JUDGMENT OF THE COURT (Grand Chamber)

3 February 2015 (*)

(Failure of a Member State to fulfil obligations — Article 49 TFEU — Article 31 of the EEA Agreement — Corporation tax — Groups of companies — Group relief — Transfer of losses sustained by a non-resident subsidiary — Conditions — Date to be used for determining whether the losses of the non-resident subsidiary are definitive)

In Case C?172/13,

ACTION under Article 258 TFEU for failure to fulfil obligations, brought on 5 April 2013,

European Commission, represented by W. Roels and R. Lyal, acting as Agents,

applicant,

v

United Kingdom of Great Britain and Northern Ireland, represented by V. Kaye, S. Brighouse and A. Robinson, acting as Agents, assisted by D. Ewart QC and S. Ford, Barrister,

defendant,

supported by:

Federal Republic of Germany, represented by T. Henze and K. Petersen, acting as Agents,

Kingdom of Spain, represented by A. Rubio González and A. Gavela Llopis, acting as Agents,

Kingdom of the Netherlands, represented by M.K. Bulterman and J. Langer, acting as Agents,

Republic of Finland, represented by S. Hartikainen, acting as Agent,

interveners,

THE COURT (Grand Chamber),

composed of V. Skouris, President, K. Lenaerts (Rapporteur), Vice-President, M. Ileši?, L. Bay Larsen and J.-C. Bonichot, Presidents of Chambers, A. Rosas, E. Juhász, A. Arabadjiev, C. Toader, M. Safjan, D. Šváby, M. Berger and A. Prechal, Judges,

Advocate General: J. Kokott,

Registrar: L. Hewlett, Principal Administrator,

having regard to the written procedure and further to the hearing on 15 July 2014,

after hearing the Opinion of the Advocate General at the sitting on 23 October 2014,

gives the following

Judgment

1 By its application, the European Commission claims that the Court should declare that, by imposing conditions on group relief for losses sustained by non-resident companies ('cross-border group relief') which make it virtually impossible in practice to obtain such relief and by restricting such relief to periods after 1 April 2006, the United Kingdom of Great Britain and Northern Ireland has failed to fulfil its obligations under Article 49 TFEU and Article 31 of the Agreement on the European Economic Area of 2 May 1992 (OJ 1994, L 1, p. 3; 'the EEA Agreement').

UK legal context

2 In the United Kingdom, the rules on group relief allow the companies in a group to offset their profits and losses among themselves. However, the rules introduced by the Income and Corporation Tax Act 1988 ('the ICTA') did not permit losses sustained by non-resident companies to be taken into account.

3 Following the judgment in *Marks & Spencer* (C?446/03, EU:C:2005:763), the ICTA was amended by provisions of the Finance Act 2006 which came into force on 1 April 2006 for the purposes of allowing cross-border group relief, subject to certain conditions. Subsequently, those provisions were reproduced in broadly the same terms in the Corporation Tax Act 2010 ('the CTA 2010').

4 The CTA 2010 sets out the conditions for cross-border group relief. Under Section 118 of the CTA 2010, a non-resident company must have exhausted all possibility of having the losses taken into account in the accounting period in which the losses were incurred or in previous accounting periods, while, under Section 119(1) to (3) of the CTA 2010, there must be no possibility of the losses being taken into account in future accounting periods.

5 Under Section 119(4) of the CTA 2010, the determination as to whether losses may be taken into account in future accounting periods must be made 'as at the time immediately after the end' of the accounting period in which the losses were sustained.

6 Under Paragraphs 14(1)(a) and 74(1)(a) of Schedule 18 of the Finance Act 1998, a general time-limit applies to group relief claims, in accordance with which they must be made within two years of the end of the accounting period in which the losses were sustained.

7 The Supreme Court of the United Kingdom concluded in paragraph 33 of its judgment of 22 May 2013 that, for cross-border group relief to be granted, the question for inquiry, regard being had to the legislation in force before 1 April 2006, interpreted in the light of EU law, is whether the claimant company has been able to show, on the basis of the circumstances known at the date when it makes its claim, that there has been no possibility of the losses in question being utilised in the Member State of the surrendering company in any accounting period prior to the date of the claim, and no possibility of such utilisation in the accounting period in which the claim is made or in any future accounting periods.

