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Is this the end of the *Marks & Spencer* Doctrine?

The Freedom of Establishment, Permanent Establishments and Objective Comparability

A Master's Thesis on whether the *Marks & Spencer* Doctrine is Applicable to Non-Resident Permanent Establishments and Whether the CJEU has Abandoned the Doctrine with Respect to the Case of *W AG*.

by

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Summary

The Thesis examines issues of European Corporate Tax Law and specifically the notion of the *Marks & Spencer* doctrine, with respect to non-resident permanent establishments. The doctrine entails the possibility for a resident company to deduct losses that were incurred by a PE, situated in another Member State. There is an ongoing debate among writers and scholars of European Tax Law concerning the application of the *Marks & Spencer* doctrine towards PE:s, due to recent judgements by the Court of Justice of the European Union on the matter. One of which have gained recent attention, namely Case C-538/20, *Finanzamt B v W AG*. Writers on the topic seem to have conflicting views on whether the Courts judgement should be seen as a *de facto* abandonment, or simply a further establishment of the doctrine's restrictive nature.

The Thesis aimed to address whether the *Marks & Spencer* doctrine applies towards non-resident PE:s to the same extent as it does towards subsidiaries, and also provide a meaningful contribution to the ongoing debate concerning the status of the doctrine.

The Thesis concluded that the doctrine of *Marks & Spencer* is applicable towards non-resident PE:s, under the circumstance that the non-resident PE can be deemed as objectively comparable to its domestic equivalent. Nevertheless, the Author of the Thesis noted that Case C-538/20, *Finanzamt B v W AG* is subject to a pattern of case-law where the Court has become more restrictive in its language and approach throughout its line of case-law. This pattern can be understood as the Courts way of not excluding a legal position for the future, where they may have to eventually or potentially abandon the doctrine.

List of Abbreviations

CJEU - Court of Justice of the European Union

DTT – Double Tax Treaty

ECJ – European Court of Justice

EU – European Union

M&S – Marks & Spencer

MNE – Multinational Entity

OECD - Organization for Economic Co-operation and Development

PE – Permanent Establishment

TEU – Treaty on European Union

TFEU – Treaty on the Functioning of the European Union

Treaties – TEU and TFEU

UK – United Kingdom

VAT - Value-Added Tax

1. Introduction

1.1. Background

The Court of Justice of the European Union (CJEU) acknowledges that tax law falls under the autonomy of the Member States and that the Court should not undermine the right to exercise the powers of taxation which are vested in the Member States.[1] On other hand, the EU has also established common standards for the Member States to harmonize their laws within the field of corporate and individual taxation. The Member States are expected to comply with the fundamental freedoms of the internal market in their domestic tax legislation.[2] Furthermore, it is evident that unharmonized domestic tax provisions pose serious obstacles to the fundamental freedoms of the internal market.[3] Issues of domestic tax rules that conflict with EU-law is a particularly delicate, and heavily debated, topic of EU-law.[4]

The depth of this debate became clear in the eminent Case C-446/03 *Marks & Spencer*[5] from 2005 with regards to cross-border group activities and the freedom of establishment. The case concerned the British multinational retailer Marks & Spencer, which at the time had subsidiaries in France, Germany and Belgium. Marks & Spencer wanted to deduct the losses of its foreign subsidiary, but this was not allowed under the law of the United Kingdom (UK) since the subsidiaries were not resident in the UK. Marks & Spencer claimed that UK law was in breach of the freedom of establishment by creating obstacles and negative tax treatment for foreign subsidiaries. The UK claimed that its domestic tax regime was necessary to ensure a balanced allocation of taxing rights between Member States, to prevent double use of losses and to prevent tax evasion. The CJEU held that the UK tax regime could be justified if their grounds are ‘considered all together’. However, the CJEU did not consider the provision as compatible with the principle of proportionality since the foreign subsidiaries had exhausted all the possibilities to take losses into account in their own States of residence, and still was not able to deduct their losses. Thus, the Marks & Spencer parent entity in the UK had to be allowed

[1] C-414/06, *Lidl Belgium GmbH & Co. KG v Finanzamt Heilbronn* [2008] ECR I-03601., para. 52; See also C-270/83, *Commission v. France (avoir fiscal)* [1986] ECLI:EU:C:1986:37., para. 24; C-279/93, *Schumacker* [1995] ECLI:EU:C:1995:3., para. 21; C-80/94, *Wielockx* [1995] ECLI:EU:C:1995:271., para. 16.
[2] C-341/05, *Laval un Partneri Ltd v Svenska Byggnadsarbetareförbundet et al* [2007] ECLI:EU:C:2007:809., para 87; See *supra* note 1. *Commission v France (avoir fiscale)*, para 13; C-334/02, *Commission v France* [2004] ECLI:EU:C:2004:129., para 21.
[3] Cruz, María., Barreiro, Carril. 'National Tax Sovereignty and EC Fundamental Freedoms: The Impact of Tax Obstacles on the Internal Market', (2010), 38, Intertax, Issue 2, pp. 105-113.
[4] Lindholm, Johan. ‘Squaring the Constitutional Circle: An Overview of EU Fiscal Powers - The Power to Tax in Europe’ (Oxford: Hart Publishing, 2023), pp. 3–18.
[5] C-446/03, *Marks & Spencer plc* [2005] ECLI:EU:C:2005:763.

to deduct the losses ofits foreign subsidiaries as long as those losses cannot be used again in any manner, or more famously established, as long as the losses are 'final'.

1.1.1 Scope of the problem

The *Marks & Spencer* ruling did not amount into a general EU right for companies to deduct foreign final losses with reference to the freedom of establishment, nor any obligation towards the Member State to take foreign final losses into account.[6] The doctrine of Marks & Spencer is restrictive in nature and for the past years, scholars of European tax law have debated the current status of the *Marks & Spencer* doctrine from various angles.[7]

One debate in particular seem to have gained attention the last couple of years, namely whether the doctrine applies to permanent establishments (PE) to the same extent as subsidiaries, and whether CJEU case-law on the matter implies that the Court wants to abandon the doctrine towards non-resident PE:s.[8] In the Case C-650/16 *Bevola* from 2018, the CJEU affirmed its decision in *Marks & Spencer* by ruling that the freedom of establishment does preclude the domestic law of Member States to prevent a resident company to deduct losses from its non-resident PE, unless the parties opts for an international joint tax scheme. More importantly, the CJEU held that a resident PE and a non-resident PE are objectively comparable and to prevent a non-resident PE from having its losses taken into account would constitute a breach on the freedom of establishment.[9] Nonetheless, in September 2022, the CJEU left a significant imprint on this debate by not even proceeding any assessment of justifications nor proportionality in Case C-538/20 *W AG*. In a very short judgement, the CJEU held that the resident PE is not objectively comparable to a non-resident PE and thus, the freedom of establishment does not preclude the domestic law of a Member State to prevent a resident company from taking losses incurred by a non-resident PE into account.[10]

The factual circumstances of case *Bevola* and *W AG* were certainly not identical, a matter which

[6] Lang, Micheal. 'The Marks & Spencer Case – The Open Issues Following the ECJ's Final Word' (2006), 46, European Taxation, Issue 2, pp. 54-67., pp. 60.
[7] Erik Pinetz, Karoline Spies, ''Final Losses' after the Decision in Commission v. UK ('Marks & Spencer II'), (2015), 24, EC Tax Review, Issue 6, pp. 309-329., pp. 310-312.
[8] Kofler, Georg. 'Should We Cut 'Final' Losses' (2022), 31, EC Tax Review, Issue 3, pp. 108-114; Ismer, Roland & Kandel, Harald. 'A Finale Incomparabile to the Saga of Definitive Losses? Deduction of Foreign Losses and Fundamental Freedoms After Bevola and Sofina' (2019), 47, Intertax, Issue 6-7, pp. 581–584; Lang, Michael. 'Has the Case Law of the ECJ on Final Losses Reached the End of the Line?' (2014), 54, European Taxation, Issue 12, pp. 539-540.
[9] Case C-650/16, *A/S Bevola and Jens W. Trock ApS v. Skatteministeriet* [2018] ECLI:EU:C:2018:424., paras. 63–64.
[10] Case C-538/20, *Finanzamt B v W AG* [2022] ECLI:EU:C:2022:717., paras. 22 and 27.

the Thesis will thoroughly address. The *W AG* decision clearly intensified the debate on whether the CJEU wants to abandon the *Marks & Spencer* doctrine towards PE:s.

