Aalto University
School of Business

THE FINNISH IMPLEMENTATION OF THE FINAL LOSSES DOCTRINE AS DEVELOPED IN EU CASE-LAW

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ABSTRACT

The issue of this thesis boils down to the EU and a more harmonized internal market. The EU aims towards a more borderless internal market, which also means that fiscal barriers need to be torn down, within the limits of the law. This thesis examines when the cross-border deduction of losses is to be allowed by a Member State, being in exceptional cases when a subsidiary's losses are final, as defined by CJEU case-law (*Marks & Spencer II* onwards until *Memira Holding* and *Holmen AB*). CJEU case-law has evolved and the definition of final losses have been clarified by various case-law, and the doctrine has been extended to cover cross-border mergers, group contribution, foreign branches and subsidiaries resident within the EEA.

As EU case-law is applicable also in Finland, Finland have had to implement the final losses doctrine in national law as well. Finnish case-law has evolved since the *Marks & Spencer II* case but yet it seems close to impossible to demonstrate the existence of final losses in Finland. This was confirmed by the five Supreme Administrative Court's cases issued in May 2020, where the court found, in all five cases, that the Finnish parent company, being the applicants, had not successfully demonstrated that the subsidiaries losses are in fact final, despite the finality of the losses being accepted in all instances before the Supreme Administrative Court.

Finland implemented a new law, the Act on Group Deduction, applicable as of 2021, whereby a Finnish parent company may deduct its foreign subsidiary's final losses in Finland for the parent company's Finnish tax purposes. However, in light of the five aforementioned Supreme Administrative Court's cases, the question arises whether it currently is possible to demonstrate the finality of a foreign subsidiary's losses. In the Government proposal for the Act on Group Contribution, the final losses concept is to be the definition as set out in CJEU case-law. Interestingly enough, other EU Member States have been successful in allowing its nationals to deduct its foreign subsidiary's final losses for the parent company's tax purposes, but in Finland this seems to yet be unsolved.

The question also arises whether Finland is yet in breach of EU law when setting the burden of proof impossibly high. This standpoint could be argued in light of the CJEU case *San Giorgio*. Another route could be to make a formal complaint to the European Commission arguing that Finland is in breach of EU law (and hence the principles in *San Giorgio*) when setting the burden of proof for final losses unreasonably high.

Keywords final losses, Marks & Spencer, Memira Holding, cross-border merger, group deduction

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ABSTRAKT (SVENSKA)

Kärnfrågan i denna avhandling handlar om EU och en mer harmoniserad inre marknad. EU siktar mot en mer gränslös inre marknad vilket också betyder att de fiskala gränserna måste rivas ner inom ramarna för lagen. Denna avhandling undersöker när gränsöverskridande förlustavdrag är tillåtna av ett medlemsland. Dessa är enligt EU-domstolens rättspraxis tillåtna endast i exceptionella fall när ett dotterbolags förluster är slutgiltiga (från och med *Marks & Spencer II* fram tills *Memira Holding* och *Holmen AB*). EU-domstolens rättspraxis har utvecklats och definitionen av slutgiltiga förluster har tydliggjorts genom diverse rättsfall och doktrinen har utsträckt sig att omfatta gränsöverskridande fusioner, koncernbidrag, utländska bolag med hemvist inom EES. Eftersom EU:s rättspraxis också är tillämplig i Finland så har Finland varit tvungen att också implementera doktrinen om slutgiltiga förluster i sin nationella lagstiftning. Finska rättspraxisen har utvecklats sedan *Marks & Spencer II* fallet, men ännu verkar det vara nära omöjligt att bevisa existensen av slutgiltiga förluster i Finland. Detta bekräftades genom fem fall utgivna av Högsta förvaltningsdomstolen i Maj 2020 där käranden i alla fallen var finska moderbolag. Domstolen ansåg i alla de fem fallen att käranden inte hade framgångsrikt lyckats bevisa att dotterbolagens förluster var slutgiltiga, trots att slutgiltigheten hade godtagits av alla andra instanser före den Högsta förvaltningsdomstolen.

Finland implementerade en ny lag, lagen om koncernavdrag, som är tillämplig från och med 2021. Lagen tillåter ett finskt moderbolag att dra av sin utländska dotterbolagets slutgiltiga förluster i Finland för moderbolagets finska skattemässiga ändamål. Dock med hänsyn till de fem ovannämnda fallen från Högsta förvaltningsdomstolen, uppstår frågan ifall det ens är möjligt att bevisa slutgiltigheten av ett utländskt dotterbolags förluster. I regeringens proposition för lagen om koncernavdrag är konceptet om de slutgiltiga förlusterna hänvisade till definitionen som utvecklats i EU-domstolens rättspraxis. Intressant nog, så har andra medlemsländer framgångsrikt tillåtit deras bolag att dra av utländska dotterbolagens slutgiltiga förluster för moderbolagets skattemässiga ändamål, men i Finland verkar denna fråga ännu vara olöst.

Frågan som också uppstår är om Finland genom att lägga bevisbördan omöjligt högt bryter mot EU lag. Denna synpunkt kunde argumenteras på bakgrund av EU-domstolens fall *San Giorgio*. Ett annat tillvägagångssätt kunde vara att göra en formell klagan till Europeiska kommissionen där man argumenterar att Finland bryter mot EU lag (och härav mot principerna i *San Giorgio*) när de lägger bevisbördan för slutgiltiga förluster oskäligt högt.

Nyckelord final losses, Marks & Spencer, Memira Holding, cross-border merger, group deduction

I. LIST OF ABBREVIATIONS

CCCTB	Common Consolidated Corporate Tax Base
CCTB	Common Corporate Tax Base
CJEU	Court of Justice of the European Union
EEA	European Economic Area
EFTA	European Free Trade Association
EU	European Union
EC	European Commission
PE	Permanent establishment
SAC	Supreme Administrative Court
TFEU	Treaty on the Functioning of the European Union
UK	United Kingdom

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1 INTRODUCTION

1.1 Background

There are several ways of conducting business, both within one state and cross-border. An entity may be a stand-alone entity, only established in one state, or upon expansion of the business, the entity may create a branch or subsidiary (for example) in the other state.
From a tax point of view, there are certain benefits to each choice of doing business both within one state and cross-border. For example, a Finnish entity may select to conduct business in another EU Member State through a subsidiary, resident in such other EU Member State, in order to make use of the tax benefits granted under the Parent-subsidiary Directive[1]. On the other hand, the Finnish entity may elect to only do business from Finland without creating a taxable presence in such other EU Member State. The selection of method of conducting business cross-border is often not conclusively driven by taxation, but often also reflect the best choice of doing business from a pure business perspective. However, it may not be denied that taxation is an important driver when deciding upon how to conduct business.

The European Union ("**EU**") has tried, to the extent possible, to ease the conduct of cross-border business and to eliminate the taxable obstacles within the EU internal market. For example, when different entities within a group incur profits and losses within only one EU Member State, the profits and losses are often automatically aggregated, as most EU Member States offers a so-called group taxation scheme, for the automatic offsetting of profits and losses between entities of the same group in the same jurisdiction. Group taxation provides for fiscal consolidation *(integration fiscal or fiscal eenheid*) and a loss carry-over or profit carry-forward mechanisms.[2] However, in Finland there is no automatic group taxation scheme, rather the legislator has taken a less automatic approach in this regard. In Finland, the Act on Group Contribution[3] allows for the equalization of income of limited liability companies or cooperatives, forming part of the same group, with the aim of balancing profits and losses within the group. The idea is that group contribution is a deductible expense in the

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[1] Council Directive 2011/96/EU of 30 November 2011 on the common system of taxation applicable in the case of parent companies and subsidiaries of different Member States, OJ L 345, 29.12.2011

2 Terra/Wattel, European Tax Law, Seventh Edition, Wolters Kluwer, p. 757 and Wolfgang Schoen, EU Tax Law: An Introduction, Max Planck Institute for Tax Law and Public Finance, Working Paper 2019 – 12, August 2019

3 Laki konserniavustuksesta verotuksessa (825/1986, KonsAvL)

taxation of the contributor and taxable income for the beneficiary, when it meets the conditions set out by the law.[4]

By contrast, when the group entities are located in different states or EU Member States, the taking into account of a branch's or subsidiary's (or between two subsidiaries in different states) losses is often restricted or impossible, as such losses will only be offset against previous or future profits incurred in the same state. Where an entity is lossmaking for several years, there might not be any previous or future profits from which to deduct the incurred losses. This results in the fact that the losses are, so to say, locked in this jurisdiction providing for a higher overall tax burden of multinational group entities (assuming some other group entity is profitable).[5] This consequently is a disadvantage for group companies established in several jurisdictions, as opposed to group companies established in only one jurisdiction,[6] a fact that also has gained the EU legislators interest. One of the solutions the EU has proposed for this disadvantage is the core of this thesis, namely the "transfer" of losses from one EU Member State to another. The solution proposed is based and developed in EU case-law and complex, due to which the subject has gained great attention.

1.2 The EU's attempt to eliminate the cross-border disadvantage of groups relating to losses incurred in different Member States

As a response to the disadvantage groups face, especially in relation to losses incurred in different EU Member States, the European Commission ("**EC**") (1990) drew a proposal for a Directive[7] on cross-border offsetting of losses between entities forming part of the same group and between headquarters and branches. This was the first attempt to a more harmonious EU internal market but unfortunately this proposal was withdrawn in 2001.[8]

Some years later (in 2004 precisely), it was expected that the EC would launch a new initiative in this regard. However, surprisingly no progress was seen until the famous EU case *Marks & Spencer II*[9], that marked the cornerstone for the final losses doctrine and a more harmonious

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[4] Valtiovarainministeriö Valtioneuvoston kanslia, Taxation Glossary, 2002
[5] Terra/Wattel, European Tax Law, Seventh Edition, Wolters Kluwer, p. 758
[6] Terra/Wattel, European Tax Law, Seventh Edition, Wolters Kluwer, p. 758
[7] Proposal for a Council Directive Concerning Arrangements for the Taking into Account by Enterprises of the Losses of Their Permanent Establishments and Subsidiaries Situated in Other Member States COM/90/595 final OJ C 53, 28.2.1991, P. 30
[8] Communication from the Commission: Withdrawal of Commission proposal which are no longer topical; COM (2001) 763 final/2 of 21 December 2001, O.J. No. C 5, p.2, of 9 January 2002.
[9] Case C-446/03, *Marks & Spencer II*, EU:C:2005;763

(or so it was thought) EU internal market for group entities. However, despite the famous EU case, the issue of losses incurred in different EU Member State and the cross-border offsetting of such was only solved to a minor extent.[10]

In the *Marks & Spencer II* judgement, the Court of Justice of the European Union ("**CJEU**") concluded that the EU Member State of the parent company (the UK) should provide relief for final or definitive foreign losses i.e. in situations 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 Member 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.[11] In simple terms, the state of the parent company should allow the parent company to deduct the subsidiary's so-called final losses, as denying the offsetting would be against the freedom of establishment.

The EU opened the door for the possibility to provide relief for group companies incurring losses in different EU Member State, however with a rather heavy restrictions, due to, for example, the risk of tax avoidance. At least Finland, has currently made the burden of proof of final losses so high, that it seems rather impossible to *de facto* demonstrate final losses. The *Marks & Spencer II* case did only provide little comfort since it only concerned final losses and not current ones.

The EC realized that the issue at stake had not been solved by current law or case-law and published, in December 2006, a Communication[12] on the Tax Treatment of Losses in Cross-Border Situations. In its Communication, the EC aimed at *"improving the competitiveness of business in the European Union, which is hampered among other things by the absence of cross-border relief for losses*."[13] In its proposal, the EC encouraged EU Member States to adopt unilateral measures for the cross-border relief of losses within groups, by way of the following criteria

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[10] Terra/Wattel, European Tax Law, Seventh Edition, Wolters Kluwer, p. 759
[11] Case C-446/03, *Marks & Spencer II*, EU:C:2005;763, para 59
[12] Communication from the Commission to the Council, the European Parliament and the European Economic and Social - Committee Tax Treatment of Losses in Cross-Border Situations, COM/2006/0824 final
[13] Communication from the Commission to the Council, the European Parliament and the European Economic and Social - Committee Tax Treatment of Losses in Cross-Border Situations, COM/2006/0824 final, para 1.1

"A targeted measure addressing cross-border loss relief should ensure that corporate groups doing business in several Member States are treated as far as possible in the same way as groups doing business with a single Member State. In particular, it should allow losses to be set off from the tax base for the year in which they are incurred. A targeted measure should thus: (a) permit an effective and immediate, once-only deduction of losses; (b) allow, as a minimum, losses to be taken into account at the level of the parent company ("vertical upward" set-off); (c) not normally result in a definite shift of income from one Member State to another, unless the losses are terminal and there is no possibility for relief in the State where such losses were incurred; (d) exhaust domestic possibilities for current loss relief first; and (e) not offer scope for abuse."[14]

The EC identified three options that would to some extent meet the aimed targets:

- The first option was a definitive cross-border transfer of losses of a group, or an intra-group cross-border profit contribution system.[15]
- The second alternative was a temporary loss transfer (the deduction or reintegration method). Here the losses, incurred by a foreign EU subsidiary, which was deducted from the results of the parent company, is recaptured once the foreign subsidiary becomes profitable.[16]
- The third option was fiscal consolidation of foreign EU subsidiaries. This entailed that profits and losses of a fiscal year of some or all group companies are taken into account over a certain time period, at the level of the parent company. Such consolidated foreign EU subsidiaries would be treated as permanent establishments. Tax paid by a foreign EU subsidiary (in its state of establishment), is credited against the tax payable in the EU Member State of the parent company.[17]

However, the EC's 2006 Communication gained little response due to which the EU's common consolidated tax base project was set in motion. The EC drew a proposal for a

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[14] Proposal for a Council Directive on a Common Consolidated Corporate Tax Base (CCCTB), COM/2011/0121 final, point 3.3.3. and Terra/Wattel, European Tax Law, Seventh Edition, Wolters Kluwer
[15] Luca Cerioni, European Union - Postponement of the Commission's Proposal for a CCCTB Directive: Possible Ways Forward, Bulletin for International Taxation, 2010 (Volume 64), No. 2.
[16] Proposal for a Council Directive on a Common Consolidated Corporate Tax Base (CCCTB), COM/2011/0121 final, point 3.4.2. and Terra/Wattel, European Tax Law, Seventh Edition, Wolters Kluwer
[17] Proposal for a Council Directive on a Common Consolidated Corporate Tax Base (CCCTB), COM/2011/0121 final, point 3.4.3. and Terra/Wattel, European Tax Law, Seventh Edition, Wolters Kluwer

Directive on an EU wide common consolidated corporate tax base ("**CCCTB**") in 2011.[18] As the CCCTB proposal did not succeed, the EC re-launched the CCCTB project in October 2016 with a proposal on a two-step approach, namely a common corporate tax base ("**CCTB**") and the common consolidated corporate tax base, whereas the CCCTB proposal was withdrawn the same day in 2011.[19] The 2016 CCCTB and CCTB proposals include cross-border relief for entities but it remains unclear whether the there is a chance of adopting a common corporate, or consolidated, tax base at all within the EU.[20] It is currently year 2021 and no such common corporate or consolidated tax base have been adopted nor does it seem to be done in the near future.