Pre-litigation procedure and proceedings before the Court

8 On 19 July 2007, the Commission sent a letter of formal notice to the United Kingdom drawing its attention to the possibility that the tax rules adopted by that Member State in the wake of the judgment in *Marks & Spencer* (EU:C:2005:763) are incompatible with the freedom of establishment to the extent that they are based on a particularly restrictive interpretation of the condition relating to the exhaustion of all possibility of the non-resident subsidiary's losses being

taken into account in the Member State where that subsidiary is resident. In addition, according to the Commission, those rules apply only from the date on which the new legislation entered into force, that is to say, from 1 April 2006.

9 By email of 23 October 2007, the United Kingdom asserted that its legislation on cross-border group relief is consistent with the principles laid down by the Court in the judgment in *Marks & Spencer* (EU:C:2005:763).

10 On 23 September 2008, the Commission sent the United Kingdom a reasoned opinion restating its position. The United Kingdom reaffirmed its own position by letter of 18 November 2008.

11 On 25 November 2010, the Commission sent the United Kingdom a supplementary reasoned opinion following the adoption of the CTA 2010.

12 Unconvinced by the line of argument put forward by the United Kingdom in its letter of 24 January 2011 in response to the reasoned opinion, the Commission brought the present action.

13 By decision of the President of the Court of 11 October 2013, the Federal Republic of Germany, the Kingdom of Spain, the Kingdom of the Netherlands and the Republic of Finland were granted leave to intervene in the proceedings in support of the form of order sought by the United Kingdom.

The action

First complaint: infringement of Article 49 TFEU and Article 31 of the EEA Agreement, in that Section 119(4) of the CTA 2010 makes it virtually impossible for a resident parent company to obtain cross-border group relief

Arguments of the parties

14 The Commission submits that Section 119(4) of the CTA 2010 does not meet the requirements entailed for the Member State concerned by paragraphs 55 and 56 of the judgment in *Marks & Spencer* (EU:C:2005:763) in so far as, under that provision, the determination that it is impossible for losses sustained by a subsidiary established in another Member State, or in a non-member State party to the EEA Agreement, to be taken into account in the future must be made 'as at the time immediately after the end' of the accounting period in which the losses were sustained. According to the Commission, that provision has the effect of making it virtually impossible for a resident parent company to obtain cross-border group relief.

15 This is because, as a result of Section 119(4) of the CTA 2010, cross-border group relief may be granted in only two situations: first, 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, secondly, where the non-resident subsidiary enters liquidation before the end of the tax year in which the losses are sustained. Cross-border group relief is thus precluded in the normal commercial situation, that is to say, where, following the end of a tax year in which losses have been suffered, the decision is taken to cease trading and subsequently to place the non-resident subsidiary in liquidation. Furthermore, that relief is limited to losses sustained in a single tax period.

16 The Commission argues that, in order to ensure compliance with the conditions laid down by the Court in paragraph 55 of the judgment in *Marks & Spencer* (EU:C:2005:763), the possibility of obtaining tax relief in the State of residence must be assessed at the time when the claim for group relief is made in the United Kingdom. Moreover, it must be assessed 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) which exists only because the foreign subsidiary has not yet been placed in liquidation.

17 According to the United Kingdom, it is clear from paragraph 55 of the judgment in *Marks & Spencer* (EU:C:2005:763) that, as regards the condition that there must be no possibility of the losses of the non-resident subsidiary being taken into account in its State of residence for future periods, the related assessment must be made at the end of the accounting period in which the losses arose.

18 As for the assertion that it is virtually impossible to obtain cross-border group relief under the UK legislation at issue, the United Kingdom contends that a company will normally have the possibility of carrying losses forward to a subsequent tax period in circumstances in which it continues to trade. In addition, the condition laid down in Section 119(4) of the CTA 2010 is capable of being satisfied in circumstances wider than those set out by the Commission. The relevant provisions do not make cross-border relief conditional upon the non-resident subsidiary having been put into liquidation before the end of the accounting period in which the losses were sustained. Evidence 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. The intention to wind up the subsidiary is taken into account, along with all other relevant facts as at the end of the accounting period in which the losses were sustained, in determining whether the above condition is satisfied, that is to say, in checking that there is no possibility of the losses being taken into account.