Writers on the topic seem to have conflicting views on the matter. While Georg Koffler[11] argues that the *W AG* case was a nail on the coffin for the doctrine and that the CJEU has led itself to a dead end with case *W AG*. Thomas Kollruss[12] argues that the factual circumstances between *Bevola* and *W AG* were so different that *W AG* cannot be seen as an abandonment of the doctrine. In fact, according to Kollruss, the test of objective comparability is of such complexity that the CJEU has acted consistently throughout its whole line of case-law.

1.2. Purpose and Aim

The purpose of the Thesis is to examine the current status of the *Marks & Spencer* doctrine with respect to non-resident PE:s, based on previous case-law of the CJEU, in the light of the *W AG* decision. Secondly, the Author of the Thesis aims to provide a meaningful contribution to the current debate among writers with respect to the current status of the *Marks & Spencer* doctrine towards non-resident PE, and whether the *W AG* case should be deemed as an abandonment of the doctrine, or whether the CJEU still want to apply it in a restrictive manner.

1.3. Method and Material

In order to achieve the purpose and aim of the Thesis, a traditional legal method will be adopted for the research. Such a method solves legal problems by using the authoritative sources of law within the respective legal order in question. The traditional sources of law constitute the stipulated law, preparatory work, case-law and literature.[13] In terms of the EU legal order, the notion of primary and secondary sources of EU-law needs to be taken into account. The starting point of any legal argument must be from EU primary law, i.e., the TEU[14] and TFEU[15] (hereinafter the "Treaties") and the freedom of establishment, alongside with the general principles of EU-law. The most predominant secondary source of EU-law for the Thesis will be CJEU case-law on the issue of deduction of foreign losses. The Thesis will examine its

[11] Kofler, Georg. 'Cross-Border Losses and W AG: The Beginning of the End of the "Final Loss Exception"?' (2022), Cahiers de fiscalité luxembourgeoise et européenne 1/2023.
[12] Kollruss, Thomas. 'The Concept of Final Losses under EU Law and its Scope of Application' (2023), 63, European Taxation, Issue 2-3, pp. 2.
[13] Qunfang, Jiang., Yifan, Yuan. 'Legal Research in International and EU Tax Law' (2014), 54, IBFD, Issue 10, pp. 471.
[14] European Union, *Consolidated version of the Treaty on European Union*, 13 December 2007, OJ C 115, 9.5.2008. [Hereinafter "TEU"].
[15] European Union, *Consolidated version of the Treaty on the Functioning of the European Union*, 26 October 2012, OJ L. 326.10.2012. [Hereinafter "TFEU].

research questions based on the relevant CJEU case-law and how they apply in the light of the freedom of establishment.[16] Such legal arguments may be supplemented by sufficient and accurate works of literature from eminent scholars, opinions from judges, as well as other sources like Commission publications, academic journal articles etc. The Thesis will not adopt a critical approach by challenging the validity of any judgments by the CJEU, rather state what the law is from a dogmatic *de lege lata* approach.

1.4. Delimitations

The Thesis will only focus on whether the *Marks & Spencer* doctrine is applicable towards non-resident PE:s, and whether the doctrine has been abandoned or not with respect to the case of *W AG*. The Thesis is limited to address the notion of 'objective comparability' between resident and non-resident PE:s. Hence, the Thesis will not go further into any other issues of cross-border tax activities where the *Marks & Spencer* doctrine may be relevant. Furthermore, the Thesis will be limited to address the works of the OECD and Double Tax Treaties (DTT), in a brief manner, for the purpose of thoroughly examining CJEU case-law.

1.5. Outline

In accordance with the traditional legal method, section two of the Thesis will address the freedom of establishment from a direct tax law perspective and the notion of cross-border transfer of losses. Furthermore, the section will extensively clarify what the doctrine of *Marks & Spencer* is with respect to its judgment, and how the doctrine generally applies towards foreign subsidiaries in terms of deduction of foreign final losses.

Section three will establish the legal distinction between subsidiaries and PE:s in order to address how the CJEU has applied the *Marks & Spencer* doctrine on PE:s in its precedent line of case-law. Section three will also elaborate on the role of DTT:s during the application of primary EU-law.

Section four will examine the application of the objective comparability analysis with respect to deductible final losses incurred by resident and non-resident PE:s. The section will address the most crucial cases on the matter and establish how the CJEU has reasoned up until its decision in case *W AG*.

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[16] Craig, Paul., De Búrca, Gráinne. 'EU Law - Texts, Cases and Materials' (3rd Ed.) (Oxford University Press, 2003), pp. 97.

Lastly, section five will thoroughly examine case *W AG* and elaborate on the grounds behind the reasoning of the CJEU, as well as addressing the variation of opinions among authors on whether the case of *W AG* should be deemed as an abandonment of the doctrine towards non-resident PE:s.

2. The Freedom of Establishment and the Doctrine of *Marks & Spencer*

2.1. The Freedom of Establishment and Transfer of Losses

2.1.1. Article 49 and 54 of the TFEU

The freedom of establishment is one of the fundamental freedoms of the European Union, enshrined in Articles 49 of the Treaty on the Functioning of the European Union (TFEU).[17] Article 49 TFEU guarantees any EU citizen who is established in one Member State the right to establish themselves in any other Member State, for the purpose of running a business or engaging in economic activity. This includes the right to own and operate a business, establish a subsidiary or branch office, or provide services. Meaning if someone establishes a business in one Member State, they have the right to expand to other Member States without facing additional barriers or restrictions.[18]

This freedom likewise applies to legal entities and companies, in accordance with Article 54 TFEU. This allows for the creation of companies in one Member State, which are then free to transfer their headquarters, branches, or subsidiaries to other Member States without facing any barriers.[19] From a tax perspective, the freedom of establishment is particularly important, as it allows companies to avoid double taxation or discriminatory tax regimes when operating across multiple EU Member States. The major difficulty in this context is to ensure the preservation of tax sovereignty among the Member States because tax law remains an issue primarily of national policy. To promote the freedom of establishment, the CJEU has been actively developing case law shaping understanding of principles surrounding the freedom of establishment. These principles highlight the importance of ensuring that Member States do not discriminate against foreign companies or entities looking to establish themselves in their country.[20]

2.1.1.1. Comparable Situations, Restriction, Justification and Proportionality

The application of EU-law follows with legal assessments that must be done in a chronological order. Before it can be established whether a restriction of the freedom of establishment exists, the foreign entity must be deemed as objectively comparable to its domestic equivalent, see Case C-48/94 *Nordea Bank*. If the tax situations are objectively comparable, the CJEU can examine whether there has been a discriminatory treatment towards the foreign entity and thus a

[17] See *supra* note 15. TFEU, Article 49 and 55.
[18] Helminen, Marjaana. 'EU Tax Law – Direct Taxation' (2022 Ed.) (IBFD, 2022), pp. 217.
[19] C-261/11, *Commission v. Denmark* [2013] ECLI:EU:C:2013:480., para. 28.
[20] Adamczyk, Łukasz. 'The Sources of EC Law Relevant for Direct Taxation', pp. 20 in Lang, Michael. 'Introduction to European Tax Law on Direct Taxation' (1st Ed.) (Linde Verlag, 2008).

restriction.[21] If the treatment is deemed as a restriction, the Member State will be obliged to prove that is has justifiable grounds for its restriction and that its law follows the legal standard of proportionality under EU-law.[22]

In its landmark decision, the Joined Cases C-163/94, C-165/94 and C-250/94 *Sanz de Lera*, the European Court of Justice (ECJ) held that restrictions on the freedom of establishment are only lawful if they are necessary to guarantee the coherence of a tax system, appropriate to prevent fraud or tax evasion, or to ensure effective fiscal supervision. The relationship of the restriction with the abovementioned, should pass a proportionality test, this means that the restriction needs to be an appropriate measure to address the issue and should not be excessive in relation to its objective. Additionally, the Court stated that Member States are prohibited from applying more restrictive measures or higher taxes on foreign companies on the grounds that they are foreign companies. Such a measure would be considered discriminatory and thus contrary to Article 49 and 54 TFEU. Furthermore, Double Taxation Treaty's (DTT) and EU Directives guiding EU tax laws pursue the aim of promoting the free movement of capital, and as well harmonizing tax laws and restrictions within the EU.[23]

