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OPINION STATEMENT

Opinion Statement ECJ-TF 3/2018 on the CJEU decision of 12 June 2018, in Case C-650/16, *Bevola*, concerning the utilisation of "definitive losses" attributable to a foreign permanent establishment

Prepared by the CFE ECJ Task Force
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CFE welcomes the Court's approach in *Bevola,* under which the comparability in territorial systems with regard to "definitive losses" was linked to the ability to pay. The Court's decision in *Bevola* reaffirms that its concept of "definitive losses", which was first established in *Marks & Spencer* and refined, *inter alia*, in *Commission v. United Kingdom* is still applicable to permanent establishments. Rejecting a reading of *Nordea Bank* and *Timac Agro* advanced by national governments, the European Commission and several national supreme tax courts, under which domestic and foreign permanent establishments were deemed as not comparable in territorial systems, the Court reiterated that the standard for testing comparability remains related to the aim pursued by the national provisions at issue. CFE notes, however, the increasing difficulty of applying the comparability test in a coherent manner, despite all the efforts of the Court in this respect.

In applying the 'final losses' doctrine, cross-border investing companies that incur losses are still at a disadvantage compared to a domestic company if the enterprise is profit-making overall: the purely national company can immediately deduct any losses, while the company that invests cross-border suffers at the very least an unfavourable "timing difference" on utilisation of losses. The CFE therefore invites Member States to consider the introduction of immediate loss utilisation with a recapture mechanism, and, urges the European Commission to propose harmonising measures in this respect.

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This is an Opinion Statement prepared by the CFE ECJ Task Force[1] on Case C-650/16, Bevola, in which the Grand Chamber of the Court of Justice of the EU (ECJ) delivered its judgment on 12 June 2018.[2] In general terms, the ECJ followed the reasoning of Advocate General Campos Sánchez-Bordona, who had delivered his opinion on 17 January 2018.[3]

The case concerned the compatibility of the Danish loss rules whereby losses attributable to a foreign (EU) permanent establishment (PE) of a Danish company could not be set-off against taxable Danish income of that company, except in the situation where the company opted for an "international integration regime". The loss attributable to the Finnish PE of Bevola was of a definitive nature. The Danish tax authorities refused to allow its utilisation, including denying the benefit of the *Marks & Spencer* doctrine for the company.

In its judgment, the Court confirms its approach to "definitive losses" ("final losses"): A loss of a foreign permanent establishment must be taken into consideration by the State of residence of the company, provided that that company has exhausted the possibilities of deducting the loss available under the law of the Member State in which the establishment is situated, and that it has ceased to receive any income from that establishment. The Danish company cannot be required, in order to obtain offsetting of its losses, to opt for an international joint taxation regime.

I. Background and Issues

1. Bevola is a Danish resident company with an ultimate Danish parent company, Jens W. Trock. Bevola's Finnish permanent establishment closed in 2009. According to Bevola, its losses could not be deducted in Finland following the closure. Bevola thus claimed to use them against Danish income, but this was denied by the Danish tax authorities.
2. Under § 8.2 of the Danish law on corporation tax, taxable income does not include income and expenditure relating to a permanent establishment situated in a foreign state. This general rule is however subject to specific provisions of the corporate tax law establishing national and international joint taxation regime. Under § 31 of the corporate tax law (dealing with the national joint tax regime) a joint income is calculated, consisting of the sum of the taxable income of each individual company covered by the regime. Losses of a foreign permanent establishment may generally only be offset against income of a Danish company if international joint taxation (see below) has been chosen (and maintained for a minimum period of ten years). The ultimate parent company participating in the joint tax regime is designated as the management company for the purposes of the regime. This regime is completed by § 31A allowing the top parent company to extend the tax integration scheme to foreign companies of the group as well as to all foreign permanent establishments owned by Danish and foreign companies participating in the joint taxation regime.
3. Bevola and its parent company Jens Trock argued that, had Bevola had a Danish establishment, its losses would have been deductible in Denmark; as such the fact that the foreign losses cannot be set off against Danish income constitutes a restriction of freedom of establishment. They also considered that the Finnish losses, as definitive losses, should be deductible from Bevola's income which is taxable in Denmark, its country of residence.

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[2] ECLI:EU:C:2018:424.

[3] ECLI:EU:C:2018:15.

4. The Danish court hearing the dispute questioned the relevance of the companies' arguments, especially in view of the possibility, offered by the Danish tax legislation, to opt for the international tax integration regime. The Court thus referred the following question to the ECJ:

> "Does Article 49 TFEU preclude a national taxation scheme such as that at issue in the main proceedings under which it is possible to make deductions for losses in domestic branches, while it is not possible to make deductions for losses in branches situated in other Member States, including in circumstances corresponding to those in the Court's judgment [of 13 December 2005] in *Marks & Spencer*, C-446/03, C-446/03, EU:C:2005:763, paragraphs 55 and 56, unless the group has opted for international joint taxation on the terms as set out in the main proceedings?"