19 The intervening parties submit that the United Kingdom is not under any obligation to allow losses sustained by non-resident subsidiaries to be taken into account in all cases in which those losses may not be taken into account elsewhere. Furthermore, it is argued, it would not be disproportionate to treat liquidation of the non-resident subsidiary as being *de facto* a condition for loss relief.

20 The Federal Republic of Germany adds that the case-law devolving from the judgment in *Marks & Spencer* (EU:C:2005:763) must be re-examined following the judgment in *K* (C?322/11, EU:C:2013:716).

Findings of the Court

21 The CTA 2010 establishes group relief arrangements under which losses sustained by a company may be offset against the profits of other companies belonging to the same group. Unlike losses sustained by resident companies, those sustained by non-resident companies may be taken into account for the purposes of group relief only if the conditions laid down in Sections 118 and 119 of the CTA 2010 are met.

22 Group relief under the CTA 2010 constitutes a tax advantage for the companies concerned. 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, that system confers a cash-flow advantage on the group (see judgments in *Marks & Spencer* EU:C:2005:763, paragraph 32, and *Felixstowe Dock and Railway Company and Others*, C?80/12, EU:C:2014:200, paragraph 19).

23 The difference in treatment, found in paragraph 21 above in relation to the granting of the tax advantage in question, between losses sustained by resident subsidiaries and those of non-resident subsidiaries is of such a kind as to hinder the exercise by the group parent company of its freedom of establishment for the purposes of Article 49 TFEU by deterring it from setting up subsidiaries in other Member States (see, to that effect, judgments in *Marks & Spencer*, EU:C:2005:763, paragraph 33; *Felixstowe Dock and Railway Company and Others*,

EU:C:2014:200, paragraph 21; and *Nordea Bank Danmark*, C?48/13, EU:C:2014:2087, paragraph 22).

24 However, according to the case-law of the Court, such a difference in treatment may be justified by three overriding reasons in the public interest, taken together, that is to say, by the need to preserve the balanced allocation of powers of taxation between the Member States, the need to prevent the double use of losses and the need to combat tax avoidance (see, to that effect, judgments in *Marks & Spencer*, EU:C:2005:763, paragraph 51; *Oy AA*, C?231/05, EU:C:2007:439, paragraph 51; and *A*, C?123/11, EU:C:2013:84, paragraph 46).

25 It remains to be considered whether the conditions laid down by the CTA 2010 for cross-border relief are consistent with the principle of proportionality in that, whilst being appropriate for achieving the objectives mentioned in the preceding paragraph, they do not go beyond what is necessary to achieve them.

26 In that regard, it should be borne in mind that, in paragraph 55 of the judgment in *Marks & Spencer* (EU:C:2005:763), which concerned the ICTA, under which the possibility of losses sustained by non-resident subsidiaries being taken into account for the purposes of group relief was wholly precluded, the Court held that the difference in treatment between the losses sustained by a resident subsidiary and those sustained by a non-resident subsidiary goes beyond what is necessary to attain the objectives pursued in a situation where, first, 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, if necessary by transferring those losses to a third party or by offsetting the losses against the profits made by the subsidiary in previous periods, and, secondly, there is no possibility for the foreign subsidiary's 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 (see also judgments in *Lidl Belgium*, C?414/06, EU:C:2008:278, paragraph 47, and *A*, EU:C:2013:84, paragraph 49).

27 According to paragraph 56 of the judgment in *Marks & Spencer* (EU:C:2005:763), where, in one Member State, the resident parent company demonstrates to the tax authorities that a non-resident subsidiary has sustained definitive losses, as described in paragraph 55 of that judgment, it is contrary to Articles 49 TFEU to preclude the possibility for the parent company to deduct from its taxable profits in that Member State the losses incurred by its non-resident subsidiary.

28 It should be noted, however, that Sections 118 and 119(1) to (3) of the CTA 2010 allow losses sustained by a non-resident subsidiary to be taken into account by the resident parent company in the situations contemplated in paragraph 55 of the judgment in *Marks & Spencer* (EU:C:2005:763).

29 Furthermore, the Commission itself acknowledges in its application that, in principle, the CTA 2010 allows the resident parent company to take into account definitive losses, as described in paragraph 55 of the judgment in *Marks & Spencer* (EU:C:2005:763), sustained by a non-resident subsidiary.