2.1.3. Cross-border Transfer of Losses within the EU

Transfer of losses within the EU refers to the ability of companies operating in different EU Member States to offset losses incurred in one country against profits made in another country. This is an important measure that enables companies to reduce their tax liability and remain competitive in the EU market. However, this mechanism is often subject to challenges and disputes. One of the main issues is the lack of harmonization of tax laws across EU Member States. This means that national tax laws often differ significantly, leading to difficulties in determining how cross-border losses can be offset against profits.[24] Another problem is the phenomenon of profit shifting, whereby companies artificially transfer profits from high-tax jurisdictions to low-tax jurisdictions in order to reduce their tax liability. This practice can lead to a loss of tax revenue for Member States and distort fair competition. The implications of these issues may result in the loss of tax revenue for some countries and benefits for others, potentially

[21] C-48/13, *Nordea Bank* [2014] ECLI:EU:C:2014:2087., paras. 23–24; C-66/14, *Finanzamt Linz* [2015] ECLI:EU:C:2015:661., para. 31.
[22] C-524/04, *Test Claimants in the Thin Cap Group Litigation* [2007] ECLI:EU:C:2007:161., para. 62; C-231/05, *OY AA* [2007] ECR I-06373., para. 42.
[23] Joined Cases C-163/94, C-165/94 and C-250/94, *Sanz de Lara et al*. [1995] ECLI:EU:C:1995:451., paras. 41-48.
[24] van den Broek, Harm. 'Final Losses in Respect of Cross-Border Mergers: Memira (Case C-607/17) and Holmen (Case C-608/17)' (2020), 60, European Taxation, Issue 2-3, pp. 53-61., pp. 53-54.

creating a disadvantageous environment for some corporations. However, it is also evident that offsetting foreign losses can be a mean for aggressive tax planning or double deduction of losses which is a form of tax fraud. It is therefore imperative that consistent and fair rules are established across the EU to ensure that cross-border transfer of corporate losses is properly managed and that all Member States can maintain their respective taxing rights. A matter of objectives that the CJEU has the primary responsibility of safeguarding in its case-law.[25]

2.2. The *Marks & Spencer* Case

2.1.1. Facts of the Case

In 2001, Marks & Spencer, a UK-based multinational retailer company, sought to offset the losses of its subsidiaries in France, Germany, and Belgium against the profits of its UK parent company for tax purposes. However, under UK law, cross-border loss relief was only available if the losses had been incurred by subsidiaries located in EU Member States or in a country with which the UK had a double taxation agreement.[26] Since France, Germany, and Belgium did not fall under either of these categories, the UK Tax Authorities rejected Marks &Spencer's claim for cross-border loss relief. As a result, Marks & Spencer initiated legal proceedings, arguing that the UK's tax rules violated the freedom of establishment under Article 49 TFEU, which allows companies to freely carry out economic activities across Member States' borders.[27] The case was first heard in the High Court in London, which referred it to the CJEU for a preliminary ruling.

The question that was referred to the CJEU was whether a resident parent company should be prevented from deducting its taxable profit’s losses incurred by a subsidiary in another Member State and whether the parent company would be allowed to deduct the losses if they were incurred by a resident subsidiary and whether UK law was compatible with the freedom of establishment.[28]

2.1.2. The Legal Merits of the Parties

Marks & Spencer claimed that the group loss relief system of the UK was in breach of the freedom of establishment. The starting point on the freedom of establishment is that an undertaking cannot be treated less favorably based on their resident Member State, such a

[25] ibid. van den Broek, Harm., pp. 60–61.
[26] See *supra* note 5. *Marks & Spencer plc*, paras. 12-13.
[27] ibid. *Marks & Spencer plc*, paras. 18-26.
[28] ibid. *Marks & Spencer plc*, paras. 32-33.

scenario is discriminatory and prohibited under EU-law. In the following case, the group loss relief system is significantly more favorable and simpler for domestic corporate groups in relation to cross-border multinational entities (MNE) groups. The incentive to establish foreign subsidiaries with less favorable tax laws also poses an obstacle to the freedom of establishment. Marks & Spencer claimed that the UK law is not the least restrictive measure possible and does therefore not satisfy the proportionality test.[29] A less restrictive and proportionate measure would have been if the UK allowed group relief from foreign subsidiaries on the condition that the subsequent profits of the non-resident subsidiaries be incorporated in the taxable profits of the company which benefited from group relief up to an amount equal to the losses previously set off.[30]

The UK claimed that the tax situation of foreign subsidiaries and non-resident PE:s is not comparable and that their group loss relief system was justified and proportionate under EU-law based on several grounds. Firstly, the UK safeguarded the motion of a balanced allocation of taxing rights between Member States, namely that allowing deduction of foreign losses would amount to grave loss of tax revenue for the treasury. Secondly, the UK claimed that allowing deduction of foreign losses could pave the way for double deduction of losses, a fraudulent practice which results into a significant tax benefit for the parent company in question. Thirdly, the risk of tax evasion would be critical if the UK allowed foreign deduction of losses because it would give rise to transfer of losses to Member States with the highest tax rates. This would not be possible with an intra-group loss relief system that only applies in domestic situations.[31]

2.1.3. The Court's Assessment

The CJEU affirmed that Marks & Spencer had exercised their freedom of establishment by setting up foreign subsidiaries. The Court acknowledged the option of intra-group loss relief as asignificant tax advantage for the company and that a refusal of such advantage creates an obstacle for parent entities to establish subsidiaries outside their resident Member State. The CJEU emphasized the principle of territoriality that the resident Member State of a parent entity does not have any tax competence over a subsidiary in another Member State. Nonetheless, the Court asserted that if the principle of territoriality would apply in themanner that a Member State can treat foreign companies less favorably than resident ones, it would deprive the whole

[29] ibid. *Marks & Spencer plc*, para. 54.
[30] ibid. *Marks & Spencer plc*, para. 43.
[31] ibid. *Marks & Spencer plc*, paras. 31-34.

meaning of the freedom of establishment. Different treatment of companies based on residence must be founded on objective and justifiable grounds. Based on the case C-250/95 *Futura Participations and Singer*, a Member State would be acting in full accordanceif it taxed its resident parent on its worldwide profits from non-resident companies. Thus, the fact that the UK does not tax the worldwide profits of its resident parent companies does not justify a restriction on its group loss relief system to exclude non-resident companies.[32] The CJEU did not regard each justifiable ground from the UK as sufficient but considered all three taken together as legitimate objectives under the Treaties to restrict the freedom of establishment.[33]

Lastly, the CJEU examined the UK group loss relief system whether the measures are the least restrictive possible. The Court stipulated two indicators of when the prevention of a parent company to deduct foreign losses incurred by its subsidiaries should be seen as a breach of the freedom of establishment. Those two indicators can be found in para. 55 of the case and stated the following:

> "...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."[34]

The starting point is that a Member States is allowed to restrict the freedom of establishment with regards to deduction of foreign losses, based on legitimate grounds such as the ones the UK presented. Nonetheless, in the event where a non-resident subsidiary has exhausted all possibilities available in their State ofresidence to take their losses into account, which was not possible, the CJEU may consider the situation differently. If the losses incurred of such non-resident subsidiaries cannot be taken into account in any Member State and neither by a third party, such national law is disproportionate with respect to the freedom of establishment. The CJEU further established that the losses incurred must be definitive and final, they cannot

[32] ibid. *Marks & Spencer plc*, paras. 36-40
[33] ibid. *Marks & Spencer plc*, para. 51.
[34] ibid. *Marks & Spencer plc*, para. 55.

in any manner be used for future periods. Neither by them nor by any third party, or by a third party that has acquired the subsidiary.

