amalgamation of questions two and four referred by the Swedish court). These concerned whether account had to be taken of the fact that the legislation of the State of establishment of the loss-making subsidiary resulted in part of the losses having to be carried forward because of a condition requiring losses to be set-off against profits of the same entity, or being impossible to set-off against the profits made by another company of the same group.

The Court recalled its answer to the previous question and indicated, in paragraphs 42 and 43 of *Holmen*, that –

> "the restrictions on the transfer of losses stemming from the legislation of the subsidiary's State of establishment are not decisive so long as the parent company has not adduced evidence that it is impossible for those losses to be used by a third party, in particular after a sale for a price including the tax value of the losses…
>
> If such evidence is adduced and the other conditions referred to in paragraph 55 of the judgment in *Marks & Spencer* have been met, the fiscal authorities are required to find that the losses of a non-resident subsidiary are final and that it is therefore disproportionate to not allow the parent company to take them into account at its level for tax purposes".

Finally, in paragraph 44 of *Holmen*, the Court explained that –

> "the extent to which the loss-making company was limited in its possibilities of carrying forward its losses or the extent to which other entities of the same group also located in the State of establishment of the loss-making subsidiary may have been limited in their possibility of having the subsidiary's losses transferred to them is irrelevant for the purposes of assessing the finality of the losses".

Analysis

The judgments of the Court in *Memira Holding* and *Holmen* demonstrate the difficulties in interpreting the judgment of the Court in *Marks & Spencer* in relation to "final losses" or perhaps, more appropriately, the "no-possibilities test" contained in paragraph 55 of *Marks & Spencer*. It is important to determine how the *Memira Holding* and *Holmen* judgments can be reconciled with the judgment of the Court in *Marks & Spencer* and other cases concerning cross-border losses.

There is also the issue of Swedish law in this case related to intra-group transfers, which raises the question concerning intra-group transfers in a final loss situation, and the Court's earlier judgment in the *Oy AA* case,[5] which concerned similar Finnish rules in a non-final loss situation. These intra-group transfer rules were discussed briefly in the Opinion of Advocate General Juliane Kokott in *Holmen*, but there was no significant analysis conducted on their relevance to this case and there was no discussion by the Court in the *Holmen* judgment.

In relation to *Memira Holding*, reconciling the Court's judgment with its earlier *A Oy case* [6] is worth further analysis, given that *A Oy* involved a merger between a parent company in one Member State with a loss-making subsidiary established in another Member State.

Reconciling *Memira Holding* and *Holmen* with *Marks & Spencer*

Interestingly, in the *Memira Holding* judgment, the only case cited by the Court other than *Marks & Spencer* is the *A Oy* case. The Court focused on delivering answers to the questions referred to it by the Swedish Supreme Administrative Court and simply referred to the "no possibilities test" contained in paragraph 55 of *Marks & Spencer*. Given that paragraph 55 expressly referred to a sale to a third party, the Court's emphasis on this issue was prevalent throughout the *Memira Holding* and *Holmen* judgments.

In *Memira Holding*, the Court highlighted, in paragraph 25, that –

> "even if all the other impossibilities referred to in paragraph 55 of the judgment in *Marks & Spencer* have been met, the losses would not be characterised as final if there is a possibility of deducting those losses economically by transferring them to a third party".

Accordingly, the Court concluded, in *Memira Holding*, (in line with paragraph 56 of *Marks & Spencer)*, that it was for Memira Holding to demonstrate that the losses at issue have not been transferred to a third party and that it was impossible to for it to deduct those losses. In such circumstances, the losses were "final losses" for the purposes of the "no possibilities test".

The Court confirmed this approach in *Holmen*, highlighting, in paragraphs 42 and 43, that –

> "the restrictions on the transfer of losses stemming from the legislation of the subsidiary's State of establishment are not decisive so long as the parent company has not adduced evidence that it is impossible for those losses to be

5 *Oy AA* C-231/05 ECLI:EU:C:2007:439.

6 *A Oy*, C-123/11, ECLI:EU:C:2013:84. For analysis by this author, see Tom O'Shea, *"Finnish Tax Rules on Cross-Border Mergers Challenged",* Tax Notes International, Sep. 23, 2013, 1209-1212.