30 However, according to the Commission, Section 119(4) of the CTA 2010 is contrary to Article 49 TFEU because it makes it virtually impossible in practice for a resident parent company to obtain cross-border group relief.

31 In that regard, it should be noted that Section 119(4) of the CTA 2010 sets the date by reference to which it must be decided whether losses sustained by a non-resident subsidiary are definitive, as described in paragraph 55 of the judgment in *Marks & Spencer* (EU:C:2005:763).

Under that provision, that assessment is to be made ‘as at the time immediately after the end’ of the accounting period in which the losses were sustained.

32 According to the Commission, that requirement makes it virtually impossible for group relief to be obtained for losses sustained by a non-resident subsidiary, since in practice it allows the resident parent company to take such losses into account in only two situations: (i) where the legislation of the Member State of residence of the subsidiary concerned makes no provision for losses to be carried forward and (ii) where the subsidiary is put into liquidation before the end of the accounting period in which the loss was sustained.

33 It should be noted, however, that the first of those situations referred to by the Commission is irrelevant for the purposes of assessing the proportionality of Section 119(4) of the CTA 2010. It is settled law that 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 (see judgment in *K*, EU:C:2013:716, paragraphs 75 to 79 and the case-law cited). In such a situation, the Member State in which the parent company is resident may not allow cross-border group relief without thereby infringing Article 49 TFEU.

34 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.

35 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.

36 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 (see judgment in *A*, EU:C:2013:84, paragraphs 53 and 54).

37 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.

38 In those circumstances, the first complaint must be rejected in so far as it is based on the alleged infringement of Article 49 TFEU.

39 With regard to the assertion that Section 119(4) of the CTA 2010 entails an infringement of Article 31 of the EEA Agreement, another contention raised by the Commission, it should be noted that, in so far as the provisions of Article 31 of the EEA Agreement have the same legal scope as

those of Article 49 TFEU, which are substantively identical, all the foregoing considerations may, in circumstances such as those of the present case, be transposed *mutatis mutandis* to Article 31 of the EEA Agreement (see, to that effect, judgment in *Commission* v *Finland*, C?342/10, EU:C:2012:688, paragraph 53 and the case-law cited).

40 Accordingly, the present complaint must be rejected in its entirety.

Second complaint: infringement of Article 49 TFEU and Article 31 of the EEA Agreement, in that the UK legislation precludes cross-border group relief for losses sustained before 1 April 2006

41 The Commission submits that losses sustained before 1 April 2006 are excluded from cross-border group relief, contrary to Article 49 TFEU and Article 31 of the EEA Agreement, inasmuch as the provisions laid down in the CTA 2010 concerning that relief apply only to losses sustained after 1 April 2006, the date on which the Finance Act 2006 entered into force.

42 In response to the Commission’s argument, the United Kingdom contends that cross-border group relief is also available for periods before 1 April 2006, but that it is governed by the legislation applicable to those earlier periods, construed in accordance with EU law following the judgment in *Marks & Spencer* (EU:C:2005:763), as was the intention of the Supreme Court of the United Kingdom in its judgment of 22 May 2013, referred to in paragraph 7 above.

43 Irrespective of whether or not the reference to the interpretation by the Supreme Court of the United Kingdom of the national legislation in force before 1 April 2006, according to which losses sustained before that date are not excluded from cross-border group relief, satisfies the need for legal certainty as regards the possibility of obtaining cross-border group relief for losses sustained before that date, it must be found 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.

44 In those circumstances, the second complaint must be rejected.

45 It follows that the action must be dismissed in its entirety.

Costs

46 Under Article 138(1) of the Rules of Procedure of the Court of Justice, the unsuccessful party must be ordered to pay the costs if they have been applied for in the other party’s pleadings. Since the United Kingdom has applied for costs and the Commission has been unsuccessful, the latter must be ordered to pay the costs.

47 Pursuant to Article 140(1) of the Rules of Procedure, the Federal Republic of Germany, the Kingdom of Spain, the Kingdom of the Netherlands and the Republic of Finland must bear their own costs.

On those grounds, the Court (Grand Chamber) hereby:

1. **Dismisses the action;**

2. **Orders the European Commission to pay the costs;**

3. **Orders the Federal Republic of Germany, the Kingdom of Spain, the Kingdom of the Netherlands and the Republic of Finland to bear their own costs.**

[Signatures]

* Language of the case: English.