In the meantime, whilst the EU is tumbling with the CC(C)TB implementation or development, several CJEU cases have been issued regarding the cross-border loss relief in respect of branches and subsidiaries, all of which has made the cross-border loss relief rather limited and complex. Alongside the CJEU's case-law development, national courts and legislators try to implement the evolving concept, as the EC issues infringement proceedings against states not enabling the use of final losses, in a group contribution situation (e.g. infringement proceedings were initiated against Finland in 2019).

1.3 Aim of the thesis

In its simplicity, this thesis aims to analyse one of the solutions of the EU to eliminate the disadvantage group entities within the EU face. The solution is, as aforenoted, based and developed in EU case-law and entails that a group company may under certain conditions deduct its foreign EU based entity's losses. This thesis tries to analyse as to when a Finnish entity may take its EU based group entity's foreign losses into account for Finnish tax purposes. In order to understand this aim, extensive EU case-law will need to be clarified, as well as the Finnish legislations evolution.

1.4 Research question

The research question of this thesis is a) what is the CJEU development of the final losses doctrine b) how and why Finland has implemented the final losses doctrine with regards to

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18 Proposal for a Council Directive on a Common Consolidated Corporate Tax Base (CCCTB), COM/2011/0121 final and Terra/Wattel, European Tax Law, Seventh Edition, Wolters Kluwer, p. 759-760
19 Terra/Wattel, European Tax Law, Seventh Edition, Wolters Kluwer, p. 760
20 Terra/Wattel, European Tax Law, Seventh Edition, Wolters Kluwer, p.484 and 760

group contribution c) how the Finnish implementation with regards to group contribution may affect cross-border mergers and the final losses related to such.
In order to answer the research question, this thesis firstly need to identify the background and development of the final losses doctrine in CJEU case-law, after which the Finnish implementation of the doctrine is further discussed.

1.5 Structure of the thesis

The thesis is divided into four chapters starting with the introduction, that will set the scene for why the final losses doctrine has been topical for years. The introduction will assist the reader to the EU history behind the development of the final losses doctrine and the challenges such has brought through the EU internal market.

Chapter II provides a background for the reader as to the applicable EU law, form where the final losses doctrine stems. Chapter II will already touch upon the subjects that will be dealt with in dept in Chapter III.

Chapter III provides for a in depth description of the creation and evolution of the final losses' doctrine in EU and EEA case-law. Chapter III is divided into different areas, where the final losses doctrine has penetrated and evolved, such as the final losses doctrine's evolution with regards to non-resident group companies, foreign branches, cross-border mergers and permanent establishments.

Finally, in Chapter IV, the thesis deals with the evolution of the final losses doctrine in Finnish law and case-law, especially noting the recent developments and infringement proceedings initiated by the EC against Finland, with regards to cross-border group contribution (or deduction). Chapter IV also deals with the Finnish implementation of the final losses doctrine with regards to cross-border mergers however noting that the evolution has not reached its end yet in Finland, as scholars further awaits for the Ministry of Finance's working groups report around the end of year 2021 (when the working group's mandate ends).

2 THE EU FOUR FREEDOMS: THE FREEDOM OF ESTABLISHMENT

2.1 The EU four freedoms

The EU and the EU internal market is built on four freedoms, as set out in the Treaty on the Functioning of the European Union[21] ("**TFEU**"), namely,

- the free movement of goods (TFEU Article 34),
- the free movement of persons, that includes
    - the free movement of EU citizens (TFEU Article 21)
    - the free movement of workers (TFEU Article 45)
    - freedom of establishment (TFEU Article 49)
- freedom to provide or receive services (TFEU Article 56), and
- free movement of capital and payments (TFEU Article 63).

The four freedoms provided for in the TFEU are considered to be part of the general principles of the EU and are protected by the CJEU.[22] The aforementioned principles also apply in relation to states belonging to the European Economic Area (EEA).[23]

The four freedoms are directly applicable meaning that these may be relied to before national courts of EU Member States, if the national law conflicts with the TFEU. [24] This right is executed repletely by its nationals.

Articles 45 and 49 of the TFEU prescribes that discrimination based on a different treatment, on the grounds of nationality, is prohibited. However, the CJEU has time and time again confirmed that a discrimination and restriction of the basic freedoms is prohibited and constitutes discrimination.[25]

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[21] Consolidated version of the Treaty on the Functioning of the European Union, OJ C 326, 26.10.2012

[22] Case 29-69, *Erich Stauder v City of Ulm - Sozialamt.* EU:C:1969:57

[23] Marjaana Helminen, EU Tax Law, Direct Taxation, 2017 Edition, IBFD, p. 67.

[24] Marjaana Helminen, EU Tax Law, Direct Taxation, 2017 Edition, IBFD

[25] For example:
Case 81/87, *The Queen v H. M. Treasury and Commissioners of Inland Revenue, ex parte Daily Mail and General Trust plc*, EU:C:1988:456,
Case C-415/93, *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*, EU:C:1995:463

Due to the four freedoms, as prescribed in the TFEU, taxation that restricts the use of a said freedom can conflict with the TFEU, even where the treatment may not be classified as discrimination. Consequently, the tax treatment in a EU Member State can also be in conflict with the TFEU even though the treatment does not distinguish between a purely internal situation and a cross-border situation, if the treatment in any way provide for a restriction of the cross-border activity. This means that all measures that prohibit impede or render less attractive the exercise of the basic freedoms are generally regarded as a restriction of the EU freedoms.[26] To provide an example, the tax treatment that prevents or restricts a taxpayer from moving or establishing from a Member State to another may constitute a restriction of the TFEU. In line with this, the treatment may be in conflict with the TFEU even where the tax burden is not higher, but the cross-border situation is subject to more burdensome procedural or administrative requirements.[27]

2.2 The freedom of establishment – the cornerstone of the final losses doctrine

As per Article 49 and 54 of the TFEU, the freedom of establishment provides EU nationals the right to establish directly in another Member State and to pursue activities therein as a self-employed person or via an undertaking. This is also called primary establishment.[28] Article 49 and 54 of the TFEU also prescribes for the right of EU nationals to establish and to pursue activities in any EU Member State via, for example, branches or subsidiaries. This establishment is also called secondary establishment. Likewise, the freedom of establishment is also applicable on a transfer of activities from one Member State to another.[29]

EU nationals have the right to choose the EU Member State, where they would wish to conduct business, and the way (legal form) of doing business in the said Member State (being a subsidiary, branch or an agency, for example).[30] The freedom of establishment prescribes that the tax treatment of a Member State may not restrict the EU nationals right to leave or to establish in another Member state. [31] In line with the aforementioned, and generally, a cross-

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[26] Case C-157/07, *Krankenheim Ruhesitz am Wannsee-Seniorenheimstatt*, EU:C:2008:588, para 30.
[27] Case C-279/93, *Finanzamt Köln-Altstadt v Roland Schumacker*, EU:C:1995:31, para 49
Case C-250/95, *Futura Participations SA and Singer v Administration des contributions*, EU:C:1997:239, para 21 and Marjaana Helminen, EU Tax Law, Direct Taxation, 2017 Edition, IBFD, p. 69.
[28] Case C-261/11, *European Commission v Kingdom of Denmark*, EU:C:2013:480, para 28. and Marjaana Helminen, EU Tax Law, Direct Taxation, 2017 Edition, IBFD
[29] Case C-261/11, *European Commission v Kingdom of Denmark*, EU:C:2013:480, para 28. and Marjaana Helminen, EU Tax Law, Direct Taxation, 2017 Edition, IBFD
[30] Case 270/83, *Commission of the European Communities v French Republic*, EU:C:1986:37, para 22.
[31] KHO 2006/1503, 9.6.2006

border situation may not be discriminated compared to a purely domestic situation (with certain exemptions further dealt with in this thesis). In other words, the tax treatment of a parent company may not be less beneficial if such has a subsidiary in another Member State (cross-border situation) as compared to a parent company that has a subsidiary in the same Member State (purely domestic situation). The differing treatment may hinder the parent company from establishing in other Member States.[32]

2.3 The restriction of the freedom of establishment – acceptable in certain limited situations

Article 49 of the TFEU prohibits for both direct and indirect discrimination on the basis of nationality. The tax treatment of EU nationals may be in conflict with the TFEU where nationals of different Member States are treated differently in a comparable situation or where nationals of different Member States are treated alike in a different situation, where the consequence is that a Member State's own national is treated worse than the other Member State's national.[33] In other words, the TFEU provisions on the freedom of establishment ensures that nationals from other Member States are treated in the same manner as nationals of such a Member State. Thus, provisions that may have an effect of hindering a Member State national (e.g. an entity) established in such Member State from leaving that state in order to establish in another Member State, may be in conflict with the TFEU.[34]

The right to invoke the freedom of establishment principle

The application of TFEU Article 49 however requires that an EU national have made use of the right to establish in another EU Member State. Thus, an establishment means a fixed integration in the economy of another Member State, with the intention to conduct economic activities for an indefinite time.[35]

[32] Case C-168/01, *Bosal Holding BV v Staatssecretaris van Financiën*, EU:C:2003:479, para 27.
[33] Case C-250/95, *Futura Participations SA and Singer v Administration des contributions*, EU:C:1997:239 and Marjaana Helminen, EU Tax Law, Direct Taxation, 2017 Edition, IBFD, p. 90.
[34] Marjaana Helminen, EU Tax Law, Direct Taxation, 2017 Edition, IBFD, p. 92, and for example, Case C-157/07, *Krankenheim Ruhesitz am Wannsee-Seniorenheimstatt*, EU:C:2008:588, para 27
[35] Case C-55/94, *Reinhard Gebhard v Consiglio dell'Ordine degli Avvocati e Procuratori di Milano*, EU:C:1995:411, para 25 and Marjaana Helminen, EU Tax Law, Direct Taxation, 2017 Edition, IBFD, p. 93.

2.3.1 Comparable situation

The freedom of establishment principle prohibits the different tax treatment of domestic and foreign undertakings by a Member State, if the undertakings are considered to be in a comparable situation. This means that a tax benefit is to be granted even where the foreign entity is a non-resident for tax purposes.[36] The comparability analysis require that it is established whether the situations are objectively comparable, in order for a different treatment to be allowed. Where two situations are comparable and a different treatment occurs, it must be evaluated whether the treatment is justified or not. However, it may be noted that all restrictions are not automatically forbidden and deemed discriminatory. As such, a restriction of the freedom of establishment may be allowed where certain requirements are fulfilled (e.g. preserving the balanced allocation of taxing rights). This is further deliberated upon in the Chapters to follow.

2.3.2 Justifications and proportionality

For a restrictive tax treatment to be justified, the tax treatment has to be appropriate to ensure the attainment of the objective in question, and the restriction may not go beyond what is necessary to attain the said objective. A tax provision that restrict the freedom of establishment is not accepted if there would be a measure available that would reach the same objective in a less restrictive manner.[37] Accepted reasons, based on the CJEU's case law, have been the following reasons:

- Anti-avoidance purposes (see for example *Marks & Spencer II*),
- The safeguarding of a balanced allocation of taxing rights between Member States (see for example *Marks & Spencer II*),
- The need to prevent the double use of losses (a double dip) (see for example *Marks & Spencer II*),

Other accepted reasons have been found to be:

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[36] Case C-406/07, *Commission of the European Communities v Hellenic Republic*, EU:C:2009:251 and Marjaana Helminen, EU Tax Law, Direct Taxation, 2017 Edition, IBFD, p. 95.

[37] For example
Case C-55/94, *Reinhard Gebhard v Consiglio dell'Ordine degli Avvocati e Procuratori di Milano*, EU:C:1995:411
Case C-250/95, *Futura Participations SA and Singer v Administration des contributions*, EU:C:1997:239
Case C-157/07, *Krankenheim Ruhesitz am Wannsee-Seniorenheimstatt*, EU:C:2008:588

- The safeguarding of effectiveness of fiscal supervision
- The need to ensure the recovery of a tax debt
- The safeguarding of fiscal cohesion of the national system and the territory principle.[38]

[38] Marjaana Helminen, EU Tax Law, Direct Taxation, 2017 Edition, IBFD, p. 97.

3 EU CASE-LAW FORMING THE FINAL LOSSES DOCTRINE

3.1 Background to the final losses doctrine

As touched upon in Chapter I, the creation of the final losses doctrine had its roots in the EU four freedoms, more specifically the freedom of establishment. In more simple terms, the creation of the final losses doctrine was a response to the need/wish for cross-border offsetting of losses within a group. [39] To recall the issue, group companies established in multiple states or EU Member States suffers a higher overall tax burden where cross-border offsetting of losses are not enabled:

> For example; an EU based group consists of a Finnish parent company, a Swedish subsidiary, a Danish subsidiary and a Norwegian subsidiary. The Finnish parent company is profitable, the Swedish subsidiary is profitable but both the Danish and the Norwegian subsidiary are loss-making and has been loss-making for several years (and is foreseen to be loss-making in future years as well). The Finnish parent company and the Swedish parent company pays corporate income tax on their profits in respective countries, whilst the Danish and the Norwegian companies are incurring losses. Should all the companies be established in Finland, group contribution would, assuming the conditions for group contribution is met, be utilized to "offset" losses against incurred profits. However, in a cross-border situation this is not automatically possible, due to which the overall tax burden of the Scandinavian group is higher compared to a situation where the group is established in, for example, Finland.

The above explained example illustrates the core issue of the final losses doctrine and why this doctrine has gained EU wide attention. As noted in Chapter I, the EU has tried to solve or ease the issue of cross-border offsetting of losses, but no tangible solution or ease was reached until the CJEU case *Marks & Spencer II*, that marked the start of a new era and the final losses doctrine. However, *Marks & Spencer II*, to the disappointment of many, did not bring about the desired solution.

Marks & Spencer II created the final losses doctrine but also marked the start for when foreign losses are to be taken into account for tax purposes by the state of the parent company. Hence,

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[39] Terra/Wattel, European Tax Law, Seventh Edition, Wolters Kluwer, p.760

Chapter III will clarify as to when the cross-border offsetting of losses is to be allowed and what *final losses* are, according to CJEU case-law.

3.2 The development of final losses in CJEU case-law – Non-resident group companies

The concept of final losses was born by the *Marks & Spencer II* case[40], where the cross-border relief of losses was hoped to be solved. However, as analysed below, *Marks & Spencer II* did not bring about the desired solution, but rather a complex definition of *final losses*, where the cross-border relief of losses has proven to be, to some extent, impossible (e.g. in Finland). Despite the unclearness of the final losses doctrine, the definition of final losses have continued to evolve in CJEU case law starting from *Marks & Spencer II* and evolving in the cases *Lidl Belgium*, *X Holding*, *A Oy*, *Memira Holding AB* and *Holmen AB*.