II. Judgment of the Court of Justice

5. As a first step, the Court[4] notes the existence of a difference in treatment, under Danish law, between Danish companies which have a permanent establishment in Denmark and those whose permanent establishment is situated in another Member State. The former can deduct losses from their local branch for Danish tax purposes, while the latter can deduct losses from their permanent establishment situated in another Member State only if they opt for the international tax integration. This difference in treatment is likely to make it less attractive for a Danish company to exercise its freedom of establishment by creating permanent establishments in other Member States.[5] This difference in treatment is also not called into question by the existence of the optional "international joint taxation" regime under § 31A of the Danish law on corporation tax, the benefit of which "is subject to two strict conditions" (i.e., inclusion of global income and minimum period of ten years).[6]

6. The Court then examines whether the difference in treatment constitutes an obstacle to the freedom of establishment. Such a restriction would not exist if *(1)* the difference in treatment concerns situations which are not objectively comparable, or *(2)* if an overriding reason in the public interest is found to exist that *(3)* is proportionate to that objective.[7] The Court addresses each step in some detail:

7. Comparability of situations. Some of the intervening governments[8], relying on the *Timac Agro*[9] and *Nordea Bank*[10] cases, consider that a Danish company with local branch and one with a branch in another Member State are not in a comparable situation since the income of the foreign permanent establishment "is not subject to the tax jurisdiction" of Denmark.[11] The EU Commission, which shares this reading of the Nordea Bank and Timac Agro cases, points out, however, that those judgments contradict the previous case-law of the Court, "which accorded no importance to the reason for the difference in treatment".[12] According to the Commission, taking into account the comparability analysis, the reason for the difference of treatment would mean considering two situations as not comparable "simply because the Member State would have chosen to treat them differently".[13] Referring to *Oy AA*,[14] *X Holding*[15] and *SCA Group Holding*,[16] the Court recalls that the "comparability of a cross-border situation with an internal

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[4] In general terms, the Court of Justice follows the reasoning of Advocate General Campos Sánchez-Bordona. We shall thus mainly refer to the judgment.

[5] *Bevola* (C-650/16), para. 29.

[6] *Bevola* (C-650/16), paras 25-27.

[7] *Bevola* (C-650/16), para. 20.

[8] I.e., Austria, Germany and Denmark.

[9] ECJ, 17 July 2014, C-48/13, *Nordea Bank Danmark A/S v Skatteministeriet*, EU:C:2014:2087.

[10] ECJ, 17 December 2015, C-388/14, *Timac Agro Deutschland GmbH v Finanzamt Sankt Augustin*, EU:C:2015:829.

[11] *Bevola* (C-650/16), para. 30.

[12] *Bevola* (C-650/16), para. 31.

[13] *Bevola* (C-650/16), para. 31.

[14] ECJ, 18 July 2007, C-231/05, *Oy AA*, EU:C:2007:439.

[15] ECJ, 25 February 2010, C-337/08, *X Holding BV v Staatssecretaris van Financiën*, EU:C:2010:89.

[16] ECJ, 12 June 2014, C-39/13 to C-41/13, *Inspecteur van de Belastingdienst/Noord/kantoor Groningen and Others v SCA Group Holding BV and Others*, EU:C:2014:1758.

situation must be examined having regard to the aim pursued by the national provisions at issue".[17] It then undertakes to explain in *Nordea Bank* and *Timac Agro*, stating that those cases "do not imply the abandonment […] of that method of assessing the comparability of the situations, which is moreover expressly applied in later judgments".[18] Actually, says the Court concerning *Nordea Bank* and *Timac Agro*, "there was no need for it to look at the purpose of the national provisions concerned, since they applied the same tax treatment to permanent establishments abroad and those in national territory".[19] Referring to *Avoir Fiscal*,[20] the Court adds that "[w]here the legislature of a Member State treats those two categories of establishments in the same way for the purpose of taxing their profits, it recognizes that, with regard to the detailed rules and conditions of that taxation, there is no objective difference between their situations which could justify a difference in treatment".[21] However, it should not be understood from these statements that "where a national tax legislation treats two situations differently, they cannot be regarded as comparable",[22] as "to accept that a Member State may in all cases apply different treatment solely because the permanent establishment of a resident company is situated in another Member State would deprive Article 49 TFEU of its substance".[23]