> used by a third party, in particular after a sale for a price including the tax value of the losses…
>
> If such evidence is adduced and the other conditions referred to in paragraph 55 of the judgment in *Marks & Spencer* have been met, the fiscal authorities are required to find that the losses of a non-resident subsidiary are final and that it is therefore disproportionate to not allow the parent company to take them into account at its level for tax purposes".

In its response to the first question in *Holmen*, the Court also followed the reasoning it adopted in *Marks & Spencer*. This concerned a Swedish rule that made the application of group relief in relation to the losses of a non-resident subsidiary conditional on a direct link between the parent company and the loss-making, non-resident subsidiary. The Court noted that this could involve two different scenarios, the second being applicable in the case of *Holmen*.

In the first scenario, the subsidiary between the parent company and the loss-making sub-subsidiary could be established in a different Member State to the sub-subsidiary. Second, the subsidiary and the sub-subsidiary with the losses could be established in the same Member State.

In relation to the first scenario, the Court applied the reasoning it adopted in paragraphs 45-52 of *Marks & Spencer* and pointed out that a group, in such circumstances, could choose in which Member State to use the final losses – the Member State of the parent company or the Member State of the intermediate subsidiary. Consequently, the Court held that it was not disproportionate for a Member State to make cross-border group relief conditional on a direct link.

The Court also pointed out that a possible claim for group relief could be made by the intermediate subsidiary in its State of residence and paragraph 55 of *Marks and Spencer* would apply also in that environment.

In relation to the second scenario, the Court highlighted in paragraphs 31 and 32 of *Holmen*, that –

> "In those circumstances, the risks of optimisation of the group tax rate by choosing in which Member State the losses are set off and of the use of losses multiple times correspond to those noted by the Court in paragraphs 45 to 52 of the judgment in *Marks & Spencer*.
>
> It would therefore be disproportionate for a Member State to impose a requirement of direct ownership such as that at issue in the case in the main proceedings where the conditions in paragraph 55 of the judgment in *Marks & Spencer* have been met".

Summing-up

The *Memira Holding* and *Holmen* judgments are completely in line with the Court's judgment in *Marks & Spencer*.

A new clarification on what constitutes a final loss is found in *Holmen* in relation to an origin Member State rule which limits group relief to cross-border situations involving a direct link. The Court determined that such a rule was proportionate if the cross-border intermediate subsidiary was located in a different Member State to the sub-subsidiary that incurred the losses. However, if the subsidiary and the sub-subsidiary were established in the same Member State, then the origin Member State rule requiring a direct link was not proportionate if the other conditions contained in paragraph 55 of *Marks & Spencer* were met. This appears to be the actual situation in the *Holmen* case.

Interestingly, in the *Marks & Spencer* case, the losses in France, Germany, Spain and Belgium all involved indirect subsidiaries since the European group was held by the United Kingdom parent company via a Dutch holding company.[7]

Intra-group Financial Transfers

In Sweden, intra-group financial transfers are regulated by Chapters 35 and 35a of the 1999 Law on Income Tax ("inkomstskattelag 1999:1229").

Under Chapter 35, losses sustained by a subsidiary may be transferred directly or indirectly to its parent company for tax purposes. Point 6 of Advocate General Juliane Kokott's Opinion in *Holmen* indicates that intra-group transfers could be made to a direct or indirect loss-making subsidiary and, hence, the parent company could assign those losses to itself.

Chapter 35a makes group relief possible if the cross-border loss in the subsidiary was final and there was a direct link between the loss-making subsidiary established in an EU or EEA State and the Swedish parent company.

This scenario brings into play the Court's earlier *Oy AA* case,[8] that concerned similar Finnish intra-group financial transfer rules, but in a non-final loss environment. The question arising is whether, in a "final loss" situation, intra-group transfer rules should operate cross-border as well as domestically.

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7 See this link, paragraph 20, for the agreed statement of facts in the *Marks & Spencer* case - http://www.bailii.org/cgibin/format.cgi?doc=/ew/cases/EWHC/Ch/2003/1945.html&query=(Halsey) .