3.2.1 *Marks & Spencer II*

Background

The *Marks & Spencer II*[41] case, and the start of the so-called final losses doctrine, concerned losses incurred by the UK resident Marks & Spencer's French, German and Belgian subsidiaries.[42] The UK resident company Marks & Spencer plc claimed that their inability to offset their foreign subsidiaries losses was contrary to EU law (the freedom of establishment. Marks & Spencer argued that the UK should allow the parent company (Marks & Spencer plc) to deduct their French, German and Belgian subsidiaries losses, on the reason that the UK allowed for the deduction of losses of foreign branches and losses of UK resident subsidiaries, through group relief. [43]

All three subsidiaries had incurred losses and would probably not have derived any profits in future years in their state of residence. It was argued that all options for making use of the losses were exhausted. Consequently, the losses would have been lost in respective Member States, unless the UK would allow the parent company to deduct the foreign losses in the UK for its tax purposes. UK law allowed for group relief for UK resident subsidiaries and foreign

[40] Case C-446/03, *Marks & Spencer II*, EU:C:2005;763
[41] Case C-446/03, *Marks & Spencer II*, EU:C:2005;763
[42] Case C-446/03, *Marks & Spencer II*, EU:C:2005;763, para 22.
[43] Case C-446/03, *Marks & Spencer II*, EU:C:2005;763, para 26.

branches, but the group relief did not apply to foreign based subsidiaries of a UK resident parent company.[44]

The CJEU

The UK High Court referred the matter to the CJEU for a preliminary ruling. The CJEU started with commenting that "*although direct taxation falls within their competence, Member States must none the less exercise that competence consistently with Community law."*[45] The Court further concluded, that not granting foreign subsidiaries established in another Member State to benefit from the advantage of the UK group relief scheme did constitute a restriction of the freedom of establishment[46].

As the exclusion of the advantage, in respect of the losses incurred by a subsidiary established in another Member State, constitutes a restriction on the freedom of establishment, the CJEU went to analyse whether the restriction could be justified by imperative reasons in the public interest.[47] The CJEU considered whether excluding the UK group relief system from foreign subsidiaries could be justified based on three justifications taken together: [48]

- First, the balanced allocation of powers between Member States where profits and losses are two sides of the same coin and must be treated symmetrically in the same tax system;
- Second, the prevention of the double use of losses as there exists a risk that the losses are taken into consideration in both Member States, and hence might well be taken into account twice (double dip);
- Third, the prevention of tax avoidance, as a risk of transferring losses to companies established in a Member State applying for the highest tax rate.[49]

Even though a justified restriction existed, the CJEU needed to ascertain whether the restrictive measure goes beyond what is necessary to attain the objective pursued.[50] The CJEU

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[44] Case C-446/03, *Marks & Spencer II*, EU:C:2005;763, para 24.
[45] Case C-446/03, *Marks & Spencer II*, EU:C:2005;763, para.29
[46] Case C-446/03, *Marks & Spencer II*, EU:C:2005;763, para 33
[47] Case C-446/03, *Marks & Spencer II*, EU:C:2005;763, para 35
[48] Michael Lang, The Marks & Spencer Case – The Open Issue Following the ECJ's Final Word, European Taxation, IBFD, 2006, and Michael Lang, Has the Case Law of the ECJ on Final Losses Reached the End of the Line?, European Taxation, 2014 (Volume 54), No. 12
[49] Case C-446/03, *Marks & Spencer II*, EU:C:2005;763, para 43 and Dennis Weber and Bruno da Silva, From Marks & Spencer to X Holding, The Future of Cross-Border Group Taxation, Wolter Kluwer, 2011.
[50] Case C-446/03, Marks & Spencer II, EU:C:2005;763, para 53

concluded that the restriction goes beyond that is necessary to attain the objective if (the famous *Marks & Spencer II* para 55):

> *"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 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."*[51]

In sum, the CJEU concluded that it would be disproportionate to deny the deduction of such foreign subsidiary's losses in cases where the deduction in the jurisdiction of residence of the subsidiary has become impossible.[52]

It can be concluded, from the CJEU's argumentation, that the CJEU accepts a significant difference with regards to timing of intra-group loss relief and a difference in cash-flow for cross border groups. The timing difference occurs where a foreign loss-making subsidiary have to wait for future profits (i.e. better years) in order to offset its incurred losses, whereas groups with subsidiaries in the same Member State, as the parent company, may carry over its losses within the same fiscal year to profit-making group companies, in order to limit the overall tax burden of the group.[53]

As a conclusion, the UK's tax administration accepted the losses as final and agreed to carry over the foreign losses to the UK, but such losses were calculated on the basis of UK tax accounting principles.[54]

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[51] Case C-446/03, *Marks & Spencer II*, EU:C:2005;763, para 55
[52] Terra/Wattel, European Tax Law, Seventh Edition, Wolters Kluwer, p.768
[53] Terra/Wattel, European Tax Law, Seventh Edition, Wolters Kluwer, p.769
[54] Terra/Wattel, European Tax Law, Seventh Edition, Wolters Kluwer, p.769

Open questions after Marks & Spencer II

The concept of final losses, as stated by the CJEU in the *Marks & Spencer II* case left several unanswered questions, as to what the final losses doctrine constitutes. The (at least) following open questions were left by the *Marks & Spencer II* decision:[55]

- Could the final losses doctrine test, as developed in Marks & Spencer II, be applied to other types of group regimes (other than regimes similar to the UK one);
- Could the final losses concept be applied irrespectively of the contributor and recipient (i.e. could the doctrine be applied between sister companies);
- Why the CJEU would not touch upon the cash-flow disadvantage, as such disadvantage would not arise in a purely domestic situation;
- According to which Member State's accounting principles are the losses to be calculated (as the accounting principles varies within the EU), and how to deal with the differences in timing and depreciation, as no common corporate tax base yet exist;
- Are all losses to be deducted in the same fiscal year (i.e. in the year when the claim has been made) or should there be a retroactive deduction (i.e. to deduct the losses retroactively when the losses have arisen);
- Why the CJEU restricted the applicability only to final losses as the issue of current losses also exist;[56]
- Who has the burden of proof to demonstrate that losses are final?

Marks & Spencer II take-away and burden of proof

Marks & Spencer II made it clear that EU Member States are to allow the cross-border offsetting of losses, however with the restriction that the losses need to be deemed final. Per the ruling, it is clear that the subsidiary may not be able to use the incurred losses not in previous years, in current years nor in future years. The evaluation does not only take into account the subsidiary's possibility to take losses into account but also whether a third party could make use of the incurred losses, either in current or future years.[57]

[55] Dennis Weber and Bruno da Silva, From Marks & Spencer to X Holding, The Future of Cross-Border Group Taxation, Wolter Kluwer, 2011, p.8
[56] Dennis Weber and Bruno da Silva, From Marks & Spencer to X Holding, The Future of Cross-Border Group Taxation, Wolter Kluwer, 2011, p.8.
[57] HE 185/2020 vp

For the question of how many year's losses may be deemed final is yet to be established, as the evaluation lacks proper standpoints.

Member State's tax administrations have taken a more stringent approach and require a foreign subsidiary to be wound up, in order to fulfil the criteria of final losses, whilst taxpayers tend to take the position that legal exhaustion of the possibilities to use the losses (the expiry of local relief time-limits included) should be characterized as final losses and the refusal of relief as disproportionate.[58]

The CJEU also seems to take the position that the burden of proof lies exclusively with the taxpayer.[59] This approach is also taken by the Finnish Supreme Administrative Court.[60] The CJEU's standpoint in this regard seems to be contradictory with previous CJEU case-law, as the CJEU have in the past noted that the "*infringement of the freedoms can be constituted by moving the burden of proof to the taxpayer in cross-border situation*."[61] However, the CJEU did not clarify as to whether it intentionally transferred the burden of proof to the taxpayer. In fact, the reasoning does not deal with the burden of proof at all.[62]

3.2.2 *Marks & Spencer III*

Background

During the aftermath of Marks & Spencer II, the UK amended its tax laws in order for such to be compatible with EU law, as per the *Marks & Spencer II* ruling. However, the UK added conditions to the final losses concept that were not mentioned in the *Marks & Spencer II* ruling, and, as a result, the EC initiated infringement proceedings against the UK.[63]

The CJEU

The CJEU concluded that *"is settled law that losses sustained by a non-resident subsidiary cannot be characterised as definitive [...] by dint of the fact that the Member State in which*

[58] Terra/Wattel, European Tax Law, Seventh Edition, Wolters Kluwer, p.773
[59] Case C-446/03, *Marks & Spencer II*, EU:C:2005;763, para 56 and Michael Lang, The Marks & Spencer Case – The Open Issue Following the ECJ's Final Word, European Taxation, IBFD, 2006
[60] For example, KHO:2020:51
[61] Michael Lang, The Marks & Spencer Case – The Open Issue Following the ECJ's Final Word, European Taxation, IBFD, 2006
[62] Michael Lang, The Marks & Spencer Case – The Open Issue Following the ECJ's Final Word, European Taxation, IBFD, 2006
[63] Terra/Wattel, European Tax Law, Seventh Edition, Wolters Kluwer, p.790

the subsidiary is resident precludes all possibility of losses being carried forward". In other words, legally exhausted losses never constitute final losses."[64] The CJEU noted that legal exhaustion of losses does not constitute final losses.[65]

The CJEU assessed that Marks & Spencer II paragraph 55 also does not require that a subsidiary is wound up before the end of the accounting period in which the losses are sustained.[66] Losses may be characterized as final "*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*."[67]

Take-away

The CJEU clarified with this decision that final losses may occur when a subsidiary no longer has any income in the Member State of residence or does not have the possibility, in the future, of having income in that Member State.[68]

For the question of how many year's losses may be deemed final is yet to be established, as the evaluation lacks proper standpoints. In *Marks & Spencer III*, in assessing the British system, CJEU adopted a starting point that the finality of losses must be assessed immediately after the loss year. However, it is not necessarily clear whether this judgment can be read as to consider that a subsidiary's last year's losses are the only losses that may be deemed final.[69]

3.2.3 *Oy AA*

Background

In *Oy AA*[70], the Finnish group contribution's legitimacy was tested against the freedom of establishment and the final losses doctrine. The Finnish group contribution scheme availed profitable group companies to give group contribution to loss-making group companies, when

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[64] Case C-172/13, Commission v. UK (Marks & Spencer III), EU:C:2015:50, para 33
[65] Harm van den Broek, Final Losses in Respect of Cross-Border Mergers: Memira (Case C-607/17) and Holmen (Case C-608/17), European Taxation February/March 2020, IBFD
[66] Case C-172/13, Commission v. UK (Marks & Spencer III), EU:C:2015:50, para 35
[67] Case C-172/13, Commission v. UK (Marks & Spencer III), EU:C:2015:50, para 36
[68] Case C-172/13, Commission v. UK (Marks & Spencer III), EU:C:2015:50, para 36 and Terra/Wattel, European Tax Law, Seventh Edition, Wolters Kluwer, p.791
[69] HE 185/2020 vp
[70] Case C-231/05, *Oy AA*, EU:C:2007:439

certain requirements are met (all entities in the group were Finnish). This resulted in loss relief between Finnish group companies, where the profit-making company may deduct the contribution for its tax purposes.[71]

Oy AA wished to contribute profits to its loss-making UK resident parent company, which was not allowed under Finnish law regarding group contribution.[72] This contribution was naturally not allowed, as the allowing of such would result in international group companies being able to transfer their profits to any desired jurisdiction/ Member State. The UK also noted that the profit contribution, did not *per se* exist under UK tax law. As a result, should *Oy AA* be able to contribute its Finnish profits to its UK parent, a double dip situation would occur, where Finland could not tax Finnish source profits whilst the loss of the UK parent would remain unaffected and could be utilized at a later date.[73]

The CJEU

The CJEU, as in line with the *Marks & Spencer II* judgement, found the Finnish group contribution scheme to constitute a restriction on the freedom of establishment. The CJEU found, the fact that a resident company was subject to tax whilst a non-resident was not subject to tax, was not seen incomparable with EU law.[74] However, the Finnish group contribution scheme treats differently subsidiaries established in Finland, as to the fact whether or not their parent is resident in that same Member State,[75] a different treatment which constitutes a restriction on the freedom of establishment.

After finding the Finnish group contribution scheme to constitute a restriction on the freedom of establishment, the CJEU went to analyse whether a justification of the differing treatment exist. The CJEU found that, by a combination of two factors, namely, the need to safeguard the balanced allocation of the power to tax between the Member States, and the need to prevent tax avoidance, the Finnish group contribution scheme, pursues legitimate objectives

[71] Case C-231/05, *Oy AA*, EU:C:2007:439, para 8 and Terra/Wattel, European Tax Law, Seventh Edition, Wolters Kluwer, p.773
[72] Laki konserniavustuksesta verotuksessa (825/1986)
[73] Case C-231/05, *Oy AA*, EU:C:2007:439
[74] Dennis Weber and Bruno da Silva, From Marks & Spencer to X Holding, The Future of Cross-Border Group Taxation, Wolter Kluwer, 2011, p.10 and Case C-231/05, Oy AA, EU:C:2007:439.
[75] Case C-231/05, *Oy AA*, EU:C:2007:439, para 31

compatible with the TFEU, and is justified by overriding reasons in the public interest, and is appropriate to ensuring the attainment of those objectives.[76]

Oy AA take-away

As contrary to *Marks & Spencer II, Oy AA* did not concern the deductibility of losses or final losses at all, for that matter. The CJEU did not need to consider the cross-border offsetting of losses, but rather the exporting of profits (to another Member State), which indeed appears to be different and may justify a more restrictive approach.[77] The CJEU did not give much attention to the 'double dip' justification, as the CJEU did in *Marks & Spencer* II, as the Finnish system of intra-group financial transfers does not concern the deductibility of losses rather the balancing out of profits and losses within a group.[78] Consequently, the CJEU held two out of the three *Marks & Spencer II* justifications to be sufficient in *Oy AA*, which poses a differing view from Advocate General Kokott's opinion[79], where she points out that all three elements are closely linked to one another and cannot be viewed in isolation.