According to the Court, where, as in the case at hand, the national legislation removes from the taxable base both the income and losses of foreign permanent establishments, it is intended to prevent the double taxation of income and, symmetrically, the double deduction of losses of foreign permanent establishments. As regards such measures, companies with foreign permanent establishments are not, as a rule, in a situation comparable to that of companies with a resident permanent establishment, for which conclusion the Court expressly refers to *Nordea B*ank and *Timac Agro*.[24] However, situations become comparable from the point of view of the objective of preventing double deduction of losses when the foreign permanent establishment *(1)* has ceased any activity and *(2)* whose losses can no longer be deducted in the State in which the permanent establishment is situated.[25] This approach is reinforced by considering the aim of the national provisions which the Court said was to ensure that the taxation of a company with a foreign permanent establishment be in line with its ability to pay tax: a company with definitive foreign losses is in a situation comparable to the one of a company with a loss-making resident permanent establishment.[26]

8. Justification of the Restriction. Based on settled case law, the Court concludes that the Danish tax rules could be justified by overriding reasons in the public interest relating *(1)* to the balanced allocation of powers of taxation between the Member States, *(2)* the coherence of the Danish tax system and *(3)* the need to prevent the risk of double deduction of losses.

   a. Regarding the balanced allocation of taxing rights, it is worth noting that the Court drew special attention to the possibility of the taxpayer being able to choose the place where the losses may be offset, which is something to be avoided.[27]

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[17] *Bevola* (C-650/16), para. 32.

[18] *Bevola* (C-650/16), para. 33, referring to ECJ, 21 December 2016, C-593/14, *Masco Denmark ApS and Damixa ApS v Skatteministeriet*, EU:C:2016:984, ECJ 22 June 2017, C-20/16, *Wolfram Bechtel and Marie-Laure Bechtel v Finanzamt Offenburg*, EU:C:2017:488, and ECJ, 22 February 2018, C-398/16 and C-399/16, *X BV and X NV v Staatssecretaris van Financiën*, EU:C:2018:110.

[19] *Bevola* (C-650/16), para. 34.

[20] ECJ, 28 January 1986, 270/83, *Commission of the European Communities v French Republic*, EU:C:1986:37, para. 20.

[21] *Bevola* (C-650/16), para. 34.

[22] *Bevola* (C-650/16), para. 35, referring ECJ, 22 January 2009, C-377/07, *Finanzamt Speyer-Germersheim v STEKO Industriemontage GmbH*, EU:C:2009:29, para. 33.

[23] *Bevola* (C-650/16), para. 35, referring to ECJ, 25 February 2010, C-337/08, *X Holding BV v Staatssecretaris van Financië*n, EU:C:2010:89, para. 23.

[24] *Bevola* (C-650/16), paras 24 and 27.

[25] *Bevola* (C-650/16), para. 38.

[26] *Bevola* (C-650/16), para. 39.

[27] *Bevola* (C-650/16), para. 43, referring to ECJ, 25 February 2010, C-337/08, *X Holding BV v Staatssecretaris van Financiën*, EU:C:2010:89, para. 29.

b. As to the coherence of the tax system, the Court recalls that the direct nature of the link between the tax advantage and the compensating tax charge must be examined in the light of the objective pursued by the legislation in question.[28] One the one hand, a resident company may use the losses of its domestic permanent establishment while for foreign losses such use is possible only if the company opted for the international joint taxation regime. On the other hand, profits of the domestic permanent establishment are taxed in Denmark while profits attributable to the foreign permanent establishment are not, unless the international joint taxation regime applies. According to the Court, this national provision indeed establishes the necessary link between the tax advantage (use of losses) and the compensating tax charge (taxation of profits).[29] Such direct link is moreover in line with the aim to tax according with the company's ability pay, because a "company's ability to pay tax would be systematically underestimated" if such "company possessing a permanent establishment in another Member State were allowed to set off against its results the losses incurred by that establishment without being taxed on the profits made by it".[30]

c. The risk of double deduction of foreign losses is also viewed by the Court as a justification,[31] even if not expressly relied on by the Danish government.

9. Proportionality. In light of those grounds of justification, the Court had to assess the proportionality of the measure and, in doing so, could largely rely on its judgments in *Marks & Spencer*[32] and *Commission v. United Kingdom ("Marks & Spencer II")*.[33] As the Court narrowed down its analysis to the deductibility of "definitive losses", it has not directly ruled on the taxpayer's option to enter the international joint taxation regime and its conditions.[34] The Court starts its analysis by noting that "[w]here there is no longer any possibility of deducting the losses of the non-resident permanent establishment in the Member State in which it is situated, the risk of double deduction of losses no longer exists".[35] Denying cross-border loss utilization in such a situation would go beyond what is necessary to achieve the objectives of the Danish rules (i.e., balanced allocation of powers of taxation, coherence of the tax system, and prevention of the risk of the double use of losses) and, conversely, "[a]lignment of the company's tax burden with its ability to pay tax is ensured better if a company possessing a permanent establishment in another Member State is authorised, in that specific case, to deduct from its taxable results the definitive losses attributable to that establishment."[36] In light of the coherence of the Danish tax system, however, "deduction of such losses can be allowed only on condition that the resident

[28] *Bevola* (C-650/16), para. 45, referring, *inter alia*, to ECJ, 30 June 2016, C-123/15, *Max-Heinz Feilen v Finanzamt Fulda*, EU:C:2016/496, para. 30.