2.1.3. Judgement

The CJEU ruled that Article 49 and 54 TFEU shall not preclude national legislation of a Member State to prevent foreign losses incurred by subsidiaries to be deducted by the resident parentcompany, even though the Member State allows losses from resident subsidiaries to be deducted. However, Article 49 and 54 TFEU shall preclude national legislation of a Member State in the event where the non-resident subsidiary has exhausted the possibilities available to deduct its losses in its own State of residence and where there cannot be any possibilities to take those losses into account in the future, either by the subsidiary or a third party. The losses in question must be definitive and final. Under such circumstances, a group loss relief system that prevents a resident parent from deducting the 'final' losses of its subsidiary is a disproportionate measure under EU-law and in breach of the freedom of establishment.[35]

2.3. The *Marks & Spencer* Doctrine on Foreign Subsidiaries

2.2.1. The General Effects of the *Marks & Spencer* Case

The doctrine of *Marks & Spence*r with regard to foreign subsidiaries established that a parent company can deduct the final losses of a subsidiary established in another EU Member State, when there is no possibility of those losses being used in their home state. The doctrine ensures that the parent company is not put in a disadvantageous position compared to those who have subsidiaries within their own jurisdiction.[36]

Shortly after the *Marks & Spencer* judgment, the CJEU dealt with Case C-231/05 *Oy AA* in 2007, the question was whether the Finnish Tax Authorities had breached EU-law by refusing to allow a Finnish parent company to deduct the losses of its Estonian subsidiary. The CJEU ruled that the Finnish Tax authorities had not breached the freedom of establishment by refusing to allow the deduction ofthe losses.[37] In Case C-337/08 *X Holding BV* from 2010, the question was whether the Dutch Tax Authorities had breached EU-law by refusing to allow a Dutch parent company to take the foreign losses of its German subsidiary into account. The CJEU ruled that the Dutch Tax Authorities had not breached EU-law, since the profits and losses of that non-

[35] ibid. *Marks & Spencer plc*, paras. 56-57.
[36] See *supra* note 6. Lang., pp. 67.
[37] See *supra* note 22. *OY AA*, paras. 63-64.

resident subsidiary are not subject to the fiscal legislation of the German tax system.[38]

The cases of *Oy AA* and *X Holding BV* implies the restrictive nature of the *Marks & Spencer* doctrine on the motion that it does not apply on general or absolute terms, but as a restrictive exception and last resort to uphold the objective of the freedom of establishment.

2.2.2. The Cases of *Holmen* and *Memira Holding*

In 2019, the CJEU applied the doctrine of *Marks & Spencer* in favour of the loss-making subsidiaries in the cases C-608/17 *Holmen* and C-607/17 *Memira Holding*. The facts of the cases involved Swedish parent companies that had incurred losses due to the liquidation of their subsidiaries situated in other Member States. The parent companies argued that they should be allowed to deduct these losses from their taxable profits.

The CJEU ruled that EU-law precludes national legislation of a Member State to deny a parent company the deduction of foreign losses resulting from the liquidation of a subsidiary, provided that the parent company can demonstrate that the subsidiary's losses could not have been taken into account in the Member State where it was resident. Furthermore, the CJEU also clarified that it is not necessary for the parent company to show that it received the assets of the subsidiary in the liquidation process, in order to be entitled to the deduction of the final losses.[39]

Overall, the cases *Holmen* and *Memira Holding* confirmed the doctrine of *Marks & Spencer* in terms of deducting foreign losses incurred by their non-resident subsidiaries, under the conditions that the losses cannot be used in the future and that they are 'final'.

2.2.2.1. Deduction of Foreign 'Final' Losses Incurred by Foreign Subsidiaries

Conclusively, the concept of 'final' losses refers to losses incurred by a subsidiary that are not capable of being used for tax relief in the jurisdiction in which the subsidiary is located. Typically, this occurs where the subsidiary has exhausted all possibilities for carrying forward or offsetting its losses against profits in the jurisdiction in which it operates. Under EU tax law, a parent company may be entitled to deduct these foreign 'final' losses incurred by its non-resident subsidiaries, subject to certain conditions. The most notable condition is that there must be no possibility of using the losses for tax relief in any other state.[40]

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[38] C-337/08, *X Holding BV* [2010] ECLI:EU:C:2010:89., para. 40-43.
[39] C-607/17, *Memira Holding* [2019] ECLI:EU:C:2019:510; C-608/17, *Holmen* [2019] ECLI:EU:C:2019:511.
[40] See *supra* note 12. Kollruss., pp. 3.; See *supra* note 24. van den Broek, Harm., pp. 59-61.

3. Applying the *Marks & Spencer* Doctrine on Permanent Establishments

3.1. Subsidiaries and Permanent Establishments

3.1.1. Subsidiaries

A subsidiary is a separate legal entity that is owned or controlled by a parent company. The parent company can own all or a portion of the subsidiary's stock or assets, nevertheless, the subsidiary is a distinct legal entity and operates its business independently from its parent company. Thus, a foreign or a non-resident subsidiary is a company that is incorporated in a foreign jurisdiction but has its parent or other subsidiaries in other jurisdictions.[41]

3.1.2. Permanent Establishments

A PE refers to a fixed place of business through which the parent entity carries out its business activities in a foreign country. A PE can be a branch, office, factory, warehouse, workshop, mine, or even a place where construction or assembly projects take place. Essentially, a PE is a physical location that is used for carrying out business operations, it lacks a legal personality of its own and cannot be separated from the general enterprise which it operates for.[42]

3.1.3. The Distinction between a Subsidiaries and PE:s from a Tax Perspective

As was stated, a subsidiary is a separate legal entity and liable to tax in its own State of residence, independently from its parent entity. A PE on the other hand is considered as a 'foreign investment' in the shape of a branch and for that reason, the PE must qualify to benefit tax treaties.[43] Despite their differences, the CJEU held its landmark Case C-307/97 *Saint-Gobain*, that Host States should accord branches of non-resident companies the same tax treatment as resident companies which includes local subsidiaries of foreign parent companies. Hence, the CJEU has established that there, in principle, should be no difference in treatment between PE:s and subsidiaries and that PE:s can benefit tax treaties.[44]

Since the PE lacks its own legal personality, its profits are taxed at the head office and thus

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[41] C-416/17, *Commission v. France* [2018] ECLI:EU:C:2018:811., paras. 29-46. C-194/06, *Orange European Smallcap Fund* [2008] ECLI:EU:C:2008:289., para. 41; C-540/11, *Levy and Sebbag* [2012] ECLI:EU:C:2012:581.

[42] Aarnio, Katri. 'Treatment of permanent establishments and subsidiaries under EC law: towards a uniform concept of secondary establishment in European tax law?', (2006), 15, EC Tax Review, Issue 1, p.18-26., p.19; C-79/85, *Segers* [1986] ECLI:EU:C:1986:308.

[43] Wattel, Peter Jacob. 'Corporate tax jurisdiction in the EU with respect to branches and subsidiaries; dislocation distinguished from discrimination and disparity; a plea for territoriality' (2003), 12, EC Tax Review, Issue 4, p.194-202., pp. 194.

[44] C-307/97, *Compagnie de Saint-Gobain v Finanzamt Aachen-Innenstadt* [1999] ECR I-6161., para. 56-59.

relieved by appropriate double taxation measures. The subsidiary's profits will be subject to double taxation in the resident State of its parent where the profits will be redistributed as dividends. Whether subsidiaries and PE:s should enjoy the same tax treatment with respect to offsetting foreign losses has been disputed in the past.[45]

3.1.4. Taxing a Non-Resident PE

According to Article 5 of the OECD Model Convention for Taxes on Income and on Capital from 2017, a PE is defined as "a fixed place of business through which the business of an enterprise is wholly or partly carried on."[46] The definition of a PE in Article 5 the OECD Model Convention essentially states the same meaning of a PE that can be found in the Parent-Subsidiary Directive[47] and the Interest Royalty Directive.[48]

Unlike PE:s, subsidiaries are considered as residents in the Member State they are established in due to their legal personality. Thus, they are subject to tax in their Member State of establishment as residents. For a PE, the tax principle of *source taxation* applies, namely where the economic activities have taken place. Despite being regarded as a non-resident company, Case C-311/97 *Royal Bank of Scotland* established that a PE should be subject to similar tax treatment to resident companies from a general standpoint.[49]

Furthermore, Article 7(2) of the OECD Model Convention states that the allocation of profits of a PE should be attributed to the PE as if it was a *separate and independent enterprise* if it engages in same or similar activities under same or similar conditions. AG Léger made an explicit reference to Article 7(2) in his opinion to Case C-253/03 *CLT-UFA SA* and argued that a PE and its head office should be treated as two legally distinctive entities.[50]

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[45] See *supra* note 43. Wattel., pp. 194.
[46] OECD, 'Commentaries on the Articles of the Model Convention' (Full Version) (OECD Publishing, 2019)., Article 5.
[47] European Council, *Council Directive on the common system of taxation applicable in the case of parent companies and subsidiaries of different Member States*, 23 July 1990, [90/435/EEC], OJ L 225. [Hereinafter "Parent-Subsidiary Directive"]., Article 2(2).
[48] European Council, Council Directive on a common system of taxation applicable to interest and royalty payments made between associated companies of different Member States, 3 June 2003, [2003/49/EC], OJ L157/49. [Hereinafter "Interest Royalty Directive"]., Article 3(c).
[49] C-311/97, *Royal Bank of Scotland* [1999] ECR I-2651., para. 27.
[50] Opinion of AG Léger in C-253/03, *CLT-UFA SA v Finanzamt Köln-West* [2006] ECR I-01831., para. 85.