Also, no attention was given to whether the proportionality test would have been met should only one of the objectives have been met (i.e. either the prevention of tax avoidance or the safeguarding of the balanced allocation of taxing powers alone). Instead, the CJEU dealt with the two justifications together as a whole.[80] It may also be noted that an increasing amount of interest has been given by the CJEU to the balanced allocation of taxing rights between Member States.[81]

Furthermore, the CJEU clearly noted that the Finnish group contribution scheme did not specifically combat artificial arrangements, but the differing treatment and the entire group contribution scheme was justified due to the fact that group companies would otherwise have the possibility to decide upon the Member State where the groups profits could be taxed in, a fact that would endanger the Member State's possibility to tax its nationals where the business activities are performed. The CJEU clearly deviates from its case law, in order to take a more

[76] Case C-231/05, *Oy AA*, EU:C:2007:439, para 60
[77] Marjaana Helminen, Freedom of Establishment and Oy AA, European Taxation November 2007, IBFD
[78] Case C-231/05, *Oy AA*, EU:C:2007:439, para 57
[79] Opinion of Advocate General Kokott, Case C-231/05, delivered on 12 September 2006, para 48
[80] Marjaana Helminen, Freedom of Establishment and Oy AA, European Taxation November 2007, IBFD, p.497
[81] Enken Cohrs, European Union/Finland - Unresolved Issues in the ECJ's Case Law on Cross-Border Intra-Group Loss Relief in the Light of A Oy, European Taxation, 2013 (Volume 53), No. 7

lenient approach and to come to the wanted end result.[82] It can be concluded that the CJEU is concerned with aggressive tax avoidance that could pose a risk to the balanced allocation of taxing rights between Member States. Hence, the freedom of establishment principle does not seem to be an absolute right of EU nationals, which leaves the Member States defenceless against increasing tax competition and aggressive tax planning.[83]

3.2.4 *X Holding*

Background

In *X Holding*[84], a company resident in the Netherlands requested to be included in a fiscal unity with its Belgian subsidiary. This was denied on the basis that the Belgian subsidiary did not meet the requirement set out by law (to either be a resident of the Netherlands or to have a permanent establishment in the Netherlands). *X Holding* found the Dutch law to be in breach with the freedom of establishment.

The CJEU

The CJEU found that the Dutch legislation, in the matter at hand, did not breach EU law and the freedom of establishment. A restriction of the freedom of establishment principle was found, as the situation of a parent company contemplated to establish a fiscal unity with a non-resident subsidiary can be seen objectively comparable to that of a parent company wishing to form a single entity with a domestic subsidiary. As a result, the difference in treatment constitutes an infringement of EU law. The question then arises as to whether there is a justification for the difference in treatment, a restriction that was justified by only one of the *Marks & Spencer II* justifications, namely the preservation of the allocation of power to impose taxes between Member States.

The fact that a Member State decides to permit a temporary offset of losses incurred by a foreign permanent establishment, does not mean that such a possibility need to be extended

[82] Dennis Weber, Abuse of Law in European Tax Law: An Overview and Some Recent Trends in the Direct and Indirect Tax Case Law of the ECJ – Part 2, European Taxation, 2013 (Volume 53), No. 7
[83] Marjaana Helminen, Freedom of Establishment and Oy AA, European Taxation November 2007, IBFD, p.497
[84] Case C-337/08, *X Holding*, EU:C:2010:89

to non-resident subsidiaries or a resident parent company.[85] The Netherlands is not obliged to open their group taxation system for cross-border situations within the EU.

The different treatment is justified because a permanent establishment in other Member States and non-resident subsidiaries are not in a comparable situation, according to the CJEU, with regards to the allocation of taxing powers. A subsidiary is subject to unlimited tax liability in the foreign Member State, whilst the permanent establishment is the fiscal subject of the jurisdiction of the parent company's Member State.[86]

The CJEU clarified that the flexibility in cross-border situations would open the door for tax optimization, as liberty would be given to parent companies to "*choose freely the Member State in which the loss of that subsidiary are to be taken into account.*"[87]

Take-away from X Holding

The take-away from X Holding is that the Netherlands does not need to extend their group taxation regimes to cross-border situations.

However, the ruling has been highly criticized by scholars for its inconsistency with earlier CJEU case-law, which shows that the final losses doctrine is even tricky within the institution itself (as to when doctrine is to apply to cross-border situations).[88]

This case-law is of relevance also for understanding the Finnish implementation of the group deduction regime, as a response to the EC's infringement proceedings relating to the final losses doctrine.

3.2.5 *Yara International*

In Yara International, the European Free Trade Association's ("**EFTA**") court extended the final losses doctrine to the EEA.

[85] Marjaana Helminen, EU Tax Law, Direct Taxation, 2017 Edition, IBFD, p. 97. and Servaas van Thiel and Marius Vascega, European Union - X Holding: Why Ulysses Should Stop Listening to the Siren, European Taxation, 2010 (Volume 50), No. 8
[86] Marjaana Helminen, EU Tax Law, Direct Taxation, 2017 Edition, IBFD, p. 97. and Servaas van Thiel and Marius Vascega, European Union - X Holding: Why Ulysses Should Stop Listening to the Siren, European Taxation, 2010 (Volume 50), No. 8
[87] Case C-337/08, *X Holding*, EU:C:2010:89, para 32
[88] Servaas van Thiel and Marius Vascega, European Union - X Holding: Why Ulysses Should Stop Listening to the Siren, European Taxation, 2010 (Volume 50), No.

In *Yara International ASA*[89], a Norwegian resident company wished to deduct group contribution provided (contributed to its Lithuanian subsidiary) for tax purposes in Norway. *Yara International ASA* was however denied the right to deduct the group contribution, as Norwegian tax law does not permit group contribution from a Norwegian company resident for Norwegian tax purposes to a non-resident subsidiary.[90]

In its reasoning, the EFTA court followed the *Marks & Spencer II* reasoning and found a restriction of Article 31 EEA (equivalent to the freedom of establishment Article of the TFEU).[91] Further, the Norwegian law shall serve a legitimate objective, such as the balanced allocation of taxing powers between EEA States or the objective of preventing wholly artificial arrangements leading to tax avoidance.[92] The EFTA court concluded that the requirements of the Norwegian national law go beyond what is necessary to pursue those objectives, in cases the losses of the foreign entity was deemed to be final.[93]

3.2.6 *Memira Holding AB*

Background

In *Memira Holding AB*[94], a Swedish company had a subsidiary in Germany, but due to the subsidiary's loss-making position, the activities were ceased. Memira Holding AB wished to absorb its German subsidiary via a cross-border merger, whereas the German subsidiary would be dissolved without liquidation whilst Memira Holding AB would cease to have activities in Germany. [95]

In Germany, the subsidiary's losses could only be used according to German laws by deducting the losses from current or future profits, without a time limit.[96] However, as the German subsidiary was loss-making and had ceased its activities, the subsidiary would no

[89] Case E-15/16, *Yara International ASA*
[90] Terra/Wattel, European Tax Law, Seventh Edition, Wolters Kluwer, p.774
[91] Case E-15/16, *Yara International ASA*, paras 35-36.
[92] Case E-15/16, *Yara International ASA*, para 38 and Terra/Wattel, European Tax Law, Seventh Edition, Wolters Kluwer, p.774
[93] Case E-15/16, *Yara International ASA*, para 55
[94] Case C-607/17, *Skatteverket v Memira Holding AB*, EU:C:2019:510
[95] Case C-607/17, *Skatteverket v Memira Holding AB*, EU:C:2019:510, para 10
[96] Harm van den Broek, Final Losses in Respect of Cross-Border Mergers: Memira (Case C-607/17) and Holmen (Case C-608/17), European Taxation February/March 2020, IBFD

longer be eligible to deduct the incurred losses, as under German law, losses cannot be transferred to another company in the event of a merger.[97]

Contrary to German law, under Swedish law, with regards domestic mergers, a receiving company may adopt the transferring company's losses (with certain limits).[98] The rule did not apply to cross-border mergers, such as the merger between the Memira entities, whereas the Swedish Supreme Administrative Court asked the CJEU whether this national rule imposed a restriction of the freedom of establishment or whether such could be justified. The Swedish Supreme Administrative Court also asked whether the losses in the case at hand could be deemed final, despite the fact that German law did not provide for a transfer of losses in case of a merger.[99]

The CJEU

Advocate General Kokott concluded in her opinion that should the use of losses be precluded in Germany, no final losses exist, and as such, no final losses in the case of Memira Holding AB exist. [100] The CJEU did not follow AG Kokott's opinion and took a rather differing path. The CJEU noted:

> *"[...] the fact that the subsidiary's Member State of establishment does not allow the losses of one company to be transferred, in the event of a merger, to another company liable for corporation tax, whereas such a transfer is provided for by the Member State in which the parent company is established in the event of a merger between resident companies, is not decisive, unless the parent company demonstrates that it is impossible for it to deduct those losses by ensuring, in particular by means of a sale, that they are fiscally taken into account by a third party for future tax periods."*[101]

> *"It should be recalled in that regard that the grounds relied on by the Court in the second indent of paragraph 55 of the judgment in Marks & Spencer expressly envisaged that the absence of such a possibility on which the finality of the losses depends may be*

[97] Case C-607/17, *Skatteverket v Memira Holding AB*, EU:C:2019:510, para 11
[98] Case C-607/17, *Skatteverket v Memira Holding AB*, EU:C:2019:510, para 6
[99] Case C-607/17, *Skatteverket v Memira Holding AB*, EU:C:2019:510, para 22
[100] Case C-607/17, *Skatteverket v Memira Holding AB,* Advocate General Kokott's opinion, paras 65-70 and 77
[101] Case C-607/17, *Skatteverket v Memira Holding AB*, EU:C:2019:510, para 28

applied to the situation in which they are taken into account by a third party for future periods, in particular where the subsidiary has been sold to that third party."[102]

The Memira case is famous for this addition to the final losses doctrine. The fact that Germany did not allow for the losses to be transferred by way of a merger was not seen decisive itself (other possibilities to transfer the losses should be exhausted), unless the parent company demonstrates that it is impossible for it to deduct those losses by ensuring, in particular by means of a sale, that they are economically taken into account by a third party for future fiscal years.[103]

Take-away from Memira Holding AB

Losses of a subsidiary are not deemed final if there remains a possibility of taking advantage of the losses *economically* by transferring the losses to a third party, the burden of proof that is left to the taxpayer to demonstrate that such is precluded.[104]

The CJEU here refers to the deduction of the losses *economically*, where selling the subsidiary was mentioned as an alternative outcome. In such a case, both the seller and the buyer would economically benefit from the incurred losses.[105] From the English wording of the decision it can be read that the CJEU referred to the sale of the shares in the subsidiary company, whereas the Dutch translation refers to the sale by the subsidiary of its assets and liabilities.[106] However, interestingly enough, several Member State's anti-abuse laws prohibits the sale of losses and empty companies (Germany and the Netherlands applies anti-abuse measures combating the trade in empty companies). [107] This ruling is also interesting from the point of view of DAC6[108], that specifically targets such arrangements.

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[102] Case C-607/17, *Skatteverket v Memira Holding AB*, EU:C:2019:510, para 24
[103] Case C-607/17, *Skatteverket v Memira Holding AB*, EU:C:2019:510, para 28 and Harm van den Broek, Final Losses in Respect of Cross-Border Mergers: Memira (Case C-607/17) and Holmen (Case C-608/17), European Taxation February/March 2020, IBFD,
[104] Marjaana Helminen, Cross-Border Group Contribution, Freedom of Establishment and Final Losses, European Taxation, 2021 (Volume 61), No. 2/3
[105] Harm van den Broek, Final Losses in Respect of Cross-Border Mergers: Memira (Case C-607/17) and Holmen (Case C-608/17), European Taxation February/March 2020, IBFD, page 58
[106] Case C-607/17, *Skatteverket v Memira Holding AB*, EU:C:2019:510, para 26, Dutch translation, which refers to the sale of an enterprise (onderneming) and [106] Harm van den Broek, Final Losses in Respect of Cross-Border Mergers: Memira (Case C-607/17) and Holmen (Case C-608/17), European Taxation February/March 2020, IBFD, page 58
[107] Germany, section 8c(1) KStG and the Netherlands, article 20a CITA.
[108] Council Directive (EU) 2018/822 of 25 May 2018 amending Directive 2011/16/EU as regards mandatory automatic exchange of information in the field of taxation in relation to reportable cross-border arrangements, OJ L 139, 5.6.2018

The CJEU did not find the losses to be legally exhausted as a result that such could not be transferred to a third party, by way of a merger. In contrast, if the losses could not be transferred to third parties, then such losses are considered final and Memira Holding AB could take such into account in Sweden.[109]

Another question asked by the Swedish Supreme Administrative Court was whether

> "*account must be taken of the fact that there is, in the State of establishment of the subsidiary, no other entity which could have deducted the losses in the context of a merger if a deduction had been authorized in that country.*"[110]

Germany does not allow for a transfer of losses upon a merger. Hence, the existence of absence of other entities in the resident state of the loss-making subsidiary, is not relevant. In contrast, should the loss-making subsidiary have been established in Finland, that allows for the transfer of losses to other group companies by means of a merger (when certain requirements are met), the second question referred by the Swedish Supreme Administrative Court, would have been of relevance.[111]

Also, under certain conditions, losses might be deemed final in cases of cross-border mergers, should the domestic law of the transferring Member State not allow for a transfer of such losses to other companies. This does not yet still mean that the CJEU disregards its settled case law where losses that are legally exhausted are not deemed final.[112] It can be understood from the decision, that the subsidiary cannot offset its losses because its business activities had been ceased and was wound up, which indicates factual exhaustion of the losses. By contrast, the losses could also not be transferred to a third party by way of a merger, due to German national tax law, due to which, if the losses cannot be used by others in any way, such losses are to be deemed final. [113]

This decision leads to the fact where a transfer of losses in a purely domestic situation would not be possible (such as in Germany), the losses may be transferred to another Member State,

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[109] Harm van den Broek, Final Losses in Respect of Cross-Border Mergers: Memira (Case C-607/17) and Holmen (Case C-608/17), European Taxation February/March 2020, IBFD, page 58

[110] Case C-607/17, *Skatteverket v Memira Holding AB*, EU:C:2019:510, para 29.

[111] Harm van den Broek, Final Losses in Respect of Cross-Border Mergers: Memira (Case C-607/17) and Holmen (Case C-608/17), European Taxation February/March 2020, IBFD, page 59

[112] Harm van den Broek, Final Losses in Respect of Cross-Border Mergers: Memira (Case C-607/17) and Holmen (Case C-608/17), European Taxation February/March 2020, IBFD, page 59

[113] Harm van den Broek, Final Losses in Respect of Cross-Border Mergers: Memira (Case C-607/17) and Holmen (Case C-608/17), European Taxation February/March 2020, IBFD, page 59

by way of a cross-border merger under the final losses' doctrine. This result is somewhat undesirable, as the tax burden, caused by the choice of a Member State, is, as a result, economically passed on to another Member State, directly leading to an export of losses. [114]

3.2.7 *Holmen AB*

Background

In *Holmen AB*[115], Holmen was the parent company of a Swedish group. The group included a Spanish subsidiary, that in turn had several sub-subsidiaries. The sub-subsidiaries had accumulated losses and was intended to be liquidated.[116] The sub-subsidiaries incurred losses could not be deducted in Sweden, by way of an intra-group financial transfer, as Holmen did not hold the sub-subsidiary directly, as required by Swedish law.

The Swedish Administrative Supreme Court asked the CJEU for a preliminary ruling in order to clarify whether the right to deduct final losses requires the subsidiary to be directly owned by the Swedish parent company.[117]

The CJEU

The CJEU referred to the *Marks & Spencer II* case where it was concluded that a restriction of the freedom of establishment may be justified, unless such restriction goes beyond what is necessary.