[29] *Bevola* (C-650/16), para. 48.

[30] *Bevola* (C-650/16), paras 49 and 50.

[31] *Bevola* (C-650/16), para. 52, referring to *Commission v United Kingdom* (C-172/13).

[32] ECJ, 13 December 2005, C-446/03, *Marks & Spencer plc v David Halsey (Her Majesty's Inspector of Taxes)*, EU:C:2005:763.

[33] *Commission v United Kingdom* (C-172/13). For a detailed analysis see Opinion Statement ECJ-TF 2/2015 of the CFE on the decision of the European Court of Justice in Case C-172/13, *European Commission v. United Kingdom ("Final Losses")*, concerning the "*Marks & Spencer* exception", ET 2016, pp. 87 et seq.

[34] *Bevola* (C-650/16), paras 55-58. However, the Court briefly addressed the conditions of the Danish international joint taxation regime and demonstrated sympathy for the underlying concepts (*Bevola* (C-650/16), paras 56): "It should be stressed that, if a resident company were free to define the extent to which that joint taxation was applied, it would be able to decide at will to incorporate only non-resident permanent establishments facing losses, which would then be deducted from its taxable income in Denmark, while excluding establishments making profits and subject in their own Member State to a rate of tax that might be more favourable than in Denmark. Similarly, the possibility which would be left to the resident company of altering the extent of international joint taxation from one year to the next would be tantamount to allowing it to choose freely the Member State in which the losses of the non-resident permanent establishment in question were to be taken into account (see, to that effect, judgment of 25 February 2010, *X Holding*, C-337/08, EU:C:2010:89, paragraphs 31 and 32). Such possibilities would jeopardise both the balanced allocation of powers of taxation between Member States and the symmetry between the right to tax profits and the possibility of deducting losses sought by the Danish tax system."

[35] *Bevola* (C-650/16), para. 58.

[36] *Bevola* (C-650/16), para. 59.

company demonstrates that the losses it wishes to set off against its results are definitive".[37] As for when a loss is "definitive" the Court refers to *Marks & Spencer*[38] and the further elaborations in *Commission* v *United Kingdom*,[39] according to which "the losses incurred by a non-resident subsidiary may be characterised as definitive 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."[40] The Court then, without further discussion, found that standard to be also applicable for the situation of permanent establishments in territorial systems.[41] "Definitive" losses hence exist where *(1)* the company possessing the establishment has exhausted all the possibilities of deducting those losses available under the law of the Member State in which the establishment is situated and *(2)* 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.[42] However, the Court eventually left it for the national court to assess whether those conditions are satisfied in the case of Bevola's Finnish establishment.[43]

10. The Court hence concluded:

> "Article 49 TFEU must be interpreted as precluding legislation of a Member State under which it is not possible for a resident company which has not opted for an international joint taxation scheme, such as that at issue in the main proceedings, 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".

III. Comments

11. This Task Force has already had the opportunity to comment on the case law of the Court relating to cross-border use of losses: A 2009 Opinion Statement analysed the consequences for the State of residence of applying either a worldwide or a territorial taxation and the respective effects on the use of foreign losses in light of the Court's case law;[44] moreover, a 2015 Opinion Statement on *Commission v. UK ("Marks & Spencer II")*[45] addressed a number of issues relating to the question whether losses are "definitive" ("final").[46] The present Opinion Statement will take up questions of comparability, the relevance of the principle of ability to pay in the context of loss-utilization, and the definition of "definitive" or "final" losses in light of *Bevola* and other recent decisions. It should be noted at the outset that – in line with *Gielen*,[47] but without explicitly referring to it – the Court was not impressed by the

[37] *Bevola* (C-650/16), para. 60, referring to ECJ, 13 December 2005, C-446/03, *Marks & Spencer plc v David Halsey (Her Majesty's Inspector of Taxes)*, EU:C:2005:763, para. 56, and *Commission v United Kingdom* (C-172/13), para. 27.

[38] *Marks & Spencer* (C-446/03), para. 55.

[39] *Commission v United Kingdom* (C-172/13).

[40] See *Bevola* (C-650/16), para. 63, referring to *Commission v United Kingdom* (C-172/13), para. 36.

[41] See *Bevola* (C-650/16), para. 64, noting that the standards set in *Marks & Spencer* and *Commission v United Kingdom* for group taxation regimes "may be applied by analogy to the losses of non-resident permanent establishments".