8 *Oy AA*, C-231/05, ECLI:EU:C:2007:439. For detailed analysis, see Tom O'Shea, "Finland's Intragroup Financial Transfer Rules Compatible with EU Law", Tax Notes International, Aug. 13, 2007, 634-638.

Oy AA

In *Oy AA*, a United Kingdom parent company held 100% of the shareholding in Oy AA, a Finnish company. In 2003, the parent company ran at a loss while Oy AA made a profit. Since the business of the parent company was important to Oy AA, it sought permission to make an intra-group financial transfer to its non-resident parent company. This was denied by the Finnish authorities. Subsequently, a preliminary ruling was sought from the CJEU as to whether the Finnish intra-group financial transfers' rules were compatible with the freedom of establishment. The Court held that the Finnish legislation was justified.

The Court noted, in paragraph 31 of *Oy AA*, that –

> "in relation to the possibility of deducting as expenses a transfer made in favour of the parent company, the legislation at issue in the main proceedings introduces a difference in treatment between subsidiaries established in Finland according to whether or not their parent company has its corporate seat in that same Member State".

This amounted to a restriction on the freedom of establishment unless some justification was shown.

The Court rejected the submission that the cross-border situation was not comparable to a purely domestic one, stressing, in paragraph 38, that –

> "in relation to the aim pursued by the Finnish system of intra-group financial transfers, the mere fact that parent companies which have their corporate establishment in another Member State are not subject to tax in Finland does not differentiate the subsidiaries of those parent companies from the subsidiaries of parent companies which have their establishment in Finland, and does not render the positions of those two categories of subsidiary incomparable".

Balanced allocation of taxing rights

In *Oy AA*, the need to preserve the balanced allocation of taxing rights was accepted by the Court as a possible justification, but the Court stressed, in paragraph 53, that –

> "that need cannot justify a Member State systematically refusing to grant a tax advantage to a resident subsidiary, on the ground that the income of the parent company, having its establishment in another Member State, is not capable of being taxed in the first Member State".[9]

9 This echoed paragraph 40 of *Marks & Spencer*, where the Court indicated that "the fact that it does not tax the profits of the non-resident subsidiaries of a parent company established on its territory does not in itself justify restricting group relief to losses incurred by resident companies".

The Court explained, in paragraph 56, that –

> "to accept that an intra-group cross-border transfer, such as that at issue in the main proceedings, may be deducted from the taxable income of the transferor would result in allowing groups of companies to choose freely the Member State in which the profits of the subsidiary are to be taxed … That would undermine the system of the allocation of the power to tax between Member States because, according to the choice made by the group of companies, the Member State of the subsidiary would be forced to renounce its right, in its capacity as the State of residence of that subsidiary, to tax the profits of that subsidiary in favour, possibly, of the Member State in which the parent company has its establishment".

Prevention of Tax Avoidance

In *Oy AA*, the Court also accepted that the need to prevent the risk of tax avoidance was an acceptable general interest justification. The Court noted, in paragraph 59, that –

> "By granting a subsidiary the right to deduct an intra-group financial transfer in favour of its parent company from its taxable income only in cases where the latter has its principal establishment in the same Member State, the Finnish system of intra-group financial transfers is able to prevent such practices, likely to be encouraged by the finding of significant disparities between the bases of assessment or rates of tax applied in the various Member States and designed only to avoid the tax normally due in the Member State of the subsidiary on its profits".

Principle of Proportionality

Lastly, the Court had to take into consideration the principle of proportionality. The Court noted that the two justifications put forward were linked. It explained, in paragraphs 62 - 64, that –

> "Conduct involving the creation of wholly artificial arrangements which do not reflect economic reality, with a view to escaping the tax normally due on the profits generated by activities carried out on national territory is such as to undermine the right of the Member States to exercise their tax jurisdiction in relation to those activities and jeopardise a balanced allocation between Member States of the power to impose taxes…
>
> Even if the legislation at issue … is not specifically designed to exclude from the tax advantage it confers purely artificial arrangements, devoid of economic reality, created with the aim of escaping the tax normally due on the profits generated by activities carried out on national territory, such legislation may

> nevertheless be regarded as proportionate to the objectives pursued, taken as a whole…
>
> In a situation in which the advantage in question consists in the possibility of making a transfer of income, thereby excluding such income from the taxable income of the transferor and including it in the taxable income of the transferee, any extension of that advantage to cross-border situations would … have the effect of allowing groups of companies to choose freely the Member State in which their profits will be taxed, to the detriment of the right of the Member State of the subsidiary to tax profits generated by activities carried out on its territory".

