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Advocate General's Opinion on Danish rules on cross-border loss relief

Denmark - Cross-Border Loss Relief – Final Losses – 'Marks & Spencer Exception' - Freedom of establishment - International Group Relief Regime

On January 17, 2018, Advocate General (AG) Campos of the Court of Justice of the European Union (CJEU) issued his Opinion in the Bevola and Jens W. Trock case (C-650/16) concerning the compatibility with EU law of the Danish rules on the deductibility of losses from foreign permanent establishments (PE), in cases where (1) the taxpayer did not elect to apply for the Danish international joint taxation regime and (2) the 'Marks & Spencer exception" applies (i.e. losses are considered final). The AG concluded that the Danish legislation is contrary to the freedom of establishment.

Background

In 2009, A/S Bevola, a Danish company, sought to deduct from its taxable base in Denmark the losses incurred at the level of its PE in Finland, arguing that the PE had ceased to exist during the same year and therefore loss relief could not be claimed in Finland. The Danish tax authorities denied the deduction on the grounds that revenue or expenses attributable to a foreign PE cannot be taken into account in a taxpayer's taxable base, unless the latter has opted for the Danish international joint taxation regime. Under this regime, a Danish company has to integrate the benefits and losses of all its branches and PEs for a period of at least 10 years, regardless of their residence.

Bevola appealed the tax authorities' decision before the Danish Eastern Regional Court, which decided to refer the case to the CJEU on December 19, 2016. In particular, the CJEU was asked whether, in circumstances equivalent to those in the CJEU decision in the Marks & Spencer case (C-446/03), Danish rules on cross-border loss relief are compatible with the freedom of establishment. Under these rules, deductions for losses in foreign PEs are not allowed, unless the group elected to apply international joint taxation. However, it is possible to deduct losses incurred by domestic branches, with or without the joint taxation scheme.

The AG's Opinion

Assuming that the facts of the case at hand are the same as those in the CJEU decision in the Marks & Spencer case (C-446/03) the AG focused on two issues:

- Are the situations between a non-resident subsidiary and a non-resident PE, and between a resident and a non-resident PE objectively comparable? and
- Is the possibility for taxpayers to opt into the Danish international joint taxation regime sufficient to prevent the Danish legislation being incompatible with EU law?

The AG first underlined that the resolution reached by the CJEU in the Marks & Spencer case, i.e. that final losses should be taken into account at least somewhere, ensures that the balance is preserved between the tax burden supported by a taxpayer incurring losses and its actual contributing capacity. In this respect, the AG concluded that in view of the principle of the taxpaying capacity, a resident and a non-resident PE with final losses are in a comparable situation. In addition, the AG observed that, in accordance with the CJEU decision in the Lidl Belgium case (C-414/06), the tax treatment of non-resident subsidiaries and PEs must be the same, if the incurred losses are final and the PE was not able to deduct them in its State of residence.

Briefly mentioning that a difference in treatment such as the one at issue leads, in principle, to a restriction of the freedom of establishment, the AG went on to analyze the effects of the Danish international group relief regime on the application of the 'Marks & Spencer exception'. The AG noted that although this regime is optional, it is disproportionately restrictive as regards it scope (i.e. all subsidiaries and all PEs have to be integrated) and its minimum application period (i.e. 10 years), making it in practice almost impossible for groups of companies operating globally to opt-in.

The AG thus concluded that the Danish legislation is not compatible with the freedom of establishment, as it prevents a Danish company from deducting, in accordance with the 'Marks & Spencer exception', final losses incurred by its PE in Finland.

EU Tax Centre comment

The AG's Opinion provides some clarity on the interpretation of the the 'Marks & Spencer exception' and in particular to what extent national measures restricting the deductibility of cross-border losses can be considered proportionate as regards the preservation of the balanced allocation of powers to tax. It remains to be seen whether the CJEU will follow the argumentation of the AG in this respect or provide additional insight on what should be considered as final losses.

Should you have any queries, please do not hesitate to contact KPMG's EU Tax Centre, or, as appropriate, your local KPMG tax advisor.

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