3.2. The Relationship between Double Tax Treaties and EU-Law

3.2.1. Is there a Conflict between DTT:s and EU-Law?

As was seen in the *Lidl Belgium* decision, it is a matter of treaty interpretation when the CJEU has to consider DTT:s between Member States in their judgements. The CJEU examined whether the provision of the German-Luxembourg DTT was justified and proportionate in the light of the freedom of establishment. In terms of secondary Union-law, where a company that is resident in one Member State has a PE that operates in another Member State, Article 23(a) of the OECD Model Convention provides an exemption method to eliminate double taxation. The Resident State should not be allowed to tax the income attributable to the PE when such income "may be" taxed in the Source State of the PE.[51] Whereas secondary Union-law may enable the Resident State to tax income attributable to the PE.[52] For the purpose of the Thesis, the following sub-section will not elaborate on the relation between DTT:s and secondary EU-law, but only how DTT:s are interpreted in the light of EU primary law.

3.2.2. DTT:s versus EU Primary Law

According to Article 351(1) TFEU, the Tax Treaties that Member States have concluded with third countries before the accession to the EU are protected. Article 361(2) TFEU on the other hand, stipulates that the Member States must take all appropriate steps to eliminate the incompatibilities established and to assist each other to this with a common attitude. Hence, DTT:s between EU Member State has no protection under EU-law. Essentially speaking, primary EU-law always prevails over DTT:s that are concluded between EU Member States, irrespective of date and content. Whether a DTT can prevail over EU-law is rarely debated since the principle of primacy applies as the general rule, nonetheless, the interpretation of conflicting provisions between a DTT and the EU primary law is a comprehensive matter which requires a thorough analysis. In the following section, the Thesis will examine on one of the most essential cases concerning the application of the *Marks & Spencer* doctrine towards non-resident PE:s and the role of DTT:s in the application of EU-law.

[51] See *supra* note 46. OECD., Article 23(a).

[52] See e.g., European Council, *Council Directive on laying down rules against tax avoidance practices that directly affect the functioning of the internal market*, 12 July 2016, [EU/2016/1164], OJ L 193/1., Article 8.

3.3. The *Lidl Belgium* Case

3.3.1. Facts of the Case

Case C-414/06 *Lidl Belgium GmbH & Co. KG* v *Finanzamt Heilbronn* concerned the German resident claimant Lidl Belgium that established a PE in Luxembourg which generated losses during the tax year of 1999. Lidl Belgium wanted to offset these losses against its German profits, however, the German Tax Authorities claimed that such offset is not possible according to the DTT between Germany and Luxembourg. Nevertheless, the *Marks & Spencer* judgment provided such a precedent that the Federal Tax Court of Germany referred the question to the CJEU on whether the non-recognition of foreign PE losses is compatible with EU-law and whether the *Marks & Spencer* doctrine applies in the circumstances of the case.[53]

3.3.2. Reasoning of the CJEU

The CJEU asserted that the establishment of a PE falls under the scope of Article 49 TFEU and that the refusal to offset losses of a non-resident PE is the refusal of a tax advantage that is available for domestic PE:s. The Court was of the belief that the German Tax Authorities had restricted the freedom of establishment. Hence, the CJEU affirmed that the *Marks & Spencer* doctrine could apply to a PE, similar to a non-resident subsidiary. The CJEU referred to the *Marks & Spence*r case when assessing the justifiable grounds of Germany and held that it will apply the criteria's set out in para. 55 of the Marks & Spencer case in a cumulative manner. The Court found two grounds of justification to be relevant for the case at hand.[54]

Firstly, the CJEU acknowledged that it would undermine the balanced allocation of taxing rights if companies were given the right to choose in which Member State their losses would be taken into account. The CJEU also affirmed the same danger of double use of losses as a form of aggressive tax planning and that the refusal of taking foreign losses into account could be justifiable.[55] However, unlike the *Marks & Spencer* decision, the DTT between Germany and Luxembourg stipulated that the Home State does not have the right to tax because such a competence would neglect the objective of symmetrical treatment of profits and losses.[56]

The CJEU distinguished the circumstances of *Lidl Belgium* from *Marks & Spencer* in terms of

[53] See *supra* note 1. *Lidl Belgium*., paras. 8-13.
[54] ibid. *Lidl Belgium*., paras. 18-26.
[55] ibid. *Lidl Belgium*., paras. 27-37.
[56] ibid. *Lidl Belgium*., para. 33.

proportionality. The third condition of the *Marks & Spencer* doctrine relates to the notion that a domestic law may only be regarded as disproportionate when a non-resident subsidiary had exhausted the possibilities for taking losses into account in the Member State where the losses were incurred.[57] The CJEU found that the laws of Luxembourg gave such opportunity for Lidl Belgium, unlike the foreign subsidiaries in the *Marks & Spencer* case. The DTT clearly stressed the tax relation between Germany and Luxembourg in the sense that the Home State lacks any taxing rights. Thus, the Court emphasized the legitimate interest of Germany to exercise their right of taxation, and that their domestic laws and the application of the DTT was proportionate.[58]

3.3.3. Judgment

The CJEU ruled that Article 49 TFEU does not preclude a situation where a resident company of one Member State is refused to deduct losses incurred by a permanent establishment that resides in another Member State.[59]

3.4. Remarks

It has been established that the *Marks & Spencer* doctrine only applies in strict circumstances and not as a general right under the freedom of establishment.[60] The *Lidl Belgium* case is of special importance because it affirms that the *Marks & Spencer* doctrine is applicable on PE:s from a theoretical standpoint, even though the Court ruled in favor of the German Tax Authorities. The case underlines the nuances of the proportionality test in the sense that the CJEU has to weigh the tax autonomy of the Member States and the justification of the balanced allocation of taxation powers with each other.

The key factor that distinguished *Lidl Belgium* from Marks & Spencer was the fact that the DTT between Germany and Luxembourg offered an exemption to the non-resident PE which outweighed the general objective of free establishment, making the German restriction proportionate under EU-law. It seems that the existence of DTT between the Member States plays a role in assessment of objective comparability and grounds for restricting the freedom of establishment. For the purposes of the Thesis, the following section will elaborate further on the notion of objective comparability and the role of DTT in the application of the *Marks & Spencer* doctrine on non-resident PE:s.

[57] ibid. *Lidl Belgium*., para. 51.
[58] ibid. *Lidl Belgium*., para. 53.
[59] ibid.
[60] See *supra* note 6. Lang., pp. 60.

4. Nuances on the Objective Comparability Analysis and the Role of DTT:s

4.1. What is the Objective Comparability Analysis?

The objective comparability analysis is a legal standard established by the CJEU to assess whether a domestic tax rule that treats cross-border situations differently from domestic situations is compatible with the freedom of establishment. In the context of tax treatment towards non-resident subsidiaries versus non-resident permanent establishments, the objective comparability test examines whether the tax treatment of these two situations is objectively comparable in the relevant tax legislation of the Member State.[61] The test requires that cross-border situations should be treated the same as domestic situations, unless there is an *objective difference* that justifies different treatment. This means that any difference in tax treatment should be based on an actual factual difference between the parties in question concerned and should not be applied in an arbitrary or discriminatory way. Therefore, the objective comparability test is an essential tool for assessing whether a Member State's tax system complies with the EU freedom of establishment. By ensuring that the same tax rules apply to all cross-border situations, regardless of whether the company is a resident or non-resident, the test promotes equal treatment and prevents discrimination against non-resident companies.[62]

4.1.1. Resident PE and Non-Resident PE:s – Comparable Situations?

In the *Nordea Bank* Case, the legal context concerned provisions of a DTT between the Nordic countries[63] which enabled the Source State to tax the profits attributable to the PE. The Nordic DTT also stated that the Resident State of the undertaking shall grant the deduction in an amount equal to the income tax paid in the Source State.