Consequently, the Court concluded that the Finnish rules at issue were a proportionate response to the general interest justifications that the Court accepted could be protected by Finland. However, the losses in *Oy AA* were not final losses as in *Holmen*.

Holmen

In relation to the *Holmen* case, the question is whether the Court's decision in *Oy AA* would be different if the cross-border losses were final in nature.

It is apparent that the proportionality determination in such a case would depend on whether the losses meet the no-possibilities test in paragraph 55 of *Marks & Spencer*. Clearly, if the losses are final in nature, the intra-group financial transfer rules should be extended cross-border because the group does not choose the Member State in which the profits are taxed.

If these rules apply only in domestic situations in Sweden, it is evident from the Court's case law that a restriction exists on the cross-border situation along the lines of the submissions in *Oy AA.* Moreover, this restriction could be justified, but in a final loss environment, would not meet the requirements of the principle of proportionality.

Moreover, the Chapter 35a group relief rules did not neutralise the problem caused by the Chapter 35 intra-group transfer rules. The Court's *Gielen* case[10] supports this conclusion. There, the Court highlighted, in paragraphs 49-54, that an optional relief regime was not sufficient to neutralise the restriction on the freedom of establishment that had been identified.

In the *Holmen* situation, the new Chapter 35a rules did not resolve the restriction contained in the Chapter 35 intra-group financial transfer rules.

10 *F. Gielen v Staatssecretaris van Financiën ("Gielen"),* C-440/08, ECLI:EU:C:2010:148. For a detailed analysis of the *Gielen* case, see Tom O'Shea, "Dutch Deduction Rules for Self-Employed Are Discriminatory, ECJ Says", 2010 WTD 60 – 5.

It will be interesting to see if this argument is advanced when the case returns to the Swedish courts.

Reconciling *Memira Holding* with *A Oy*

The Court's decision in *Memira Holding* echoes much of what the Court determined in *A Oy*.[11] Thus, in *Memira Holding*, the Court highlighted, in paragraphs 25 and 27, that -

> "even if all the other impossibilities referred to in paragraph 55 of the judgment in *Marks & Spencer* have been met, the losses would not be characterised as final if there is a possibility of deducting those losses economically by transferring them to a third party…
>
> it is for Memira to demonstrate that the possibility referred to in the previous paragraph is precluded, with the mere fact that the subsidiary's State of establishment does not allow the transfer of losses in the event of a merger cannot, in itself, be sufficient to regard the losses of the subsidiary as being final".

This simply confirms what the Court held in paragraph 49 of *A Oy* –

> "a restrictive measure such as that at issue in the main proceedings goes beyond what is necessary to attain the essential part of the objectives pursued in a situation in which the non-resident subsidiary has exhausted the possibilities available in its State of residence of having the losses taken into account … It is for the parent company to show that that is the case".

In *Memira Holding*, the Court held, in paragraph 31, that if the necessary evidence was adduced and the other conditions referred to in paragraph 55 of the judgment in *Marks & Spencer* were met,

> "the fiscal authorities are required to find that the losses of a non-resident subsidiary are final and that it is therefore disproportionate to not allow the parent company to take them into account at its level for tax purposes".

However, the situation in *A Oy* was not as clear-cut. Hence, the Court referred the matter back to the national court to check a number of matters.

First, the Finnish rules at issue appear to have excluded loss deduction domestically and also in cross-border in merger situations, where the operation was carried out for the sole purpose of obtaining a tax advantage. Thus, there was a possibility that, in such circumstances, there was no restriction in operation in the case. This was a matter for the national court to determine.

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11 *A Oy*, C-123/11, ECLI:EU:C:2013:84. For analysis of the *A Oy* case, see Tom O'Shea, "Finnish Tax Rules on Cross-Border Mergers Challenged", Tax Notes International, Sep. 23, 2013, 1209-1212.