[42] See *Bevola* (C-650/16), para. 64.

[43] See *Bevola* (C-650/16), para. 65.

[44] Opinion Statement of the CFE ECJ Taskforce on Losses Compensation within the EU for Individuals and Companies Carrying Out Their Activities through Permanent Establishments, ET 2009, 487 et seq.

[45] ECJ, 3 February 2015, C-172/13, *European Commission v United Kingdom of Great Britain and Northern Ireland*, EU:C:2015:50.

[46] Opinion Statement ECJ-TF 2/2015 of the CFE on the decision of the European Court of Justice in Case C-172/13, *European Commission v. United Kingdom ("Final Losses")*, concerning the "*Marks & Spencer* exception", ET 2016, pp. 87 et seq.

[47] ECJ, 18 March 2010, C-440/08, *F. Gielen v Staatssecretaris van Financiën*, EU:C:2010:148, paras 49 et seq.

existence of the optional "international joint taxation" regime under § 31A of the Danish law on corporation tax, the benefit of which "is subject to two strict conditions" (i.e., inclusion of global income and minimum period of ten years).[48]

A. Comparability, Ability to Pay and Double Deduction of Losses

12. The Court's explanations with respect to comparability of domestic ("resident") and foreign ("non-resident") permanent establishments[49] are of particular importance. In an attempt to reconcile its decision in *Lidl Belgium*[50] with those in *Nordea Bank* and *Timac Agro*, the Court resorts to link the question of comparability to the existence of definitive losses. This marks an important new development that rejects a reading of the latter judgments as excluding the *ex ante* comparability between domestic and foreign permanent establishments where the residence state applies a territorial tax system. In *Bevola*, the Court made it clear that it has not abandoned its approach to comparability of domestic and foreign situations from earlier case law.[51] This clarification is all the more relevant since its jurisprudence had already been misread in this manner by several national supreme courts in Europe.[52]

13. The Court reaffirms the principle that comparability needs to be assessed having regard to the aim of the national provision,[53] while rejecting the apparent consequence that comparability depends on the legal framework a given State adopts at a given time. A reading that would allow Member States to exclude comparability by way of designing its tax law in such a way as to always treat foreign permanent establishments different from domestic establishments would "deprive Article 49 TFEU of its substance".[54]

14. The Court also retains the statement from *Nordea Bank* and *Timac Agro* that "companies which have a permanent establishment in another Member State are not, in principle, in a comparable situation to that of companies possessing a resident permanent establishment" with respect to measures concerned with the prevention of double taxation.[55] This was followed in those judgments with an exception to this rule of non-comparability in the case where the State has decided to include the results from a resident company's foreign permanent establishment in its domestic tax base.[56] In *Bevola*, the Court made it clear that this was not to be understood to be the *only* exception to such rule, as had been contended by several Member States intervening in the case.[57] The Court is undoubtedly correct to say that such reading of *Nordea Bank* (para. 24) and *Timac Agro* (para. 27) was not necessary, as these merely pointed to situations where the Member State actually treated foreign permanent establishments equal to

[48] *Bevola* (C-650/16), paras 25-27.

[49] The Court frequently uses the notion of "residence" when referring to permanent establishments, which are neither taxpayers nor persons (e.g., *Bevola* (C-650/16), para. 30). It seems that this terminology is not used in a technical sense and must therefore not be confused with the international tax concept of tax residency, which only applies to persons.

[50] ECJ, 15 May 2008, C-414/06, *Lidl Belgium GmbH & Co. KG v Finanzamt Heilbronn*, EU:C:2008:278.

[51] *Bevola* (C-650/16), para. 33.

[52] See German Supreme Tax Court (BFH), 22 February 2017, IR 2/15, and Austrian Supreme Tax Court (VwGH), 29. March 2017, Ro 2015/15/0004.

[53] *Bevola* (C-650/16), para. 32.

[54] *Bevola* (C-650/16), para. 35.

[55] *Bevola* (C-650/16), para. 37, referring to *Nordea Bank* (C-48/13), para. 24, and *Timac Agro* (C-388/14), para. 27.

[56] *Nordea Bank* (C-48/13), para. 24; *Timac Agro* (C-388/14), para. 28. In the latter case, the Court refers to Germany's granting of a "tax advantage" by permitting the deduction of losses, which established comparability. It should be noted here that the Court used that term (in line with its earlier case law on loss relief and the „coherence" justification) to establish a link between tax benefits and tax burdens, and not in the technical sense relevant for a State aid analysis: there is no indication in the Court's case law that the granting of loss relief would by itself be considered a tax advantage that could give rise prohibited State aid. In fact, the recent judgment in case *Andres* makes it clear that loss relief could only be considered an "advantage" in this sense if it were a deviation from the normally applicable tax system (ECJ, 28 June 2018, C-203/16 P, *Andres (liquidation Heitkamp BauHolding)*, ECLI:EU:C:2018:505, para. 88).