Nordea Bank had its seat in Denmark and engaged in retail banking activity in Finland, Sweden and Norway through its PE:s, and it later deducted the losses incurred of the PE:s from its taxable income in Denmark. Since the activities of those PE:s was later restructured, Danish law enabled the Danish Tax Authorities to reincorporate Nordea Banks taxable profits and losses which had previously been deducted in respect of the business sold, and which had not been matched by subsequent profits. Nordea Bank claimed that the reincorporation made by the Danish Tax Authorities was in breach of Article 49 TFEU.[64]

[61] C-18/11, *Philips Electronics* UK [2012] EU:C:2012:532, para. 17; See *supra* note 18. Helminen.
[62] C-252/14, *Pensioenfonds Metaal en Techniek* [2016] ECLI:EU:C:2016:402., paras. 51-63; C-28/17, *NN* [2018] ECLI:EU:C:2018:526., para. 31; See *supra* note 9. *Bevola*., paras. 32-33, 35; See *supra* note 22. *OY AA*, para. 38; See *supra* note 38. *X Holding BV*., para. 22.
[63] Norway, Denmark, Iceland, Sweden, Finland.
[64] See *supra* note 21. *Nordea Bank*., paras. 10–14.

The question referred was whether the freedom of establishment precludes a company in its State of Residence to deduct losses incurred from its PE:s in the Source States in so far as they are not matched by profits in subsequent years, and where it must be assumed that the possibilities for applying the losses in question have been exhausted.[65]

The CJEU affirmed its decision in *Lidl Belgium* that allowing losses incurred by a foreign PE in another Member State to be taken account in the State of Residence of the principal company constitutes a tax advantage. The CJEU held that the Danish law was a restriction of the freedom of establishment and further held that the restriction may be deemed permissible if the situations are not objectively comparable or if it is justified by an overriding reason in the public interest.[66] Furthermore, the CJEU made an important statement by claiming that resident PE:s and non-resident PE:s are, in principle, not in comparable situations in relation to measures laid down by a Member State in order to prevent or mitigate the double taxation of a resident company's profits. A ground which the Danish Government invoked as a ground for justifying the restriction of EU-law.

However, by making the profits of permanent establishments situated in Finland, Sweden and Norway subject to Danish tax, the Kingdom of Denmark has equated those establishments with resident permanent establishments so far as concerns the deduction of losses. [67] Hence, the CJEU could proceed with a justification and proportionality assessment of Danish law and the Nordic DTT and ultimately held that the Danish law went beyond what was necessary in order to attain its objectives and the grounds for justification.[68]

4.2. DTT Exempt PE: Case of *Timac Agro*

4.2.1. Facts of the Case

In Case C-388/14 *Timac Agro*, the German resident company Timac Agro had a PE in Austria, which was later transferred to an Austrian subsidiary company belonging to the same group with Timac Agro. Timac Agro transferred its losses incurred in the PE to its German subsidiary, in full accordance with German law. Due to the transfer of losses, the losses were incorporated into the subsidiary's taxable profits that resulted into a situation where the subsequent losses could not be

[65] ibid. *Nordea Bank.*, para. 15.
[66] ibid. *Nordea Bank.*, paras. 18–23.
[67] ibid. *Nordea Bank.*, para. 24; See also C-170/05, *Denkavit Internationaal and Denkavit France* [2006] EU:C:2006:783, paras. 34, 35.
[68] See *supra* note 21. *Nordea Bank.*, paras. 36–40.

taken into account in Germany.[69]

The DTT between Germany and Austria further established that the Source State can only tax the profits to the extent to which they are attributable to the PE. More importantly, the revenue from Austria and assets situated in Austria which are taxable in turn taxable in Austria shall be excluded from the basis of assessment for German taxation.[70]

Since it was no longer possible for Timac Agro to deduct the losses anywhere, the CJEU deemed the losses to be final because the PE continued its operation under the Austrian subsidiary. The restriction in question concerned an unfavorable treatment that may discourage a domestic company from conducting business through a PE in a different Member State than where it is headquartered.[71]

4.2.2. Objective Comparability between a Resident and Non-Resident PE

The CJEU addressed the objective comparability between the Austrian PE and the German PE before it could address the justification grounds and the proportionality test. The CJEU affirmed its precedent stance from the *Nordea Bank* decision[72] by establishing that there is, in principle, no comparability between a resident and non-resident PE. The DTT between Germany and Austria played a significant role in the CJEU:s reasoning. The Court found that under the DTT, Germany did not have authority over taxation of profits generated by such a PE, and as a result, it cannot permit loss deduction in Germany.[73] Therefore, the status of a PE in Austria is not analogous to that of a PE in Germany with respect to measures put in place by Germany to deter or alleviate double taxation of profits for resident companies.[74]

4.2.3. Judgement

The CJEU ruled that Article 49 TFEU does not preclude the existence of a tax system of a Member State whereby a resident company transfers a permanent establishment to a non-resident company within the same group situated in another Member State, and the previously deducted losses pertaining to the transferred establishment are added back to the taxable profit of the transferring company. This is especially true when the income produced by the PE is exempt from tax under

[69] C-388/14, *Timac Agro Deutschland GmbH v Finanzamt Sankt Augustin* [2015] ECLI:EU:C:2015:829., paras. 9–13.
[70] ibid. *Timac Agro*., paras. 15-18.
[71] ibid. *Timac Agro*., para. 25.
[72] See *supra* note 21. *Nordea Bank*., para. 24.
[73] See *supra* note 69. *Timac Agro*., para. 28.
[74] ibid. *Timac Agro*., para. 65.

a DTT where the establishment's parent company is based.[75]

Furthermore, Article 49 TFEU allows for the interpretation that a Member State's tax system, such as the one in question, may also prohibit the resident company from including the losses of the transferred establishment in its tax base if the profits of the establishment are subject to taxation only in the Member State where the facility is situated.[76]

4.3. Absence of a DTT: Case of *Bevola*

4.3.1. Facts of the Case

Case C-650/16 *A/S Bevola and Jens W. Trock* concerned the Danish company Bevola that sought to subtract the losses experienced by its PE in Finland from its taxable base in Denmark. The company argued that since the PE no longer existed in that year, loss relief could not be claimed in Finland. However, the Danish Tax Authorities rejected the deduction, citing that revenue or expenses linked to a foreign PE cannot be included in a taxpayer's taxable base, except if the taxpayer has opted for the Danish international joint taxation scheme. Under this scheme, a Danish company must amalgamate the benefits and losses of all its group companies, actual properties, and PEs for at least ten years, despite their residence. [77]

Bevola appealed this decision to the Danish Eastern Regional Court, which referred the case to the CJEU in December 2016. The CJEU was asked to assess whether the Danish laws on cross-border loss relief, under equivalent circumstances to those in the CJEU ruling in the *Marks & Spencer* case, adhere to the freedom of establishment. Under these laws, deductions for losses from foreign PEs are not permitted, unless the group opts for the Danish international joint taxation scheme. However, losses acquired by domestic branches can be deducted, with or without the scheme.[78]

4.3.2. Objective Comparability between a Resident and Non-Resident PE

The CJEU conducted an objective comparability assessment between the resident Danish PE and the non-resident PE in Finland. Having verified that the situation falls under the scope of the

[75] ibid. *Timac Agro*., para. 58.
[76] ibid. *Timac Agro*., paras. 65-66.
[77] See *supra* note 9. *Bevola*., paras. 7–12.
[78] ibid. *Bevola*, para. 12.