Secondly, there was an argument in the *A Oy* case that even after the merger operation takes place between the Finnish parent company and the loss-making Swedish subsidiary, the losses were not final. For instance, the subsidiary's leases in Sweden could be assigned and the losses could be set of against any income from that assignment and any other liquidation income of the subsidiary. Again, this matter was referred back to the national court to determine whether A Oy has proved that its Swedish subsidiary has exhausted all the possibilities of taking account of the losses which existed in Sweden.

The Court concluded, in paragraph 55 of *A Oy*, that –

> "Were the referring court to reach the conclusion that such proof has been produced, it would be contrary to Articles 49 TFEU and 56 TFEU for A to be denied the possibility of deducting from its taxable profits in the Member State concerned the losses incurred by its non-resident subsidiary, in the context of the merger at issue in the main proceedings".

Thus, the *Memira Holding* and *A Oy* cases are completely in line with *Marks & Spencer*.

Some Critical Comments on Kokott's Opinions in *Holmen* and *Memira Holding*

The *Memira Holding* and *Holmen* cases demonstrate the significance of the judgment of the Grand Chamber in *Marks & Spencer*. Despite the numerous protestations of Advocate General Kokott, the Court has been steadfast in its application of the judgment, in particular paragraph 55, the "no-possibilities test".

Equal Treatment Principle

The Advocate General asks where does the concept of "final losses" come from? The Court supports the concept of "final losses" in situations where relief is granted to parent companies with loss-making subsidiaries in a domestic setting. In such circumstances, in a cross-border situation, where the freedom of establishment comes into play from an origin Member State perspective, the equal treatment principle (seen, for example in *de Groot*) [12] requires the origin Member State to ensure that one of its nationals, exercising a fundamental freedom, is treated no less favourably than another of its nationals operating a subsidiary domestically, unless there is an objective difference in situation between the cross-border and the domestic situation or unless some general interest of the origin Member State applies and the principle of proportionality is complied with. Thus, the problem of "final losses" springs from the rules of the origin Member State dealing with group losses (or intra-group financial transfers dealing with intra-group financial transfers in loss-making situations).

12 *F.W.L. de Groot v Staatssecretaris van Financiën ("de Groot"),* C-385/00, ECLI:EU:C:2002:750, para. 94.

In *Marks & Spencer,* the United Kingdom did not have to provide group relief for cross-border losses if it did not maintain such loss relief rules domestically.[13] However, if it operated such rules, then, it was obliged to comply with EU law. Failing to provide group relief for cross-border losses amounted to a restriction on the exercise of freedom of establishment. The Court accepted that this could be justified in most situations, but not if the conditions set-out in paragraph 55 of *Marks & Spencer* were met. In such instances, the balanced allocation of taxing rights was not put in jeopardy because the "final losses" could only be relieved in the origin Member State and not in the State of establishment; the final losses could not be used twice and there was no risk of loss tax-planning because they could only be used in the origin Member State. In such circumstances, the United Kingdom's rules constituted a restriction on the freedom of establishment that was not justified when the principle of proportionality was taken into account and the test set out in paragraph 55 of the *Marks & Spencer* case was satisfied.

The Court applies the same reasoning in *Memira Holding* and *Holmen*.

Comparability

In point 38 of her Opinion in *Holmen,* Kokott suggests that –

> "the criterion of comparability is vague. Given that all situations are comparable in some respect, if they are not identical … this test should in any case be abandoned".

The comparability in *Holmen* is pretty straight-forward! The Court compares the different tax treatment of two Swedish resident companies, one of which has exercised its freedom of establishment in another Member State.

In *Marks & Spencer*, the Court compared the different tax treatment of two United Kingdom parent companies, one of which set up a subsidiary in the United Kingdom that incurred losses, the other that set up subsidiaries in other Member States (via freedom of establishment) that incurred losses. In the former situation, loss relief was granted by the United Kingdom, in the latter situation, when freedom of establishment was exercised, the United Kingdom denied group relief. Thus, there was different treatment of the cross-border situation compared with the tax treatment of the purely domestic. This constituted a restriction on the freedom of establishment that needed to be justified.