[57] See the arguments cited in *Bevola* (C-650/16), para. 30.

domestic establishments; the same cannot be said about the statement in para. 65 of *Timac Agro*, where the Court denied comparability *solely* on the fact that Germany did not exercise any tax powers over a foreign permanent establishment (that did not have definitive losses).In relationto that reasoning, the Court's clarification seems more like a reversal of the earlier judgment. Rather than outright denying comparability in the equivalent situation, the Court accepts, in *Bevola*, that comparability may nevertheless follow from the existence of losses attributable to a foreign permanent establishment, if that permanent establishment has "ceased activity and whose losses could not, and no longer can, be deducted from its taxable profits in the Member State [of its activity]".[58]

15. This result effectively corrects the overly restrictive approach seemingly taken in *Timac Agro*, which had appeared to abolish the "Marks & Spencer" exception for "definitive losses" incurred by foreign permanent establishments.[59] In doing so, it creates a new uncertainty about the structure of the fundamental freedoms' application, as the criterion defining comparability in this case seems to coincide with the standard used for testing proportionality.[60] The Court thus rejects anew the suggestions made by several Advocates General,[61] who, concerned with the clarity and dogmatic coherence of the path taken by the Court in this context, urged to drop both the exception for "definitive losses" and the traditional approach to comparability as relevant to the application of the freedom of establishment in such cases.[62]

16. The Court, finally, links comparability to the ability-to-pay principle, noting that the relevant tax provisions aim at ensuring taxation in line with the company's ability to pay, which requires the prevention of both double taxation and a double deduction of losses. The Court recognizes that a company is "affected in the same way" whether its domestic establishment has incurred losses or a foreign permanent establishment has "definitively incurred losses".[63] It is thus clear that comparability here is also inextricably linked to the objective of the tax system to tax income in accordance with the taxpayer's ability to pay. It remains unclear, however, why the Court considers the situation of domestic losses only to be comparable to that of *definitive* foreign losses, since these are defined, in the Court's own case law, as losses that could not *ever* be taken into account anywhere else but in the residence State. But the taxpayer's ability to pay is clearly already affected where a loss is not definitive: if a taxpayer's global income is 0, there is no ability to pay (or, in the AG's words: no *tax paying capacity*) and thus no tax should be payable in the relevant tax year. This holds true regardless of whether it results from foreign or domestic losses. The fact that losses might be carried forward does not change the lack of capacity to pay taxes in the year when the loss is incurred.[64]

17. Admittedly, the risk of a double use of losses is increased whenever a permanent establishment exists outside the territory of the State of residence. Any double deduction would, as the Court states too,[65] is equally inconsistent with the ability-to-pay principle. Yet, the more proportionate way to prevent this remains a recapture mechanism at the time when the State where the permanent establishment is situated actually grants such deduction. This solution, which was already proposed by AG *Sharpston* in *Lidl*

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[58] *Bevola* (C-650/16), para. 38.

[59] Although one could rightly argue, as AG Campos Sánchez-Bordona did in para. 57 of his Opinion, that this apparent deviation from *Marks & Spencer* and *Lidl Belgium* resulted merely from the fact that *Timac Agro* did not concern such definitive losses (as also pointed out clearly by AG Wathelet in his Opinion on that case, at para. 67).

[60] See further below in Chapter III.C.

[61] See Opinion AG Kokott, 19 July 2012, C-123/11, *A*, ECLI:EU:C:2012:488, para. 50; Opinion AG Mengozzi, 21 March 2013, C-322/11, *K*, ECLI:EU:C:2013:183, para. 88; Opinion AG Kokott, 13 March 2014, C-48/13, *Nordea Bank Danmark A/S v Skatteministeriet*, ECLI:EU:C:2014:153, para. 26; Opinion AG Kokott, 23 October 2014, C-172/13, *Commission v. UK*, ECLI:EU:C:2014:2321, paras 49-53.

[62] Opinion AG Kokott, 13 March 2014, C-48/13, *Nordea Bank Danmark A/S v Skatteministeriet*, ECLI:EU:C:2014:153, para. 26.

[63] *Bevola* (C-650/16), para. 39.

[64] This is supported by the fact that countries typically do not deny a deduction of losses incurred by a domestic establishment on the basis that such loss might be capable to be offset against foreign profits in another country. Indeed, the Court has previously held such denial an unjustifiable restriction of the freedom of establishment (ECJ, 12 September 2012, C-18/11, *Philips Electronics*, EU:C:2012:532; see also ECJ, 14 December 2000, C-141/99, *AMID*, EU:C:2000:696).

[65] *Bevola* (C-650/16), para. 39.