freedom of establishment, the Court proceeded to examine whether there is a differentiation in treatment between Danish companies with a Danish PE and those with a PE situated in another EU Member State.[79] According to the Danish rules on cross-border loss relief, foreign PEs are not permitted an allowance for final losses unless the company chooses to use international joint taxation.[80] However, final losses experienced by domestic PEs can be deducted, irrespective of whether the joint taxation scheme is being employed. In such circumstances, Danish companies encounter unfair treatment compared to those that own a PE in Denmark and have experienced final losses.[81] Furthermore, the Court noted that this inequality in treatment is liable to discourage Danish resident companies from exploiting their freedom to establish businesses. It deemed this conclusion unaffected by the capability to opt for the international joint taxation scheme, which practices stringent requirements.[82]

Regarding whether this discrepancy in treatment is applicable to situations that are objectively comparable, the Court outlined that this should be determined with respect to the purpose of the Danish regulations under consideration. Since such regulations were created to prevent double loss deduction, the Court concluded that a Danish company with a Danish PE and a Danish company with a non-resident PE's situations are alike, regarding this specific objective. This outcome is consistent with the Danish laws' broader intention to make certain that the company's taxation is commensurate with its capacity to pay taxes. Hence, the CJEU held that the resident Danish PE was objectively comparable to the Finish non-resident PE.[83]

4.3.3. Judgment

The CJEU held that Article 49 TFEU does preclude a Member State's regulations from preventing a resident company, which has not chosen an international joint taxation scheme, from offsetting losses incurred by a permanent establishment located in another EU Member State from its taxable profit must not exist. This mandate upholds as long as the company in question has reaped all the income deduction options available under the establishment's residing Member State's law and has halted receiving any revenue from that establishment. This results in the losses being ineligible for account inclusion in the Member State, which it is the national court's responsibility to verify.[84]

[79] ibid. *Bevola*, paras. 20–21.
[80] ibid. *Bevola*, paras. 23-26.
[81] ibid. *Bevola*, paras. 31–33.
[82] ibid. *Bevola*, paras. 24.
[83] ibid. *Bevola*, paras. 36-40.
[84] ibid. *Bevola*, paras. 39, 53, 66.

4.4. Comment

The case of *Bevola* is an exceptional case in many aspects. It is a case, unlike the rest, where the CJEU established an objective comparability between a resident and non-resident PE, and it granted the *Marks & Spencer* exception to a PE. Nonetheless, the factual constellations in *Bevola* and *Timac Agro* were evidently not the same. It seems clear that the CJEU makes a distinction between DTT exempt PE:s on one hand and PE:s that wish to be exempted in the event where no DTT is relevant to the matter. However, from an observer's perspective, it seems odd that the CJEU would claim no objective comparability between resident and non-resident PE:s in one case, but claim the opposite in another. It proves the complexity and the thorough link between the facts of the case and the law at hand that needs to be examine before applying the EU-law on domestic tax situations, as well as the restrictive nature of the *Marks & Spencer* doctrine.

The cases that have been examined in the Thesis up until this point represents the current established precedent case-law on the issue of deduction of foreign losses incurred by non-resident PE:s. In the following section, the Thesis will thoroughly examine the *W AG* case in order to analyze whether the CJEU, indeed, wants to abandon the doctrine of *Marks & Spencer* towards non-resident PE:s. The following section will furthermore elaborate on the different views that authors seem to have on the matter.

5. The *W AG* Case: The End of the *Marks & Spencer* Doctrine?

5.1. The *W AG* Case

5.1.1. Facts of the Case

In September 2022, the CJEU gave its ruling in Case C-538/20 *Finanzamt B* v *W AG*. The facts of the case concerned the company W AG, a resident in Germany for tax purposes with a PE in the UK. During 2007, the PE ceased its operations and W AG claimed the losses incurred by it as a deduction in the company's tax return for that same year.[85]

The German Tax Authorities did not allow the deduction of the losses incurred, on the basis that the UK-Germany DTT exempted the profits attributable to the PE in the country of the company's residency from taxation, which in turn, precipitates that the losses also fall under exemption from relief.[86] W AG proceeded to challenge this decision on the grounds that German law alongside with the UK-Germany DTT is in breach of the freedom of establishment. In this context, the CJEU was solicited to provide a rule based on another ruling linked to deductible losses in the *Bevola* case.[87]

The question referred to the CJEU was whether Article 49 and 54 TFEU should be interpreted as a preclusion against the domestic system of a Member State where a resident company in that Member State may not deduct from its taxable profits the final losses incurred by its PE situated in another Member State where the State of residence has waived its power to tax the profits of that permanent establishment under a double taxation convention.[88]

5.2.1. The Court's Assessment on Objective Comparability

The CJEU conducted its test of objective comparability by referring to its previous case-law, namely *Nordea Bank*, *Timac Agro* and *Bevola*. The *Bevola* decision affirmed the notion of a right to exercise their activity in other Member States through a subsidiary, branch, or agency in the EU under the freedom of establishment.[89] The Court further affirmed that the *Bevola* case applies in the sense of prohibiting the Member State of Residence from hindering the establishment in another Member State of one of its nationals or of a company incorporated under its legislation.[90]

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[85] See *supra* note 10. *Finanzamt B v W AG*., paras. 7–10.
[86] ibid. *W AG*., paras. 5–6.
[87] ibid. *W AG*., para. 11.
[88] ibid. *W AG*., para. 12.
[89] ibid. *W AG*., paras. 14, 21.
[90] ibid. *W AG*., paras. 18–20.

The CJEU acknowledged that the exclusion of letting losses incurred by a PE situated in another Member State to be taken into account creates a difference in treatment which could discourage a resident company from carrying on its business through such a PE. Such difference in treatment will only be deemed permissible if the situations concerned are not objectively comparable. This is settled by examining the aim pursued by the national provisions at issue.[91]

As has been established, the CJEU makes a distinction between resident and non-resident PE:s when the DTT stipulates a clear distinction between the States in their tax relation, see *Timac Agro*. In the present case, the CJEU held that there is a distinction the circumstances of W AG from the case of *Bevola*. In the *Bevola* decision, the resident company that wanted to deduct the losses by its non-resident PE had not, by means of a double taxation convention, waived its power to tax that establishment's profits. Denmark had unilaterally decided the losses shall not be taken into account, unless the parties opt for an international joint tax scheme.[92]

The CJEU seemed firmly convinced that the DTT between UK and Germany in the present case posed a situation where Germany had waived its power to tax profits attributable to non-resident PE:s. The Court has stated that it examines objective comparability based on the aim pursued by the national provisions at issue. The aim of the provisions at hand in the DTT was to prevent or mitigate the double taxation of profits and, symmetrically, the double taking into account of losses. In such a situation, where the resident Member State has no taxing power over the source, the lack of recognition of losses of a tax treaty-exempt non-resident PE cannot be considered the same as a resident PE where the resident Member State has taxing jurisdiction.[93]

Thus, according to the CJEU, the fact that a Member State waives its power to tax foreign incurred losses in the light of such objectives amounts into a domestic and cross-border tax situation that are not objectively comparable with each other. As a result, the unequal treatment of the two situations does not infringe upon the freedom of establishment, and there is no obligation under EU legislation to subtract the final losses of the foreign PE at the parent firm level. The CJEU also concluded that this verdict does not negate the decision made in the *Bevola* case since Denmark renounced its authority to execute its tax rights on the profits and losses sustained in another Member State unilaterally through national law in the latter ruling.[94]

[91] ibid. *W AG*., paras. 18–19.
[92] ibid. *W AG*., paras. 24–25.
[93] ibid. *W AG*., para. 25.
[94] ibid. *W AG*., paras. 25–29.

The CJEU did not proceed with any further assessment of justifications nor proportionality since it held that there was not objective comparability between the non-resident PE and the resident PE in the case at hand.

5.3.1. Judgement

The CJEU ruled that Article 49 and 54 TFEU does not preclude a Member State's tax system to prevent a company that resides in that Member State to subtract final losses incurred by its permanent establishment located in another Member State from its taxable profits. This is permissible when the Member State of residence has forgone its authority to tax the profits of that permanent establishment based on a double taxation treaty. Since this was not the case, the requirement of objective comparability was not met.[95]

5.2. The Debate on the Current Status of the *Marks & Spencer* Doctrine on PE:s

There are conflicting views regarding the applicability of the *Marks & Spencer* doctrine in non-resident PE:s cases. Some authors[96] argue that the CJEU abandoned the doctrine with the *Timac Agro* decision, and that the *W AG* case was the nail in the coffin. Others[97] maintain their opinion that final losses of any non-resident PE can be objectively compared to those of a resident PE, as declared in the *Bevola* decision.