The Court applies this "migrant/non-migrant test" in all its fundamental freedom cases from both an origin Member State perspective and from a host Member State perspective

13 Because there would be no restriction of the cross-border situation compared to a purely domestic one. For earlier analysis of the *Marks & Spencer* case, see Tom O'Shea, "Marks and Spencer v Halsey (HM Inspector of Taxes): Restriction, Justification and Proportionality", [2006] 15(2) EC Tax Review 66-82, and Tom O'Shea, *EU Tax Law and Double Tax Conventions,* (Avoir Fiscal, London, 2008).

when the national rule at issue treats the cross-border and the domestic situations differently. In "even-handed" rule situations, the national rule can treat the cross-border and the purely domestic situation in the same way, but these "even-handed" rules may still amount to a restriction on the exercise of a fundamental freedom.[14]

Discrimination: Comparable vs. Non-Comparable

Comparability also comes into play at the level of justification. If the cross-border situation is not comparable to a purely domestic situation, taking into account the purpose of the national rule at issue, then an origin Member State can treat one of its own nationals differently to a person exercising a fundamental freedom. This is because the Court's definition of discrimination, seen, for example, in paragraph 30 of *Schumacker*, states that –

> "discrimination can arise only through the application of different rules to comparable situations or the application of the same rule to different situations".

This means that situations that are non-comparable may be treated differently without constituting discrimination under EU law.

The Court has accepted that, generally speaking, residents and non-residents are non-comparable for tax purposes.[15] However, its case law demonstrates that from a host Member State perspective, a non-resident may be in a comparable situation to a resident. Hence, there is a comparability test at the level of justification because even though a national rule can be considered, in principle, a restriction, a Member State is entitled to

14 Two classic examples are - *Union royale belge des sociétés de football association ASBL v Jean-Marc Bosman, Royal club liégeois SA v Jean-Marc Bosman and others and Union des associations européennes de football (UEFA) v Jean-Marc Bosman ("Bosman"),* C-415/93, ECLI:EU:C:1995:463 and *CaixaBank France v Ministère de l'Économie, des Finances et de l'Industrie ("CaixaBank"),* C-442/02, ECLI:EU:C:2004:586. For an in-depth commentary on the Court's "migrant/non-migrant test" or, more appropriately, its equal treatment test, see Tom O'Shea, "European Tax Controversies: A British-Dutch Debate: Back to Basics and Is the ECJ Consistent?" (2013) WTJ, 101-127 at p119. For a more recent commentary, see Tom O'Shea, "A Critical Analysis of the CJEU Advocate General's Opinion In *Hornbach-Baumarkt",* Tax Notes International, 23 July 2018, 373-383.

15 For an explanation by the Court, see *Schumacker,* paras. 31 et seq.

treat situations that are non-comparable differently. Examples in the Court's case law include *Gschwind*, [16] *Truck Center* [17] and *Manninen*.[18]

Kokott's suggestion that the Court should abandon its comparability test was not accepted by the Court in the *Holmen* and *Memira Holding* judgments.

Notion of "Fair" Internal Market

In both *Holmen* and *Memira Holding,* Kokott reimagines the European internal market, as defined in the Treaty on the Functioning of the European Union (TFEU), as some magical "Fair Internal Market". In point 69 of her Opinion in *Holmen*, she argues –

> "A possibility of setting off final losses transnationally would, specifically in the particular situation at issue, favour above all large groups operating across borders as opposed to smaller undertakings (which do not generally operate across borders). For example, if Holmen knows that all losses incurred from the Spanish business model can ultimately be set off against the profits in Sweden, then, in attempting to position itself in the Spanish market, Holmen can compete very differently from a Spanish competitor that has to assume that its losses will be forfeited if it ceases its commercial activity in Spain. For Holmen the 'Spanish losses' would be a much lesser burden than for a domestic competitor without a similar group structure".[19]

Of course, the Court paid no attention to this submission!

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16 *Frans Gschwind v Finanzamt Aachen-Außenstadt ("Gschwind"),* C-391/97, ECLI:EU:C:1999:409. The Gschwind judgment may be contrasted with *Schumacker*. In *Schumacker*, the Court found comparability in a host Member State environment between a resident and a non-resident. In *Gschwind,* the Court determined that the cross-border and the domestic situations were non-comparable.