Belgium[66] (but unfortunately rejected by the Court) is the only one that avoids a disadvantage from establishing a presence in another Member State as protected by the freedom of establishment while also safeguarding the fundamental principles underlying the tax system. The counterargument that such mechanism is insufficiently secure to prevent a double use of losses is unconvincing in light of the experience with already existing domestic (procedural) rules and in the context of increasingly effective exchange of information within the European Union.[67] But even if that risk were still considered to be so high as potentially to outweigh the freedom of establishment's restriction, this question ought to be analysed as a matter of justification, since it is an objection grounded in a lack of coordination of tax administrations rather than an aspect inherent to the companies involved and thus needs to be subject to a proportionality analysis.

B. Grounds of Justification

18. Contrasting with the lengthy discussion on comparability, the Court was rather short in assessing the justifications for this measure. In this case, the Court has reviewed and considered as applicable three justifications: *(1)* balanced allocation of taxing rights; *(2)* coherence of the tax system; and *(3)* risk of double deductions of losses. The analysis of the Court is well aligned with the Court's traditional position in similar cases:[68]

    a. Relying on *X Holding*,[69] the Court first found that allowing a deduction of losses of permanent establishments located in other Member States would undermine the balanced allocation of taxing rights since it would allow taxpayers a right to choose the jurisdiction where its losses (and profits) would be taken into account.

    b. Second, tax coherence would also be undermined since there is a direct link between accepting the losses and taxing the profits of permanent establishments. This link is particularly clear if one takes into account the joint taxation regime where the taxpayer could deduct losses of foreign permanent establishments if it also opts for taxing its profits in Denmark.

    c. Lastly, and even if not mentioned by the Danish government, the Court held that the national provision at stake could also be justified by the need to prevent double use of losses.[70]

C. Proportionality and the 'Definiteness' of Losses

19. The Court then analyses whether the legislation at issue goes beyond what is necessary to achieving those objectives and concludes that the risk of double deduction of losses no longer exists where there is no longer any possibility of deducting the losses of the non-resident permanent establishment in the Member State in which it is situated.[71] Referring to its judgment in *Marks & Spencer* the Court holds that a Member State has to allow a company to deduct from its tax base the "definite losses" attributable to a permanent establishment located in another Member State. Allowing the deduction of "definite losses" better aligns with the company's ability to pay.

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[66] Opinion of AG Sharpston, 14 February 2008, C-414/06, *Lidl Belgium GmbH & Co. KG v Finanzamt Heilbronn*, EU:C:2008:88, para. 25.

[67] Such recapture mechanism is indeed used in several Member States (see, e.g., § 2(8) of the Austrian Income Tax Act) and has also been proposed by the European Commission (see Art 42 of the Commission's Proposal for a Council Directive on a Common Corporate Tax Base, COM(2016)685 final, on "Loss relief and recapture").

[68] *Bevola* (C-650/16), paras 41-54.

[69] ECJ, 25 February 2010, C-337/08, *X Holding*, EU:C:2010:89, paras 28-29.

[70] See *Bevola* (C-650/16), para. 52, referring to *Commission v United Kingdom* (C-172/13), para. 24.

[71] *Bevola* (C-650/16), para. 58.

20. To benefit from the deduction the taxpayer is obliged to show that the losses in question satisfy the "*Marks & Spencer* requirements", as further clarified in *Commission* v *United Kingdom*.[72] These requirements were originally stated in the context of a parent-subsidiary relationship and have to be applied by analogy to the losses of a foreign permanent establishment. As a result, losses attributable to a foreign permanent establishment become definitive if, first, the company possessing the establishment has exhausted all 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.[73] The second prong of that test – "ceased to receive any income from *that* establishment" – seems to imply that (future) positive income from other activities in the source State is irrelevant,[74] i.e., that the Court equates a permanent establishment effectively with a separate entity.

21. The "*Marks & Spencer* requirements" are now, in substance, applied both at the level of the comparability and at the level of proportionality.[75] This comparability analysis that seemingly includes a proportionality test, however, resembles the approach in *Schumacker*[76] and *X*,[77] where the Court also established comparability – from the source State's perspective – based on whether the other State is in a position to take certain tax benefits into account; in those cases the Court effectively mingles the analytical levels of comparability and proportionality. Concerning comparability, the Court has already held that the situation of a resident company with a foreign permanent establishment is not different from the situation of a resident company with a domestic permanent establishment if the permanent establishment has ceased its activity and the losses attributable to the permanent establishment could not, and no longer can, be deducted from its taxable profits in the Member State in which it carried on its activity.[78]

IV. The Statement

22. The Court's decision in *Bevola* is a continuation of the Court's case-law on cross-border use of losses. The Court reaffirms that its concept of "definitive losses", which was first established in *Marks & Spencer* and refined, *inter alia*, in *Commission v. United Kingdom*,[79] is (still) applicable to permanent establishments. Rejecting a reading of *Nordea Bank* and *Timac Agro* advanced by national governments, the European Commission and several national supreme tax courts that would deem domestic and foreign permanent establishments as not comparable in territorial systems, the Court reiterated its standard of testing comparability having regard to the aim pursued by the national provisions at issue. However, the CFE notes the increasing difficulty of applying the comparability test in a perfectly coherent manner, despite all the efforts of the Court in this respect.

