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Advocate General's Opinion in the NN case on Danish rules concerning loss relief

Denmark - Freedom of Establishment – Loss Relief – Permanent Establishment - "Philips Electronics" Judgment - BEPS – Anti-Tax Avoidance Directive - Proportionality

On February 21, 2018, Advocate General (AG) Campos of the Court of Justice of the European Union (CJEU) issued his Opinion in the NN A/S case (C-28/17) concerning the compatibility with EU law of the Danish rules on the deductibility of losses from a Danish permanent establishment (PE) whose head office is not tax resident in Denmark. The AG concluded that the Danish legislation constitutes a restriction to the freedom of establishment, but that such restriction may be justified by the prevention of double deduction of losses.

Background

NN A/S, a Danish resident company, had a subsidiary in Sweden which was the head office of a PE in Denmark. In 2008, NN A/S sought to offset the tax losses of the Danish PE against its profits. The tax authorities rejected the request arguing that losses incurred by the Danish PE of a non-resident company can only be offset against the profits of a Danish tax group to the extent that these losses cannot be used in the jurisdiction of the PE's head office. On the contrary, in a purely domestic situation, the possibility to offset the losses of a PE against the group's profits is not subject to any conditions.

NN A/S appealed the decision, considering that based on the CJEU decision in the Philips Electronics case (C- 18/11) this difference in treatment constitutes a restriction to the freedom of establishment that cannot be justified. In this context, the Danish Court of Appeal requested the CJEU to clarify whether its decision in the Philips Electronics case is applicable in the case at hand and to analyze the compatibility of the Danish rules with the freedom of establishment.

The AG's Opinion

Applying the conclusions reached by the CJEU in the Philips Electronics case to the situation at hand, the AG first considered that the situation of a non-resident company with a Danish PE and that of a Danish company are objectively comparable, also having regard to the objective of the Danish legislation to prevent the double use of losses. He further observed that there is a difference in treatment constitutive of a restriction to the freedom of establishment, as Danish groups with foreign subsidiaries are treated less favorably than Danish groups with only domestic companies.

The AG then turned to analyzing whether such restriction may be justified by overriding reasons in the public interest. Referring again to the CJEU decision in the Philips Electronic case, he first observed that the objective of preventing the double use of losses should in principle not be relied on, as the fact that the losses could be used both in Denmark and in Sweden does not affect Denmark's power to tax. However, the AG further noted that the recent efforts made by the European Union to prevent Base Erosion Profit Shifting (BEPS) and the adoption of anti-hybrid rules in the recent Anti-Tax Avoidance Directive (2016/1164/EU) could justify a change in the CJEU's approach. In light of those initiatives, the AG concluded that the objective to prevent the double deduction of losses should be considered as an appropriate justification, independent from the prevention of tax fraud.

As a consequence, the restriction may be justified, as regards the Danish legislation's objective to prevent the same losses from being offset in two different states. However, such restriction may not go beyond what is necessary to attain the objective pursued. In this respect, the AG considered that the interpretation given by the Danish administration to the applicable provisions may lead to a disproportionate situation of double non-deduction, in particular if the actual circumstances of the taxpayer are not taken into account. In the case at hand, the AG left it to the referring court to assess whether the losses incurred by the Danish PE can or cannot be offset in Sweden.

The AG thus concluded that the Danish legislation is a restriction of the freedom of establishment, but that such restriction may be justified by the prevention of double deduction of losses. He further left it to the national court to assess whether the application of such legislation is proportionate in the case at hand.

EU Tax Centre comment

The case is very similar to the Philips Electronics case; however, the AG brings a new interpretation in light of the recent anti-BEPS measures that Member States have committed to at both OECD and EU level, by introducing the justification of prevention of double deduction (double use of losses) as an autonomous justification, independent from the prevention of tax fraud. According to the AG, although it is too soon to refer to the provisions of the Anti-Tax Avoidance Directive, the case should nevertheless be decided upon in the light of those initiatives, including as regards the prevention of hybrid PE mismatches. Nevertheless, it remains to be seen whether the CJEU will follow the AG's opinion.

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

Robert van der Jagt
Chairman, KPMG's EU Tax Centre and
Partner,
Meijburg & Co

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