17 *Belgian State - SPF Finances v Truck Center SA ("Truck Center"),* C-282/07, ECLI:EU:C:2008:762, para. 41. See Tom O'Shea, "*Truck Center*: A Lesson in Source vs. Residence Obligations in the EU", Tax Notes International, Feb. 16, 2009, 593-601.

18 *Petri Manninen ("Manninen"),* C-319/02, ECLI:EU:C:2004:484. Although, the Court determined that comparability existed in this case, it highlighted in paragraph 34 that comparability would not exist if "the tax legislation of the Member State in which the investments were made already eliminated the risk of double taxation of company profits distributed in the form of dividends, by, for example, subjecting to corporation tax only such profits by the company concerned as were not distributed". In such circumstances, a Finnish resident that invested in Swedish company would not be in a comparable situation to a Swedish resident who invested in a Finnish company from the perspective of a national rule that was designed to eliminate economic double taxation".

19 The Advocate General makes the same assertion in point 76 of her Opinion in *Memira Holding.*

Scope of the Freedom of Establishment

The freedom of establishment is open to big companies and small companies without distinction as long as they are incorporated in an EU Member State and have their registered office, central administration or principal place of business within the EU (see Article 54 TFEU).

Kokott fails to understand that it is this freedom which is at play in the cross-border loss cases.

The freedom of establishment intersects with national rules of the origin Member State that grant loss relief to domestic groups but fail to grant similar loss-relief in cross-border situations. Thus, in *Marks & Spencer,* as highlighted above, the comparator involved two origin State parent companies, one of which exercised freedom of establishment and created a subsidiary in another Member State, that incurred losses; the other that created a subsidiary in the origin Member State which incurred losses in that State.

The freedom of establishment, from an origin Member State perspective, is not concerned with "fair" competition in a host Member State. The comparator, as suggested by Kokott, does not concern a large company competing in the host Member State with a small company established in that host Member State, where both incur losses and only the big company can receive loss relief for "final losses".

The rule at issue in *Marks & Spencer*, *Holmen* and *Memira Holding* is an origin Member State rule which denies loss relief for cross-border losses. The Court's response is simple: these losses must be relieved in the host Member State, but if they are not and they are "final losses", then they should be relieved in the origin Member State because it is disproportionate for that origin Member State to grant group relief in domestic situations and not extend that relief to cover "final loss" situations, involving an exercise of the freedom of establishment, that occur in other Member States, where the "no-possibilities test", contained in paragraph 55 of *Marks & Spencer* is met.

Moreover, even if Kokott's submission warranted consideration, it is important to compare like with like – thus, a Swedish company with a loss-making subsidiary in Spain (with final losses there) should be compared with a Spanish company with a loss-making subsidiary in Spain. Both of these groups compete in Spain on the same basis. Small Spanish companies have to compete with big Spanish companies that operate via a subsidiary in Spain. Hence, Kokott's comparison is flawed and unhelpful to the Court and demonstrates a complete misunderstanding of the Court's direct tax case law.

Finally, as noted above, the main principle operating in the EU's internal market is the principle of equal treatment. From an origin Member State perspective, this involves comparing the tax treatment of two origin Member State nationals, one of which has exercised a fundamental freedom. From a host Member State perspective, generally, speaking,[20] the comparison involves the tax treatment of a host Member State national with a national from another Member State that has exercised a fundamental freedom in that host Member State.

Getting these comparators right is the key to understanding the direct tax jurisprudence of the CJEU.

20 "Generally, speaking", because the comparator usually involves a foreigner and a local in the host Member State. However, this is not always the case according to the Court's decided cases. Sometimes, the comparator can involve two host State nationals, where one of them has exercised a fundamental freedom in another Member State and is now returning to his origin Member State. See, for example, *The Queen v Immigration Appeal Tribunal and Surinder Singh, ex parte Secretary of State for Home Department ("Singh"),* C-370/90, ECLI:EU:C:1992:296. The comparator could also involve two foreigners, exercising free movement of worker rights in the host Member State. See, for example, *C.G. Sopora v Staatssecretaris van Financiën ("Sopora"),* C-512/13, ECLI:EU:C:2015:108.