The CJEU continued that to give companies the option to have their losses taken into account in the Member State in which they are established or in another Member State would significantly jeopardize a balanced allocation of the power to impose taxes between Member States.[118]

[114] Harm van den Broek, Final Losses in Respect of Cross-Border Mergers: Memira (Case C-607/17) and Holmen (Case C-608/17), European Taxation February/March 2020, IBFD, page 59
[115] Case C-608/17, *Skatteverket v Holmen AB, EU:C:2019:511*
[116] Case C-608/17, *Skatteverket v Holmen AB, EU:C:2019:511, para 10*
[117] Case C-608/17, *Skatteverket v Holmen AB*, EU:C:2019:511 and Harm van den Broek, Final Losses in Respect of Cross-Border Mergers: Memira (Case C-607/17) and Holmen (Case C-608/17), European Taxation February/March 2020, IBFD, page 60
[118] Case C-608/17, *Skatteverket v Holmen AB,* EU:C:2019:511, para 23 and Harm van den Broek, Final Losses in Respect of Cross-Border Mergers: Memira (Case C-607/17) and Holmen (Case C-608/17), European Taxation February/March 2020, IBFD, page 60

Hence, the CJEU concluded that it is not against the freedom of establishment to require that the parent company should hold the subsidiary directly. [119] However, where the intermediary subsidiary is established in the same state, as the entity applying for group relief, the risks of optimisation of the group tax rate by choosing in which Member State the losses are set off and of the multiple use of losses, does not exist. Hence, the CJEU noted that it would be disproportionate for a Member State to impose a requirement of direct ownership in the aforementioned situation, where the losses have been deemed final.[120]

Following the reasoning of *Memira Holding*, the CJEU argued that, the fact that Spain does not allow the losses of one company to be transferred to another company, in the year of liquidation, is not decisive, unless the parent company demonstrates that it is impossible for it to deduct those losses by ensuring, in particular by means of a sale, that they are taken into account by a third party for future periods.[121] In this regard, it is worth reading the reasoning of the CJEU, as it constitutes a clarification of the final losses doctrine:

> *"(...) 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.*
>
> *In fact, as the Advocate General stated in points 57 to 63 of her Opinion, 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 (...).*
>
> *Consequently, (...) it is for Holmen to demonstrate that the possibility referred to in the previous paragraph is precluded, as 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."*[122]

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[119] Case C-608/17, *Skatteverket v Holmen AB,* EU:C:2019:511, para 29
[120] Case C-608/17, *Skatteverket v Holmen AB,* EU:C:2019:511, para 30-33
[121] Case C-608/17, *Skatteverket v Holmen AB,* EU:C:2019:511, para 40
[122] Case C-608/17, *Skatteverket v Holmen AB,* EU:C:2019:511, paras 37-39

Take-away from Holmen

The Holmen case builds on the Marks & Spencer II paragraph 55 reasoning of final losses. Holmen clarified that the final losses doctrine may not apply to sub-subsidiaries, unless the intermediary is established in the same Member State as the sub-subsidiary.[123]

Also, the fact that the losses of a sub-subsidiary company may not be transferred to a domestic group entity (in the year of liquidation) is not detrimental, "unless the parent company demonstrates that it is impossible for it to deduct those losses by ensuring, in particular by means of a sale, that they are taken into account by a third party for future periods."[124]

3.3 The development of final losses in CJEU case-law – Cross border mergers

A Oy

Background

In *A Oy*, a Finnish parent company contemplated to merge with its fully owned Swedish subsidiary, after which the Swedish subsidiary would be liquidated due to its loss-making position. After the merger, the Finnish parent company would have deducted the Swedish losses in Finland for Finnish tax purposes.[125]

In a purely domestic situation, the absorbing company would have been able to use the merging company's losses (with certain exceptions).[126]

The CJEU

In its ruling, the CJEU followed the *Marks & Spencer II* approach and held that the freedom of establishment was applicable to the case at hand, as Finnish law did distinguish between a purely national merger as opposed to a cross-border merger whereas foreign losses could not be taken into account whilst the advantage would be available for purely national mergers.[127]

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[123] Case C-608/17, *Skatteverket v Holmen AB,* EU:C:2019:511, para 33 and Harm van den Broek, Final Losses in Respect of Cross-Border Mergers: Memira (Case C-607/17) and Holmen (Case C-608/17), European Taxation February/March 2020, IBFD, page 61

[124] Case C-608/17, *Skatteverket v Holmen AB,* EU:C:2019:511, para 40

[125] Case C-123/11, *A Oy*, EU:C:2013:84, paras 10-13

[126] Case C-123/11, *A Oy*, EU:C:2013:84, para 15

[127] Case C-123/11, *A Oy*, EU:C:2013:84, paras 29-39 and Terra/Wattel, European Tax Law, Seventh Edition, Wolters Kluwer, p.786

The CJEU also considered the three *Marks & Spencer II* justifications and found the restriction to be justified by all three justifications taken together; balanced allocation of taxing powers, the danger of double use of losses and tax avoidance, taken together. [128]

However, the CJEU did not find the Finnish measures to be proportionate and applied the final losses doctrine and Finland were to allow for cross border loss relief where all possibilities were exhausted by subsidiary or a third party.

Bearing *X Holding* in mind, the CJEU clarified why the final losses doctrine was to be applied in case of *A Oy* and not in *X Holding*. The CJEU noted *"[w]ith respect to the proportionality of the obstacle to freedom of establishment, it must be observed, first, that granting the parent company the possibility of taking into account the losses of its non-resident subsidiary in connection with a cross-border merger is not a priori such as to allow the parent company to choose freely from one year to the next the tax scheme applicable to its subsidiaries' losses (…)"*[129]

Take-away

In *A Oy*[130] the CJEU extended the Marks & Spencer II principle to cross border mergers.

3.4 The development of final losses in CJEU case-law – Foreign branches and permanent establishments

The development of the final losses doctrine continued to evolve in CJEU cases regarding foreign branches starting from *Lidl Belgium* to *Krankenheim Ruhesitz am Wannsee* and *Deutsche Shell*. The development of the final losses doctrine regarding permanent establishments have evolved in the cases *A/S Bevola* and *Timac Agro.* The development of the final losses doctrine in foreign branches and permanent establishments are only briefly touched upon in in this sections (as such is not of major importance for this thesis).

3.4.1 *Lidl Belgium*

Background

[128] Terra/Wattel, European Tax Law, Seventh Edition, Wolters Kluwer, p.787
[129] Case C-123/11, *A Oy*, EU:C:2013:84, para 48 and Enken Cohrs, Unresolved Issues in the ECJ's Case Law on Cross-Border Intra-Group Loss Relief in the Light of A Oy, European Taxation, 2013 (Volume 53), No. 7
[130] Case C-123/11, *A Oy*, EU:C:2013:84

Lidl Belgium[131] concerned a company resident in Germany, whose deduction of losses, incurred by its Luxembourg branch, was disallowed by the Germany.

The CJEU

In delivering its decision, the CJEU followed the three-step approach in *Marks & Spencer II.* First, due to the difference in treatment the CJEU identified a discrimination and a restriction of the freedom of establishment.[132] The CJEU noted, that the tax situation of a company, with its registered office in Germany and a permanent establishment in another Member State, is less favourable as compared to if the permanent establishment would be German. As a result, the German company could be discouraged from carrying on its business through a permanent establishment situated in another Member State.[133] The CJEU found the restriction to be justified, unless the non-resident subsidiary had exhausted the possibilities for taking the losses into account in the Member State, where the losses had been incurred.

In *Lidl Belgium* the CJEU followed the reasoning concluded with regards to non-resident subsidiaries, in *Marks & Spencer II*[134]. Also, the decision clarified that under the Marks & Spencer II requirements, it remains unclarified as to whether the legal or factual possibility, of taking the losses into account, is indeed relevant at all. The CJEU did not touch upon the subject as the losses were both legally and factually the losses may be used in the state where incurred.[135]

3.4.2 *A/S Bevola*

Background

A/S Bevola[136] concerned a company established in Denmark with subsidiaries and permanent establishment outside of Denmark, including a permanent establishment in Finland (that was closed in 2009).[137] The Finnish permanent establishment's losses could not be deducted in

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[131] Case C-414/06, *Lidl Belgium*, EU:C:2008:278

[132] Case C-414/06, *Lidl Belgium*, EU:C:2008:278, para 25 and Terra/Wattel, European Tax Law, Seventh Edition, Wolters Kluwer, p.777

[133] Case C-414/06, *Lidl Belgium*, EU:C:2008:278, para 25

[134] Case C-446/03, *Marks & Spencer II*, EU:C:2005;763

[135] Michael Lang, Has the Case Law of the ECJ on Final Losses Reached the End of the Line?, European Taxation, 2014 (Volume 54), No. 12

[136] Case C-650/16, *A/S Bevola, Jens W. Tricj ApS v Skateministeriet*, EU:C:2018:424

[137] Case C-650/16, *A/S Bevola, Jens W. Tricj ApS v Skateministeriet*, EU:C:2018:424, paras 7-8

Finland, due to which Bevola applied to be able to deduct the losses in Denmark instead.[138] The deduction right was rejected on the grounds that the losses were only deductible if the Bevola ground would have opted for international joint taxation in Denmark.[139]

The CJEU

According to the CJEU Denmark provided for a tax advantage as the losses could be taken into account when calculating a parent company's taxable profit. Where this deduction advantage is always available in a purely domestic situation and not in a cross-border situation, companies could be discouraged from carrying on business activities in another Member State.[140]

A difference in treatment does not constitute a restriction of that freedom if it concerns situations which are not objectively comparable, or if it is justified by an overriding reason in the public interest proportionate to that objective.[141] The CJEU found that the Danish legislation can be justified by overriding reasons in the public interest relating to the balanced allocation of powers of taxation between the Member States, the coherence of the Danish tax system, and the need to prevent the risk of double deduction of losses.[142]

The CJEU came to the conclusion that Danish legislation, "*under which it is not possible for a resident company which has not opted for an international joint taxation scheme, to deduct from its taxable profits losses incurred by a permanent establishment in another Member State, where, first, that company has exhausted the possibilities of deducting those losses available under the law of the Member State in which the establishment is situated and, second, it has ceased to receive any income from that establishment, so that there is no longer any possibility of the losses being taken into account in that Member State, which is for the national court to ascertain.*"[143]

Take-away

A/S Bevola, amongst others, established that the *Marks & Spencer II* final losses doctrine applies also to foreign permanent establishments.

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[138] Case C-650/16, A*/S Bevola, Jens W. Tricj ApS v Skateministeriet*, EU:C:2018:424, paras 8-9
[139] Case C-650/16, *A/S Bevola, Jens W. Tricj ApS v Skateministeriet*, EU:C:2018:424, para 10
[140] Case C-650/16, *A/S Bevola, Jens W. Tricj ApS v Skateministeriet*, EU:C:2018:424
[141] Case C-650/16, *A/S Bevola, Jens W. Tricj ApS v Skateministeriet*, EU:C:2018:424, para 20
[142] Case C-650/16, *A/S Bevola, Jens W. Tricj ApS v Skateministeriet*, EU:C:2018:424, para 53
[143] Case C-650/16, *A/S Bevola, Jens W. Tricj ApS v Skateministeriet*, EU:C:2018:424, para 66

3.5 The definition of final losses as developed in CJEU case-law: summary

In its decisions, the CJEU has accepted the premise that a parent company resident in one Member State does not generally have the possibility to reduce the losses of a subsidiary established in another Member State. The CJEU has thus accepted the exclusion of foreign subsidiaries from the national group tax system, apart from a foreign subsidiary's final losses.

A Member State shall allow a parent company to deduct foreign losses only (*Marks & Spencer II*)

> *"[...] 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, 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 where 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."*[144]

Per the *Marks & Spencer II* ruling, it is clear that the subsidiary may not be able to use the incurred losses not in previous years, in current years nor in future years. The evaluation does not only take into account the subsidiary's possibility to take losses into account but also whether a third party could make use of the incurred losses, either in current or future years.[145]

In *Marks & Spencer III*, the CJEU clarified with this decision that final losses may occur when a subsidiary no longer has any income in the Member State of residence or does not have the possibility, in the future, of having income in that Member State.[146] *Marks & Spencer III* also clarified that losses cannot be characterized as final, only by the fact that the Member State in which the subsidiary is resident precludes all possibility of losses being carried forward.[147]

For the question of how many year's losses may be deemed final is yet to be established, as the evaluation lacks proper standpoints. In *Marks & Spencer III*, in assessing the British

[144] Case C-446/03, *Marks & Spencer II*, EU:C:2005;763, para 55
[145] HE 185/2020 vp
[146] Case C-172/13, Commission v. UK (Marks & Spencer III), EU:C:2015:50, para 36 Terra/Wattel, European Tax Law, Seventh Edition, Wolters Kluwer, p.791
[147] Case C-172/13, Commission v. UK (Marks & Spencer III), EU:C:2015:50, para 33

system, CJEU adopted a starting point that the finality of losses must be assessed immediately after the loss year. However, it is not necessarily clear whether this judgment can be read as to consider that a subsidiary's last year's losses are the only losses that may be deemed final.[148]

Memira Holding clarified that, losses of a subsidiary are not deemed final if there remains a possibility of taking advantage of the losses *economically* by transferring the losses to a third party, the burden of proof that is left to the taxpayer to demonstrate that such is precluded. [149]

Holmen AB clarified that the final losses doctrine may not apply to sub-subsidiaries, unless the intermediary is established in the same Member State as the sub-subsidiary.[150] Also, the fact that the losses of a sub-subsidiary company may not be transferred to a domestic group entity (in the year of liquidation) is not detrimental, "unless the parent company demonstrates that it is impossible for it to deduct those losses by ensuring, in particular by means of a sale, that they are taken into account by a third party for future periods."[151]

[148] HE 185/2020 vp
[149] Case C-607/17, *Skatteverket v Memira Holding AB*, EU:C:2019:510, para 28
[150] Case C-608/17, *Skatteverket v Holmen AB,* EU:C:2019:511, para 33 and Harm van den Broek, Final Losses in Respect of Cross-Border Mergers: Memira (Case C-607/17) and Holmen (Case C-608/17), European Taxation February/March 2020, IBFD, page 61
[151] Case C-608/17, *Skatteverket v Holmen AB,* EU:C:2019:511, para 40

4 THE FINNISH IMPLEMENTATION OF THE FINAL LOSSES DOCTRINE

The final losses doctrine, as developed in CJEU case-law, has naturally also been implemented in Finland, and Finland has had to take the developments into account in its national matters. However, Finland has not seemed to be too eager to implement national measures implementing the final losses doctrine, until the EC reminded Finland with infringement proceedings concerning the group contribution scheme. Prior to the infringement proceedings and the legislative change stemming from the infringement proceedings, the final losses doctrine has developed in Finnish case-law. Due to the EC's infringement proceedings against Finland, the final losses doctrine started to develop in Finnish law regarding group contribution. We are yet to see any developments in the case of cross-border mergers, but it is not excluded that such development will be seen in the near future.

This chapter will provide for an understanding of the implementation of the final losses doctrine in the field of group contribution, the final losses development with regards to cross-border mergers and any issues stemming from the current Finnish view of such (burden of proof and a claim to the EC).