23. The CFE welcomes that the Court in *Bevola* has linked the approach to comparability in territorial systems with regard to "definitive losses" to the idea of ability to pay. For the Court, if a loss is "definitive", the

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[72] *Commission v United Kingdom* (C-172/13).

[73] *Bevola* (C-650/16), para. 64.

[74] For a contrary argument by the Austrian government see Opinion of AG Wathelet, 3 September 2015, C-388/14, *Timac Agro Deutschland GmbH v Finanzamt Sankt Augustin*, EU:C:2015:533, para. 67 with footnote 45 ("According to the written observations of the Austrian Government, the losses of the Austrian permanent establishment accrued up to 2005 were in principle recoverable and capable of being deferred. The deferred losses could thus be set against any capital gain arising from the transfer, with any balance continuing to exist in principle for an unlimited period as deferred losses of Timac Agro. These losses could therefore be used at a later point in time if the applicant in the main proceedings resumed its business in Austria […]. The losses could also be passed on to the transferee limited company if the permanent establishment was transferred 'in a tax neutral manner' […]."

[75] For a critical view regarding this duplication see already above at para. 15 of this Opinion Statement.

[76] ECJ, 14 Feb. 1995, C-279/93, *Finanzamt Köln-Altstadt v Roland Schumacker*, EU:C:1995:31.

[77] ECJ, 9 Feb. 2017, C-283/15, *X v Staatssecretaris van Financiën*, EU:C:2017:102.

[78] *Bevola* (C-650/16), para. 38.

[79] See the Opinion Statement ECJ-TF 2/2015 of the CFE on the decision of the European Court of Justice in Case C-172/13, *European Commission v. United Kingdom ("Final Losses")*, concerning the "*Marks & Spencer* exception", ET 2016, pp. 87 et seq.

ability to pay principle requires such losses to be taken into account in the state of residence as otherwise the enterprise would be taxed beyond its overall profits.

24. It should be noted, however, that taking this loss into account when it is “final” or “definitive” in the source State implies that there are sufficient profits to offset it in the State of residence. Moreover, applying this concept of "final losses", a company investing in another Member State, where it incurs losses, is still economically disadvantaged if the overall enterprise is in a profit-making position: the purely national company can immediately deduct any losses, while the company that invests beyond its borders suffers at the very least an unfavourable “timing difference”.[80] It is doubtful whether this situation is really in line with the fundamental objective of the TFEU to create a single market without internal borders. The CFE therefore invites Member States to consider the introduction of immediate loss utilisation with a recapture mechanism, and urges the European Commission to propose harmonising measures in this respect.[81]

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[80] See, e.g., Opinion of AG Sharpston, 14 February 2008, C-414/06, *Lidl Belgium GmbH & Co. KG v Finanzamt Heilbronn*, EU:C:2008:88, paras 24 and 25.

[81] Such an idea is strongly supported by the CFE Tax Advisers Europe to the extent that its member organisations are in favour of the common corporate tax base itself (*see CFE Tax Advisers Europe,* Opinion Statement FC-1/2016 on the EU Public Consultation on the Relaunch of the CCCTB in January 2016, available at *http://taxadviserseurope.org/*). See already the (withdrawn) Commission Proposal COM(90)595 for the introduction of a cross-border loss relief mechanism and more recently, in the broader context of corporate tax base harmonization, Art 42 of the Commission’s Proposal for a Council Directive on a Common Corporate Tax Base, COM(2016)685 final, on “Loss relief and recapture See also, e.g., Opinion of AG Sharpston, 14 February 2008, C-414/06, *Lidl Belgium GmbH & Co. KG v Finanzamt Heilbronn*, EU:C:2008:88, para. 24: “Such a rule, which allowed the deduction of losses while providing for the recapture of the loss relief in future profitable periods, would manifestly be a less restrictive means of avoiding the risk that losses might be used twice than a rule altogether excluding relief for such losses. Although a deduction-and-recapture rule involves a loss of symmetry and hence does not wholly attain the objective of the balanced allocation of the power to tax, that asymmetry is merely temporary where the permanent establishment subsequently becomes profitable. Moreover provision could be made for automatic reincorporation of amounts previously deducted if reincorporation had still not occurred after, for example, five years, or if the permanent establishment ceased to exist in that form.”