4.1 The Finnish group contribution scheme and final losses

4.1.1 *The Finnish group contribution system in a nutshell*

Companies may do business through several companies that belong to the same group. In Finland, companies are not consolidated for corporate income tax purposes, but a group contribution scheme is used. Group companies may, so to say, even out their taxable profits and losses, which effectively leads to the same result, should consolidation have been used. Group contribution is a deductible cost for the granting company and taxable income for the receiving company, provided that all the requirements in the Act on Group Contribution[152] is met.

Based on the Act on Group Contribution, both the granter and the received should belong to a group, whereas there is a direct or indirect common ownership of at least 90%.[153] In other words, in a direct ownership situation, the parent company owns at least 90% of the subsidiary. In an indirect ownership situation, the parent company, together with one or several

[152] Laki konserniavustuksesta verotuksessa, 21.11.1986/825
[153] Laki konserniavustuksesta verotuksessa, 21.11.1986/825, Section 3

subsidiary's own at least 90% of the receiver of group contribution. Additionally, this 90% ownership needs to be in force for at last one entire fiscal year.[154]

Based on Finnish case law, the ownership may be traced via foreign entities, on condition that a tax treaty between Finland and the country, wherein the parent for the group is resident in, is in force.

Furthermore, both companies need to be resident in Finland for tax purposes (see more Section 3.3 for more deliberations on the domestic requirement) and need to be either limited liability companies or co-operatives conducting business activities. This means that they need to have income belonging to the business income basket (Fin: *EVL-tulo*). The entities may however not be financial, insurance, or pension institutions.

The group contribution needs to be recorded in the annual statutory accounts of both the receiving and the giving company and should have an effect on the company's annual net income.[155]

The additional requirements are that both companies fiscal period need to end at the same date[156], that the group contribution does not exceed the taxable business income of such granting company[157] (i.e. hence naturally not possible for loss-making group contribution grantors) and that the contribution may not be considered a capital investment of the giver to the receiver.[158]

4.1.2 *Finnish case-law concerning final losses and group contribution*

4.1.2.1 KHO:2020:36

In April 2020, the Finnish Supreme Administrative Court issues a decision (KHO:2020:36)[159] concerning final losses and cross-border group contribution. The case concerned a Finnish parent company that contemplated to give group contribution to its wholly owned Swedish

[154] Laki konserniavustuksesta verotuksessa, 21.11.1986/825, Section 7 and Verohallinnon ohje, Konserniavustus, dated 1.1.2021 number VH/8085/00.01.00/2020
[155] Verohallinnon ohje, Konserniavustus, dated 1.1.2021 number VH/8085/00.01.00/2020
[156] Laki konserniavustuksesta verotuksessa, 21.11.1986/825, Section 7
[157] Laki konserniavustuksesta verotuksessa, 21.11.1986/825, Section 6
[158] Laki konserniavustuksesta verotuksessa, 21.11.1986/825, Section 2
[159] Supreme Administrative Court of Finland, KHO:2020:36, 2 April 2020, ECLI:FI:KHO:2020:36

subsidiary in 2019. The idea was to use the group contribution received by the Finnish parent against the Swedish subsidiary's losses incurred in years 2001-2003 and 2008.[160]

The issue at stake was whether the group contribution was deductible for the Finnish parent for Finnish tax purposes, despite the fact that the Finnish legislation, at the time, required both the receiving and giving companies to be Finnish resident entities, as such would not be in accordance with EU law and the freedom of establishment.[161] The Finnish parent company found that the group contribution should be deductible in Finland, as the Swedish subsidiary's losses should be seen final.

The Supreme Administrative Court in its decision did not take a stance on the finality of the losses nor on its relevance for the deductibility of group contribution, as the statute of limitation of the losses had ended already in a purely domestic situation. In other words, in a comparable Finnish situation (with only Finnish companies) the losses would not have been deductible against group contribution, according to Finnish national law. As the case concerned cross-border group contribution, the parent company as stake were not worse off as compared to a similar domestic situation.[162]

The Supreme Administrative Court did however touch upon the subject of group contribution in a cross-border situation being deductible for Finnish purposes, in case of final losses. In its decision, the Supreme Administrative Court referred to *Marks & Spencer II* and *Holmen AB* and noted that group contribution given to a foreign subsidiary is not deductible for Finnish tax purposes, unless group contribution is given to cover final losses of the foreign subsidiary.[163]

The Supreme Administrative Court's decision should be in line with EU law, as the group contribution systems of Member States are not harmonized on an EU level. Thus, Member States do not need to eliminate the tax disadvantage caused by the fact that Finland's tax system does not recognize the tax benefits provided by another Member State. In the case at hand, the statute of limitation of losses seemed to be longer in Sweden than in Finland, but

[160] Verohallinnon ohje, Konserniavustus, dated 1.1.2021 number VH/8085/00.01.00/202
[161] Supreme Administrative Court of Finland – KHO:2020:36, 2 April 2020, ECLI:FI:KHO:2020:36
[162] Supreme Administrative Court of Finland – KHO:2020:36, 2 April 2020, ECLI:FI:KHO:2020:36
and Cross-Border Group Contribution, Freedom of Establishment and Final Losses, European Taxation 2021 (Volume 61), Marjaana Helminen, published 12 January 2021.
[163] Cross-Border Group Contribution, Freedom of Establishment and Final Losses, European Taxation 2021 (Volume 61), Marjaana Helminen, published 12 January 2021.

this did not require Finland to carry forward losses of the foreign Swedish subsidiary, even if such losses would have been deemed final.[164] This standpoint had been established already in *A Oy*[165], where the CJEU noted that denying the deductibility of losses in a cross-border merger does not restrict EU law and the freedom of establishment, should the losses be non-deductible in a comparable domestic Finnish situation.

In other words, as the tax system of Finland includes a time limit on the carry forward of losses (generally 10 years), such time limit does not need to be extended only in order to enable foreign losses to be deductible for Finnish tax purposes, by way of cross-border group contribution. Where expired losses are unable to be set off against group contribution, in a purely domestic Finnish situation, Finland does not treat a cross-border situation worse than a comparable domestic situation, and hence does not restrict the freedom of establishment.[166]

4.1.2.2 Central Tax Board, KVL 2018/23

In the Finnish Central Tax Board's case, KVL 2018/23[167], the Central Tax Board also avoided the determining of final losses. In KVL 2018/23, a Finnish company were to give group contribution to its loss-making foreign company, both having a common parent company in a third Member state. In its decision, the Central Tax Board noted that, as the Finnish company, that were to give group contribution, did not make use of its freedom of establishment in a third Member State, the CJEU's case law concerning the finality of losses were not applicable to the case at hand, and the Central Tax Board did not need to assess the finality of the losses.[168]

The Central Tax Board did not give relevance to the fact that the entities common parent had established in Finland and in the sister company's state. This seems to be a logic standing as the CJEU's case law concerning final losses rather concerns situations in which a parent company has established itself in another Member State by way of a subsidiary or a permanent

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[164] Cross-Border Group Contribution, Freedom of Establishment and Final Losses, European Taxation 2021 (Volume 61), Marjaana Helminen, published 12 January 2021.
[165] Case C-123/11, *A Oy,* EU:C:2013:84, paras 36 -37
[166] Cross-Border Group Contribution, Freedom of Establishment and Final Losses, European Taxation 2021 (Volume 61), Marjaana Helminen, published 12 January 2021.
[167] Central Tax Board, 4 May 2018, KVL 2018/23
[168] Central Tax Board, 4 May 2018, KVL 2018/23 and Cross-Border Group Contribution, Freedom of Establishment and Final Losses, European Taxation 2021 (Volume 61), Marjaana Helminen, published 12 January 2021.

establishment.[169] This approach seems justified as it is primarily the responsibility of the parent company state to take into account final losses of a subsidiary. However, the Finnish group contribution scheme allows for group contribution to be paid between sister companies as well, whereas (where an actual payment has been made) group contribution between sister companies could fall in the scope of the free movement of capital (TFEU).[170]

4.1.3 *Contradictory Finnish and Swedish decisions with regards to group contribution*

The unclear reasoning of the CJEU in both *Marks & Spencer II* and *Oy AA* lead to contradictory national interpretations of the final losses doctrine in Finland and Sweden.

The CJEU did not deal with whether the final losses doctrine would apply to other group contribution schemes, than the UK group contribution scheme, which considers the transfer of losses and not profits (as the Finnish group contribution scheme.) In other words, the Finnish group contribution system is a mirror of the UK group contribution scheme, whereas Finland transfers profits to group companies whilst the UK transfers losses to group companies. The CJEU did not take a stand on the final losses doctrine Oy AA, which might result from the fact that profits would have been transferred from a profit-making subsidiary to a loss-making parent company and the losses incurred does not seem to be final, as in the *Marks & Spencer II* case.[171] This non-finality of the incurred losses was also noted by Advocate General Kokott in her Opinion:

> *"However, on the information the reference for a preliminary ruling gives as to the facts, it does not appear that Oy AA is in an exceptional situation corresponding to that in Marks & Spencer. It follows that there is no cause to consider whether, by way of exception, the principle of proportionality requires a divergence from the allocation of powers to impose taxes."*[172]

Due to the unclarity of the application of the final losses doctrine, Finland and Sweden gave contradictory decisions in similar matters. The Supreme Administrative Court of Finland in

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[169] Central Tax Board, 4 May 2018, KVL 2018/23 and Cross-Border Group Contribution, Freedom of Establishment and Final Losses, European Taxation 2021 (Volume 61), Marjaana Helminen, published 12 January 2021

[170] Cross-Border Group Contribution, Freedom of Establishment and Final Losses, European Taxation 2021 (Volume 61), Marjaana Helminen, published 12 January 2021 and Marjaana Helminen, EU Tax Law – Direct Taxation, Section 2.2.6 IBFD

[171] Dennis Weber and Bruno da Silva, From Marks & Spencer to X Holding, The Future of Cross-Border Group Taxation, Wolter Kluwer, 2011, p.12

[172] Opinion of Advocate General Kokott, Case C-231/05, delivered on 12 September 2006, para 71

its decision KHO 2007/92[173] took the stand that the intra-group transfer of profits is not a deductible expense for Finnish tax purposes, in cross-border situations, even when the loss is considered final. The Finnish Supreme Administrative Court found the difference between the Finnish and the UK group contribution schemes of importance for justifying for why the final losses doctrine would not apply in the case at hand.[174]

As opposed to the Finnish Supreme Administrative Court's decision, the Swedish Supreme Administrative Court, in its decision[175], came to an opposite outcome and concluded that a Swedish parent company may deduct losses incurred by a subsidiary resident in another Member State, provided that such losses are considered final.

The Swedish Supreme Administrative Court was here confronted with a situation where a Swedish parent company contemplated to make a contribution to two foreign subsidiaries, where one was in liquidation and the other one had losses expiring in time (the end of the stature of limitation). The Swedish Supreme Administrative Court considered that final losses only referred to losses arising from the liquidation of the foreign subsidiary and hence did not accept final losses to exist due to the end of the stature of limitation. The finality of losses was also only accepted where a parent would contribute to a subsidiary, which had incurred final losses. Hence, the contribution to a foreign sister company or to a foreign parent company, were not accepted.[176]

4.1.4 *The EC's infringement proceeding regarding final losses and cross-border group contribution*

The EC initiated an infringement proceeding against Finland in May 2019, concerning the tax deductibility of group contribution in a cross-border situation. The letter of formal notice, sent by the EC to the Finnish Government was the first step in the infringement proceedings.[177] After the letter of formal notice, the EC concluded that Finland failed to fulfil its obligation under EU law, and that Finland had not remedied the tax treatment of group contribution in a

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[173] KHO 2007/92 31.12.2007/3378
[174] Dennis Weber and Bruno da Silva, From Marks & Spencer to X Holding, The Future of Cross-Border Group Taxation, Wolter Kluwer, 2011, p.12
[175] Supreme Administrative Court of Sweden, Gambro AB, decision date 11 March 2009, decision number 6511-06
[176] Dennis Weber and Bruno da Silva, From Marks & Spencer to X Holding, The Future of Cross-Border Group Taxation, Wolter Kluwer, 2011, p.13
[177] European Commission – Infringement Procedure (Accessed: https://ec.europa.eu/info/law/law-making-process/applying-eu-law/infringement-procedure_en, 23 January 2021).

cross-border situation, due to which the EC sent a reasoned opinion to Finland, requesting Finland to bring its rules on tax deductibility of group contribution in line with EU law. The reasoned opinion is the second step in the EC's infringement proceedings.

In its publication[178], the EC notes

> *"group contributions made to affiliated companies in other EU/EEA States are not deductible even in situations where these cover definitive losses incurred by the latter. The lack of deductibility in such situations constitutes a restriction on the freedom of establishment (Article 49 TFEU and Article 31 EEA). If Finland does not provide a tangible proposal to remedy the infringement within the next four months, the Commission may decide to bring the case before the Court of Justice of the EU."*[179]

The third step of the EC's infringement proceedings would thus have been a potential referral to the CJEU.

4.1.5 *Finland's response to the EC's infringement proceedings and the future of the group contribution scheme*

In light of CJEU case-law, the EC is correct, the Finnish group contribution system should cover (deductibility of group contribution) final losses of a foreign subsidiary. In response to the EC's infringement proceedings, Finland set up a working group on 31 October 2019 (VM163:00/2019), with the intention to review the need to amend the Finnish group contribution scheme and the tax treatment of final losses for Finnish tax purposes.[180] However, Finland did not have time to wait for the findings of such working group, as the working group's mandate ends 31 December 2021. Thus, the filings are yet to be published.[181]

However, due to the EC's infringement proceedings, the issue at hand had to be solved quicker, due to which, on 19 September 2020, the Ministry of Finance of Finland issued a draft government proposal for a law concerning group deduction of final losses within the

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[178] European Commission – May Infringements Package – Key decisions 14 May 2020(Accessed: https://ec.europa.eu/commission/presscorner/detail/en/inf_20_859).
[179] European Commission – May Infringements Package – Key decisions 14 May 2020(Accessed: https://ec.europa.eu/commission/presscorner/detail/en/inf_20_859).
[180] VM163:00/2019
[181] Marjaana Helminen, Rajat ylittävä konserniavustus, vapaa sijoittautumisoikeus ja lopulliset tappiot – aika ottaa seuraava askel kohti lisääntyvää konserniajattelua, Verotus lehti 5/2020.

EEA. However, 22 October 2020, a government proposal (HE 185/2020 vp) was issued by the Parliament in this regard, whereas the Act on Group Deduction was initiated. [182]

According the government proposal (HE 185/2020 vp), a Finnish parent company may, as of 2021, deduct the amount of so-called final losses of its foreign EU/EEA resident subsidiary in Finland, by a so-called group deduction. This would result in the fact that such group deduction of a foreign EU/EEA resident subsidiary's final losses, would be considered as a deductible expense for the Finnish parent company's taxation in Finland, should the losses be deemed final, as in accordance with EU case-law.[183]

A group deduction of such a foreign EU/EEA resident subsidiary's final losses would however only be possible between limited liability companies and/or co-operatives and only between a Finnish parent company and such foreign EU/EEA resident subsidiary, where the parent company's direct ownership of the foreign EU/EEA resident subsidiary is at least 90% (the same conditions as in a purely domestic situation).[184]

Furthermore, as with group contribution, group deduction would not be available for banks, insurance companies or pension institutions.

Group contribution requires that the transferring affiliated entity, also effectively transfers the assets to the recipient affiliated entity either by paying the contribution or by recording it as a liability and as a receivable. Group contribution also requires that the corresponding expense and income are recorded for the receiving and transferring entity's accounting purposes. Such conditions are ill-suited to a situation where the recipient of group contribution would be a foreign subsidiary and in case of final losses. The government proposal hence proposes that the final losses of a foreign EU/EEA resident subsidiary should not be taken into account through group contribution but should be taken into account as a separate deduction, known as a group deduction.[185]

[182] Marjaana Helminen, Rajat ylittävä konserniavustus, vapaa sijoittautumisoikeus ja lopulliset tappiot – aika ottaa seuraava askel kohti lisääntyvää konserniajattelua, Verotus lehti 5/2020.

[183] EUDTG Newsletter Issue 2020 – nr. 006, September – October 2020 (written by the Author of this thesis) and (SAC:185:2020 vp)

[184] HE 185/2020 vp and Laki Euroopan talousalueella sijaitsevan tytäryhtiön lopullisen tappion konsernivähennyksestä, 1198/2020

[185] EUDTG Newsletter Issue 2020 – nr. 006, September – October 2020 (written by the Author of this thesis) and (SAC:185:2020 vp)

According to the government proposal, the definition of final losses would correspond to the definitions set out in the CJEU decision *Marks & Spencer II*, and such subsequent EU case-law. According to the government proposal, final losses are to entail losses, that cannot be taken into account in the foreign EU/EEA resident subsidiary's state of residency in also future periods either by such foreign subsidiary itself or by a third party. A prerequisite would be, amongst others, that the subsidiary's business operations are terminated, and that the subsidiary is dissolved. Furthermore, the final losses need to exist in accordance with the laws of the foreign EU/EEA resident subsidiary (i.e. cannot be time barred). [186]

The parent company would also have the burden of proof that the losses of the foreign EU/EEA resident subsidiary are in fact final, within the meaning of the applicable EU case-law.[187]

The amount deducted would be calculated on the basis of the amount of the foreign EU/EEA resident subsidiary's final losses and is to be calculated according to the time of the last whole financial year and at the time when the foreign EU/EEA resident subsidiary is dissolved. The amount would be calculated for both aforementioned dates, in accordance with the laws of the state of residency of the foreign EU/EEA resident subsidiary and the Finnish Business Income Tax Act. [188] The amount of final losses would be considered to be the lower of the two aforementioned calculated amounts.[189]

The deduction would take place during the financial year when the foreign EU/EEA resident subsidiary is dissolved. The proposed act and changes entered into force on 1 January 2021.

4.1.6 *Analysis of the Group Deduction Act*

The proposed changes are an effort to bring the Finnish law in accordance with EU law and case-law, with regards to cross-border EU/EEA group contribution (and to avoid been taken to court by the EC, as the third step of the infringement proceedings). Finland chose to deal with the issue of group contribution rather than solving the final losses challenges, as defined

[186] EUDTG Newsletter Issue 2020 – nr. 006, September – October 2020 (written by the Author of this thesis) and (SAC:185:2020 vp) and Laki Euroopan talousalueella sijaitsevan tytäryhtiön lopullisen tappion konsernivähennyksestä, 1198/2020, section 5

[187] Laki Euroopan talousalueella sijaitsevan tytäryhtiön lopullisen tappion konsernivähennyksestä, 1198/2020, section 5

[188] Laki elinkeinotulon verottamisesta, 24.6.1968/360

[189] Laki Euroopan talousalueella sijaitsevan tytäryhtiön lopullisen tappion konsernivähennyksestä, 1198/2020, section 8, EUDTG Newsletter Issue 2020 – nr. 006, September – October 2020 (written by the Author of this thesis) and (SAC:185:2020 vp)

in EU law (an issue that would extend beyond group contribution to cross-border mergers and final losses therein). It seems like Finland wanted, at least at this stage, to do the bare minimum.

The Ministry of Finance ended up taking the chosen route, as such is less problematic in cross-border situations, as the deduction does not require an actual transfer of funds and corresponding income and expense for accounting purposes. The grant of group contribution would record income and assets for the loss-making subsidiary, whereas the subsidiary's losses would not be deemed final any longer.[190] The decision of using the group deduction regime was likely also influenced by the fact that Sweden has applied a group deduction regime for subsidiaries, resident within the EEA and their final losses, as of 2010, alongside their group contribution regime.[191] A particular group deduction regime is also more justified than a mere deduction of the final losses, as the group deduction may be adjusted in order for such to behave, in accounting, in the same manner as group contribution. [192]

The application of different systems for national and cross-border activities is justified and not in breach of EU law, provided that the different systems do not lead to a worse treatment of the cross-border situation as compared to a purely national situation. This is ensured by the government proposal by allowing the Finnish resident parent company to issue a group deduction for the subsidiary's final losses based on the same conditions and for the same maximum amount, as such Finnish resident parent company would have been able to give in a purely domestic situation (in a group contribution situation), apart from the fact that group deduction only need to be granted in case of final losses.[193]

For example, the Finnish group deduction law would apply to those corporations and cooperatives, that may be grantor or recipients of group contribution, as per the Group Contribution Act. Furthermore, in accordance with the Group Contribution Act, the parent company should own the subsidiary's share capital or shares directly 90%. As in accordance with CJEU case-law, should there be an entity between the parent company and the foreign subsidiary, and such intermediary entity is in the same state as the foreign subsidiary, such

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[190] Marjaana Helminen, Rajat ylittävä konserniavustus, vapaa sijoittautumisoikeus ja lopulliset tappiot – aika ottaa seuraava askel kohti lisääntyvää konserniajattelua, Verotus lehti 5/2020
[191] Cross-Border Group Contribution, Freedom of Establishment and Final Losses, European Taxation 2021 (Volume 61), Marjaana Helminen, published 12 January 2021.
[192] Cross-Border Group Contribution, Freedom of Establishment and Final Losses, European Taxation 2021 (Volume 61), Marjaana Helminen, published 12 January 2021.
[193] Marjaana Helminen, Rajat ylittävä konserniavustus, vapaa sijoittautumisoikeus ja lopulliset tappiot – aika ottaa seuraava askel kohti lisääntyvää konserniajattelua, Verotus lehti 5/2020

indirect ownership would also be taken into account for the purposes of group deduction (as in *Holmen AB*). In line with the Act on Group Contribution, group deduction would not be applicable for banks, insurance companies or pension institutions. The parent company would also only be able to deduct a maximum of the parent company's taxable income for the fiscal year in question, in the same manner as per the Act on Group Contribution.

The freedom of establishment principle also requires that group deduction is also enabled between a Finnish entity's foreign permanent establishment. The taxation of a EU/EEA permanent establishment of a Finnish parent may not be more severe than the taxation of a Finnish resident entity.[194] This is argued to be a fulfilment of the minimum requirements, set out by EU law, but also from the fact that the group deduction regime would lead to a better end result in a purely domestic situation. [195]

It is also, to some extent, left unclear whether group deduction should be allowed between sister companies, as such may be given in a purely domestic situation as per the Act on Group Contribution. However, it is worth noting that Finland's effort regarding the Act on Group Deduction is an effort to avoid court proceedings due to the EC's infringement proceedings and is as such a mere *de minimi* correction. Thus, the government proposal and the corresponding Act only ensures that group deduction is granted for only in those EEA resident subsidiaries and for such final losses, only up to the amount as required by CJEU case-law. The Act on Group Deduction is not intended to enable equalization of profits between group companies, in a broader sense, and is not intended to resolve other problems related to group taxation.[196]

The wider reform of the Finnish group contribution regime, and the deduction of final losses in a cross-border merger, is left to be reflected and dealt with by the working group set up by the Ministry of Finance in 2019. As noted, it is expected that the working group would deliver their findings around the end of 2021, when the mandate ends. For example, it will be

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[194] Marjaana Helminen, Rajat ylittävä konserniavustus, vapaa sijoittautumisoikeus ja lopulliset tappiot – aika ottaa seuraava askel kohti lisääntyvää konserniajattelua, Verotus lehti 5/2020

[195] Marjaana Helminen, Rajat ylittävä konserniavustus, vapaa sijoittautumisoikeus ja lopulliset tappiot – aika ottaa seuraava askel kohti lisääntyvää konserniajattelua, Verotus lehti 5/2020

[196] Marjaana Helminen, Rajat ylittävä konserniavustus, vapaa sijoittautumisoikeus ja lopulliset tappiot – aika ottaa seuraava askel kohti lisääntyvää konserniajattelua, Verotus lehti 5/2020

necessary to legislate the deductibility of final losses in case of a cross-border merger, even though such is already enabled by CJEU case-law.

To highlight the issue with the deduction of final losses in a cross-border merger, the Finnish Supreme Administrative Court issued five judgments, in May 2020, where the question concerned the right of a Finnish parent to utilize the tax losses of its EU resident subsidiary, upon a cross-border upstream merger. In brief, the Supreme Administrative Court ruled in all five cases that the Finnish parent company had not demonstrated that the criteria for finality of the subsidiary's tax losses were met, despite such criteria being considered met in all five cases by the previous instances and court. Hence, in light of the Supreme Administrative Court's five judgements, the bar regarding the fulfilment of criteria for the finality of tax losses was set very high, if not almost impossibly high.

It furthermore remains to be seen how the final losses doctrine will evolve in national law, as the government proposal for the Act on Group Deduction specifically states that the Finnish interpretation of final losses would follow the interpretation taken in EU case-law. As EU case-law yet leaves certain facts unsolved/unanalysed, it remains to be seen how and in which direction the Finnish national law will evolve. Hence, future CJEU case-law forming the final losses doctrine will play a key role in interpreting the new law on the Act of Group Deduction.

Reflecting back on the Supreme Administrative Court's case KHO 2020:36, group deduction would only be applicable in case the losses are deemed final and that the losses would be deductible in a corresponding Finnish domestic situation. Hence, the statute of limitation of the losses may not have ended, as per Finnish national law, and a change of ownership would prevent the deduction of such losses (with certain exceptions relating to a special permit to deduct losses despite an ownership change).

Also, the extremely high threshold for the finality of losses may be justified (see however below for thoughts on the level of burden of proof), from an EU law perspective, by the prevention of abuse, as it is not intended to allow for groups to plan the use of losses where the taxation is the most burdensome nor the use of losses that already would have exceeded the statute of limitation in a purely domestic situation. Lastly, artificial arrangements, set up

in order to apply the Finnish group deduction regime, could also be tackled with Section 28 of the Finnish Act on Tax Procedure.[197]

4.2 Final losses in a cross-border merger

4.2.1 *Background regarding final losses in a cross-border merger*

The EU Merger Directive's[198] aim is to remove fiscal barriers to cross-border reorganizations, that involve entities situated in two or more EU Member States, without jeopardizing the fiscal interest of each Member State. The outcome of the EU Merger's Directive is to attain the aforementioned objective by implementing cross-border reorganizations, such that fulfil the requirements in the Merger Directive, without adverse tax implications for the entities involved in the reorganization nor their shareholders.[199] In Finland, the Mergers Directive have been implemented into the Finnish Business Act, Sections 52-52h.[200]

Cross-border reorganizations have however been discouraged by the fact that no company law rules exist for cross-border mergers and divisions. This however changed already in 2007 when Finland changed (by way of 1415/2007) the Limited Liability Companies Act[201] to include provisions concerning cross-border mergers and divisions.[202] Cross- border transfers of assets and exchanges of shares have however practically been possible since 1995.[203]

In Finland, the transfer of assets (*Fin: liiketoimintasiirto*) and the exchange of shares (Fin: *osakevaihto*) are not transactions where losses are transferred from one entity to another.[204] However, in mergers and divisions, losses are transferred to the receiving entity when fulfilling the preconditions set out by Finnish national law.[205] In Finnish national law, cross-border mergers and divisions have not been put into a different light, as compared to purely

[197] Laki verotusmenettelystä, 18.12.1995/1558, Section 28
[198] Council Directive 2009/133/EC of 19 October 2009 on the common system of taxation applicable to mergers, divisions, partial divisions, transfers of assets and exchanges of shares concerning companies of different Member States and to the transfer of the registered office of an SE or SCE between Member States OJ L 310, 25.11.2009
[199] Council Directive 2009/133/EC of 19 October 2009 on the common system of taxation applicable to mergers, divisions, partial divisions, transfers of assets and exchanges of shares concerning companies of different Member States and to the transfer of the registered office of an SE or SCE between Member States OJ L 310, 25.11.2009
[200] Laki elinkeinotulon verottamisesta, 24.6.1968/360, 52-52h §
[201] Osakeyhtiölaki, 21.7.2006/624
[202] Seppo Penttilä, Lopulliset tappiot – lopullinen ongelma? Verotuslehti 5/2009.
[203] Seppo Penttilä, Lopulliset tappiot – lopullinen ongelma? Verotuslehti 5/2009, p. 468
[204] Seppo Penttilä, Lopulliset tappiot – lopullinen ongelma? Verotuslehti 5/2009
[205] Tuloverolaki, 30.12.1992/1535

domestic mergers and divisions, with the result that it has become unclear as to when losses are transferred in cross-border mergers and divisions. [206]

The EU Merger's Directive also only to a limited extent regulates the transferring of losses in a reorganization falling inside the scope of application of the Directive. The only article in the EU Merger's Directive dealing with the transfer of losses is Article 6, which precludes that

> *"to the extent that (...) the Member State would apply provisions allowing the receiving company to takeover the losses of the transferring company which had not yet been exhausted for tax purposes, it shall extend those provisions to cover the takeover of such losses by the receiving company's permanent establishments situated within its territory."*[207]

Article 6 of the EU Merger's Directive is of relevance for Finnish mergers and divisions, as if a Finnish entity merges with another entity, situated in another EU Member State, a permanent establishment is usually created in Finland (with certain exceptions). Hence, the losses are to be transferred to such Finnish permanent establishment by way of the same prerequisites as such would be transferred to a Finnish limited liability company.[208] Also, Finnish national law does not take the loss equalisation into account in cross-border mergers and divisions.

4.2.2 *Finnish domestic rules regarding cross-border mergers*

When a Finnish limited liability company merges with another company in another EU Member State or a company in an EEA state, Section 52 of the Finnish Business Income Tax Act[209] is applied. Should assets be left affiliated in Finland, a permanent establishment is created, as per Section 52e paragraph 1 of the Finnish Business Income Tax Act. The principle of continuity is applied to both the merging and the receiving entities and in no revenue recognition is taking place in the merging entities' accounting.[210] On the other hand, the

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[206] Seppo Penttilä, Lopulliset tappiot – lopullinen ongelma? Verotuslehti 5/2009, p. 468
[207] Council Directive 2009/133/EC of 19 October 2009 on the common system of taxation applicable to mergers, divisions, partial divisions, transfers of assets and exchanges of shares concerning companies of different Member States and to the transfer of the registered office of an SE or SCE between Member States OJ L 310, 25.11.2009, Article 6.
[208] Prof. Seppo Penttilä, Lopulliset tappiot – lopullinen ongelma? Verotuslehti 5/2009, p. 468
[209] Laki elinkeinotulon verottamisesta, 24.6.1968/360
[210] Prof. Seppo Penttilä, Lopulliset tappiot – lopullinen ongelma? Verotuslehti 5/2009, p. 469

receiving entity creates a permanent establishment in Finland, the acquisition cost of which is the undepreciated acquisition cost (fin: *poistamaton hankintameno*) of the merging company.

If a permanent establishment is not created for the receiving entity in Finland, the tax implications are based on Section 52e paragraph 2 of the Finnish Business Income Tax Act. Based on Section 52e paragraph 2, the exit value less the undepreciated acquisition cost is considered taxable income.[211]

4.2.3 *Finnish case-law regarding cross-border mergers and the deduction of final losses*

Articles 49 and 54 of the TFEU have not been considered to require that the losses of a merging entity into a Finnish parent, should be deducted in Finland, unless the losses of such merging entity is considered final, within the meaning of EU case-law. The assessment of whether losses are deemed final are made based on a case-by-case analysis and according to the relevant Finnish Tax Administration's guidance on mergers, currently at least the following EU case-law is regarded as relevant for the assessment of finality of losses: CJEU C-446/03 (*Marks & Spencer II)*, CJEU C-123/11 (*A Oy*), CJEU C-172/13 (*Commission v United Kingdom*) and CJEU C-607/17 (*Memira Holding*) and the Finnish Supreme Administrative Court's decisions SAC:2013:155, SAC:2020:36 and SAC:2020:5.[212]

KHO:2013:155

In KHO:2013:155[213], the case concerned whether a Finnish parent company may deduct its foreign subsidiaries losses, by way of the same conditions as in a corresponding domestic Finnish merger. KHO:2013:155 is based on the CJEU's preliminary ruling *A Oy*[214]. In its ruling, the Supreme Administrative Court ruled that A Oy (as the Finnish parent company) could deduct the confirmed losses, incurred by the Swedish merging entity, should A Oy demonstrate that the Swedish merging subsidiary have exhausted the possibilities to take the losses into account and that there was no possibility that either the Swedish merging subsidiary itself or a third party could take such losses into account in Sweden.[215] The deduction of the

[211] Laki elinkeinotulon verottamisesta, 24.6.1968/360, 52e, paragraph 2
[212] Yritysjärjestelyt ja verotus – sulautuminen, VH/8356/00.01.00/2020, 16.12.2020
[213] KHO:2013:155, ECLI:FI:KHO:2013:155
[214] CJEU C-123/11, *A Oy*
[215] Yritysjärjestelyt ja verotus – sulautuminen, VH/8356/00.01.00/2020, 16.12.2020: *"Päätöksessä korkein hallinto-oikeus katsoi, että A Oy sai vähentää siihen sulautuvalle ruotsalaiselle tytäryhtiölle vahvistetut tappiot, jos A Oy näytti toteen, että tytäryhtiö oli käyttänyt loppuun mahdollisuudet kyseisten tappioiden huomioon ottamiseksi, eikä ollut mahdollisuutta siihen, että joko tytäryhtiö itse tai kolmas osapuoli saisi ottaa ne huomioon Ruotsissa."*

losses also required that the losses would be deductible in a similar purely domestic situation. The losses were also to be calculated in accordance with the Finnish Business Tax Act (being the business income basket).

In its decision, the Supreme Administrative Court stated that it had not resolved the question whether the conditions for the deduction of the losses of the merged Swedish subsidiary, by the Finnish parent, had met the general conditions as set out by Finnish tax law, which must be assessed in the light of the nature of the company's operations, previous changes of ownership and other factors. KHO:2013:155 therefore did not fully resolve the question of whether the Finnish parent company could deduct the losses of its Swedish merging subsidiary.[216]

KHO:2020:51 and four other non-published Supreme Administrative Court's case-law issued in May 2020[217]

The utilizing of a foreign subsidiary's final tax losses in Finnish tax assessment has gained additional attention, as the Supreme Administrative Court issued five judgements on 15 May 2020 in this regard. One of the five cases is the precedent case KHO:2020:51 and the rest are unpublished cases by the Supreme Administrative Court (the author has read also the unpublished decisions). [218]

In all the five cases the question concerned the right of a Finnish parent to utilize the tax losses of its EU resident subsidiary, upon a cross-border upstream merger. In other words, the Supreme Administrative Court assessed whether the condition of finality, as in accordance with the CJEU's case-law, was met in the five situations at hand, and hence whether the Finnish parent could deduct the foreign tax losses for Finnish tax purposes.

More specifically about KHO:2020:51[219], the case concerned a Latvian subsidiary A AS, that was the subsidiary of the Finnish entity A Oy. The business of A AS had been terminated and the intention was to merge Latvia A AS into the parent company A Oy. Per the merger plan, the assets of Latvia A AS exceeded the liabilities of the entity. The sale of A AS to a third

[216] KHO:2013:155, ECLI:FI:KHO:2013:155 and Ahonen, Pykönen, Salmikivi, Tappioiden lopullisuudesta ja vähentämisestä rajat ylittävässä yritysjärjestelytilanteessa, Verotuslehti 5/2016.
[217] The text was also published by the EUDTG Newsletter May-June 2020 and written by this author.
[218] Supreme Administrative Court, 682/2/19 t 2105, 15 May 2020, Supreme Administrative Court, 681/2/19 t 2104, 15 May 2020, Supreme Administrative Court, 4470/2/18 t 2106, 15 May 2020, Supreme Administrative Court, 6050/2/18 t 2107, 15 May 2020.
[219] KHO:2020:51, 15 May 2020, ECLI:FI:KHO:2020:51

party was not considered a concrete option within the group. Also, Latvian tax law had restrictions on the deduction losses of an entity the ownership of which is changed and especially in case of a merging entity that is loss-making. [220]

The Supreme Administrative Court stated that, on the basis of the case-law of the CJEU, A Oy had to prove that A AS had exhausted all the possibilities available in Latvia to take such losses into account.

The Supreme Administrative Court ruled in all five cases that the Finnish parent company had not demonstrated that the criteria for finality of the subsidiary's tax losses were met, despite such criteria being considered met in all five cases by the previous domestic court. In KHO:2020:51, the Supreme Administrative Court ruled that in view of A AS's statement of assets, A Oy had not shown that A AS could not have received even a small amount of financial or other income in Latvia in the coming years. Nor had A Oy shown that there was no possibility that a third party, in the event of A AS being sold to it, could take A AS's losses into account in Latvia in future tax years. As a result, A Oy could not deduct A AS's losses for Finnish tax purposes following the merger.

The Supreme Administrative Court's rulings for all five cases dealt with the following two main themes:

First, according to the Supreme Administrative Court's rulings, the subsidiary's losses may not be deemed final in case the subsidiary receives income, no matter how minor, as there in such cases exists a possibility that the losses could be deducted in the subsidiary's jurisdiction of residence in future years. According to the Supreme Administrative Court's rulings, it had not been demonstrated that the subsidiary could not receive minor financial or other income in its jurisdiction of residence, during future years.

Second, according to the Supreme Administrative Court, the finality of the losses could not be determined on the basis that the subsidiary's jurisdiction of residence does not allow for any possibility to transfer losses. Hence, the restrictions imposed by the jurisdictions of residence of the subsidiary (Denmark, Latvia (in two cases), Hungary and Sweden) on the

[220] KHO:2020:51, 15 May 2020, ECLI:FI:KHO:2020:51

utilization of tax losses, does not, *per se*, rule out the possibility for a third party to utilize the subsidiary's losses, in future tax years, upon an acquisition of such subsidiary.

Thoughts on the five Supreme Administrative Court's cases issued in May 2020

In light of the five Supreme Administrative Court's cases issued in May 2020, the bar is set sky high for entities to have final losses. The bar is set so high that it currently seems close to impossible to satisfy the requirements of final losses in Finland. The author believes that a legislative change or a bigger reform of the current legislation is needed in order for to allow for cross-border mergers and the deduction of losses, where the losses have been deemed final. It is a fact that Finland allows for final losses to be deducted following a cross-border merger, however, currently, it is yet unknown whether entities are able to demonstrate that subsidiary losses are final, as per the Supreme Administrative Court's case-law. It is yet to be seen what the result of the Finnish working group, that was set up on 31 October 2019 (VM163:00/2019), and the report's results and possible changes on the deduction of final losses in a cross-border merger.

4.3 Is the level of burden of proof for demonstrating final losses in Finland currently in line with EU law?

In KHO:2020:51(and the four other decisions issued by the Supreme Administrative Court 15 May 2020 with the numbers 2104-2107) the burden of proof for demonstrating final losses is put extremely high.

In KHO:2020:51 the Supreme Administrative Court notes, that the burden of proof lies with the taxpayer to demonstrate that the foreign subsidiary has exhausted all the possibilities for taking the losses into account in its state of residence. In the decision, the Supreme Administrative Court notes that the taxpayer had not demonstrated that the foreign subsidiary's losses were final and hence the losses may not be deemed final, as per the CJEU's established case-law.

In light of CJEU case-law, it should be noted that EU law precludes any burden of proof, which make it virtually impossible or disproportionately difficult to recover such taxes or charges, levied in breach of EU law. This conclusion has been reached e.g. in Case C-199/82 *San Giorgio*, which states: (paragraph 14):

> *"Any requirement of proof which has the effect of making it virtually impossible or excessively difficult to secure the repayment of charges levied contrary to Community law is incompatible with Community law, even if repayment of a substantial number of, or even all, the national taxes, charges and duties levied in breach of Community law is subject to the same restrictive conditions."*[221]

In the current five Supreme Administrative Court's cases from 15 May 2020, the burden of proof is set, according to the authors opinion, virtually impossible or excessively difficult also taking into account that other Member States legislations have accepted losses to be final (i.e. the taxpayer has successfully demonstrated that the losses are final). In Finland, it yet seems to be impossible to demonstrate final losses, but time will tell whether the burden of proof requirements will be kept on the current high level or will such evolve to correspond to other Member State's legislations and legal practice.

A taxpayer may also make a former complaint to the EC regarding the standard of burden of proof arguing that Finland is yet again in breach of EU law, as per the *San Giorgio* principles.

4.4 Should there be a final losses doctrine in the EU, or should it be accepted that the internal market is not harmonized?

Depending on whom you speak to in the tax sphere, there are differing thoughts on whether there should be a cross-border loss relief within the EU. There are valid arguments both for and against there being a final losses doctrine, but the author believes the opinion is much rooted in politics, whether one is for a fiscally harmonized EU or whether one believe a state is better off by itself (or a mix of the two options).

The author believes the final losses doctrine has been developed to be too complex to be understood by EU nationals but the author understands that this is sort of a "quick fix", as the EU have not been successful with the common (consolidated) corporate tax base. In Finland, during the years after *Marks & Spencer II*, a large amount of entities has applied to deduct its foreign subsidiaries losses, but the Finnish court system has continuously made it close to impossible to prove the finality of a subsidiaries losses. This was confirmed, at last, by the five Supreme Administrative Court's cases issued in May 2020, the decision of which concluded that the applicants had not sufficiently demonstrated the finality of the losses, even

[221] Case C-199/82 *Amministrazione delle Finanze dello Stato v SpA San Giorgio*, ECLI:EU:C:1983:318

thought the finality had been accepted by all instances before the Supreme Administrative Court. The question hence remains, what is sufficient to prove the finality of losses? It is already established that Finland need to allow for the deduction of a final losses, but is there a possibility to prove that losses are final, in light of the current case-law in Finland? The Supreme Administrative Court heavily relies on the fact that losses are not deemed final if the subsidiary may receive even a small amount of financial or other income in the state of residency. According to the Supreme Administrative Court's view, if the subsidiary receives 1 euro in interest, the losses are not to be deemed final.

As long as the EU does not introduce (or agree upon) a common corporate tax base, the issue of finality of losses will exist. Some Member States have been able to implement the final losses doctrine in a more forceable and user friendly way, but the current practise in Finland makes it hard to reach up to the burden of proof, as set by the Supreme Administrative Court's five cases issued in May 2020. What exactly is needed for proofing final losses is yet to be discovered in Finland.

5 CONCLUSIONS

The issue of this thesis boils down to the EU and a more harmonized internal market. The EU aims towards a more borderless internal market, which also means that fiscal barriers need to be torn down, within the limits of the law. As corporate tax remains an unharmonized area, within the EU, the harmonization and unification of the fiscal side of the internal market becomes more and more complex. The EU, on one side, tries to harmonize the internal market with several proposals in this regard, the latest one being the CC(C)TB, and the Member States on the other side trying to keep the reins regarding their taxation to the largest extent possible.

This thesis has examined when the cross-border deduction of losses is to be allowed by a Member State, being in exceptional cases when a subsidiary's losses are final, as defined by CJEU case-law (*Marks & Spencer II* onwards until *Memira Holding* and *Holmen AB*). CJEU case law has evolved and the definition of final losses have been clarified by various case-law, and the doctrine has been extended to cover cross-border mergers, group contribution, foreign branches and subsidiaries resident within the EEA.

As EU case-law is applicable also in Finland, Finland have had to implement the final losses doctrine in national law as well. Finnish case-law has evolved since the *Marks & Spencer II* case but yet it seems close to impossible to demonstrate the existence of final losses in Finland. This was confirmed by the five Supreme Administrative Court's cases issued in May 2020, where the Court found in all five cases that the Finnish parent company, being the applicants, had not successfully demonstrated that the losses are in fact final, despite the finality of the losses being accepted in all instances before the Supreme Administrative Court. In these five cases, the Supreme Administrative Court heavily relied on the argumentation that the losses may not be deemed final as the applicants had not demonstrated that the subsidiary could not be in the receipt of even a small amount of financial or other income in the Member State of residence, in the coming years.

Finland implemented a new law, the Act on Group Deduction, applicable as of 2021, whereby a Finnish parent company is able to deduct its foreign subsidiary's final losses in Finland for the parent company's Finnish tax purposes. However, in light of the five aforementioned Supreme Administrative Court's cases, the question arises whether it currently is possible to demonstrate the finality of a foreign subsidiary's losses. In the Government proposal for the Act on Group Contribution, the final losses concept is to be the definition as set out in CJEU

case-law. Interestingly enough, other EU Member States have been successful in allowing its nationals to deduct its foreign subsidiary's final losses for the parent company's tax purposes, but in Finland this seems to yet be unsolved. A law is in force in this regard, but none knows what exactly is needed in order to successfully demonstrate that a foreign subsidiary's losses are indeed final.

The question also arises whether Finland is yet in breach of EU law when setting the burden of proof impossibly high. This standpoint could be argued in light of the CJEU case *San Giorgio*. Another route could be to make a formal complaint to the EC arguing that Finland is in breach of EU law (and hence the principle argued in *San Giorgio*) when setting the burden of proof for final losses unreasonably high.