5.2.1. The 'Beginning of the End' for the Doctrine

Georg Kofler claims that the *W AG* case affirms the precedence of the *Timac Agro* decision, but also departure from the established legal standard of comparability that was set out in the *Lidl Belgium* case. According to Kofler, the *W AG* judgement should be understood in the sense that not even 'final' losses are to be taken into account in terms of the proportionality of the domestic laws. The existence of a DTT where the resident Member State waives its power to tax foreign profits and losses restricts the *Marks & Spencer* doctrine towards PE:s one step further.[98]

Kofler believes that the political state of the EU during *Marks & Spencer* and *Lidl Belgium* posed a conflict of interest where the CJEU had to find a solution to uphold the objectives of the internal market, and also secure tax sovereignty of the Member States.[99] In a much earlier publication,

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[95] ibid. *W AG*., paras. 28-29.
[96] Georg Kofler.
[97] Thomas Kollruss.
[98] See *supra* note 11. Kofler., pp. 20–21.
[99] See *supra* note 8. Kofler., pp. 110.

Michael Lang came to a similar conclusion alike Kofler, namely, that the Marks & Spencer doctrine was subject to its time in a union with politically unharmonized policies in the area of tax while also balancing between domestic tax autonomies and the competence of the EU on the matter.[100]

Kofler describes the *W AG* judgement as an 'abandonment' of the doctrine towards PE:s and that the whole body of the Marks & Spencer case-law is in doubt. By further affirming the ruling from *Timac Agro*, Kofler is under the belief that the CJEU is not interested in applying the doctrine towards PE:s unless the circumstances are of such exceptional nature such as the ones in *Bevola*. If one may argue from a *de facto* standpoint, Kofler sympathizes with AG Kokott as she once pointed out, it is indeed "very difficult to identify any cases in which it might apply".[101] Kofler is not necessarily interested in whether case *W AG* is the end of the doctrine, but rather the pattern of case-law that it represents. Namely, a clear pattern where the CJEU becomes more restrictive in its application of the doctrine and has now reached a dead end.[102]

5.2.2. The Doctrine has always been Restrictive in Nature

Unlike Kofler, Thomas Kollruss is skeptical to the notion that the CJEU wants to abandon its own line of case-law. He does not believe that the *W AG* decision poses an end to the doctrine towards PE:s, as Kofler seems to argue for. Kollruss renounces the premise that case *Bevola* should, in any manner, be seen as a default guarantee every non-resident PE with final losses is objectively comparable to a resident PE. According to Kollruss, Kofler seems to disregard the narrow discretion of the *Marks & Spencer* doctrine considering the complexity of the objective comparability analysis, and that the doctrine never amounted into a general EU obligation for Member States to take foreign final losses into account.[103]

From an observer's perspective, it may be possible to view the *Marks & Spencer* line of case-law as inconsistent. Namely, that one case rejects objective comparability between resident and non-resident, while the other one affirms comparability and obliges the Member States to take the losses into account.[104] Kollruss attempts to narrow the discourse by establishing the objective difference between a case where a DTT stipulates a clear relation of taxation powers between the

[100] See *supra* note 8. Lang., pp. 539-540.
[101] Opinion of AG Kokott in C-172/13, *European Commission v United Kingdom of Great Britain and Northern Ireland* (*Marks & Spencer II*) [2015] EU:C:2014:2321., para. 38.
[102] See *supra* note 11. Kofler., pp. 22–23.
[103] See *supra* note 12. Kollruss., pp. 6–8.
[104] ibid. Kollruss., pp. 2.

Member States on one hand, and where such provisions of international law is inapplicable on the other.[105]

The CJEU wants to respect the tax autonomy of the Member States, hence, if two Member States already have come to an arrangement, that must be weighed to the objective of upholding the freedom of establishment. In the event where no DTT applies, a legal gap is left in which EU-law can fill by having the interest of the taxpayer in cross-border tax situations. Kollruss is firmly convinced that the *W AG* decision closes the circle, but not in the same way as Kofler might argue. The case of *W AG* does not pose any threat to future application of the *Marks & Spencer* doctrine, as long as the situations are objectively comparable. This has always been the position of the CJEU and thus, the *W AG* decision simply follows the line of case-law established in *Lidl Belgium* and *Timac Agro*.[106]

5.2.3. Dissenting Opinions

Other writers have also expressed their opinions on the matter. Ismer and Kandel agrees with Kollruss on the motion that the CJEU does not act inconsistent in its line of case-law. However, unlike Kollruss, they conclude that objective comparability is not possible in treaty-exempt cases, especially in regard to non-resident PE:s.[107] Interestingly, there also seem to be a dissenting stance by Johanna Hey, who concludes that final losses from non-resident PEs must be considered by the Member State of residence, even if the PE is fully exempt under a DTT.[108]

[105] ibid. Kollruss., pp. 7.
[106] ibid. Kollruss., pp. 8.
[107] See *supra* note 8. Ismer., Kandel., pp. 582–584.
[108] Hey, Johanna. 'Taxation of Business in the EU: Special Problems of Cross-Border Losses and Exit Taxation, in Research Handbook on European Union Taxation Law' (Edward Elgar Publishing, 2020)., pp. 204-206.

6. The Author's Analysis

Evidently, the doctrine of *Marks & Spencer* is applicable towards PE:s from a theoretical standpoint. Otherwise, the CJEU would have never referred to the *Marks & Spencer* decision in its reasoning to case *Lidl Belgium*. Furthermore, the CJEU affirmed the motion that the doctrine can, also in practice, apply to non-resident PE:s in the *Bevola* decision. Nonetheless, there is a clear distinction between subsidiaries and PE:s from a cross-border tax perspective. One is a separate legal entity that operates independently from its parent company. While the other lacks a legal personality and is simply regarded as a physical extension of its parent company. Despite this clear distinction, the line of case-law from CJEU seems clear on one matter. There should be no difference in treatment between resident and non-resident undertakings, and this applies in principle, to the same extent towards subsidiaries as it does towards PE:s.

Moving on, the case of *W AG* is an interesting case to examine for the purpose of establishing the *de facto* status of the *Marks & Spencer* doctrine towards non-resident PE:s. Nevertheless, the Author of the Thesis does not consider the CJEU:s decision in *W AG* as exceptional, in the same sense as Kofler seems to believe. It is the view of the Author that Kollruss conducted the most accurate interpretation of the CJEU:s line of case-law on the matter in question. The CJEU acknowledged its precedence in both *Timac Agro* and *Bevola*, and simply concluded that the circumstances of *W AG* were more similar to its precedence of *Timac Agro*, as well as *Lidl Belgium*. Kofler seems to believe that the CJEU has *de facto* abandoned the doctrine by shifting the focus to the objective comparability analysis. Since the CJEU further established an even more restrictive interpretation of objective comparability in *W AG*, Kofler claims that the doctrine has, in practice, been abandoned.

Kollruss underlines an important notion, namely, that the objective comparability analysis is necessary and that its legal assessment is complex in nature. On that point, Kofler seems to overlook that the CJEU has always distinguished the principal nature of the difference between resident and non-resident PE:s on one hand, and situations where a DTT creates new circumstances for the parties. The role of the DTT and whether a Member State waives its power to tax is a critical part of the objective comparability analysis that needs to be taken into account.

If the question asked is whether the *W AG* decision was a *de facto* abandonment of the doctrine, the Author believes that Kollruss holds the most accurate view. The CJEU did not abandon the doctrine, but simply upheld its tradition of being a restrictive exception.

However, Kofler also underlines a crucial notion in this debate as well, namely, that the line of case-law indicates a clear pattern where the CJEU becomes more restrictive in its language and approach for each case that comes. Even though the *W AG* decision may not have been the nail on the coffin which Kofler believes it to be, he still believes that this is the 'beginning of the end' for the doctrine. Despite going in full defense for the CJEU and the doctrine, Kollruss does not deny that this topic will be subject for future debate in the literature. Kollruss seems firmly convinced that the CJEU has acted consistent throughout its entire line of case-law and that an abandonment is out of question. The Author of the Thesis believes that Kollruss overlooks the fact that the CJEU has become more restrictive in its language and approach throughout the years. In fact, Kollruss himself claims that if the case and its factual constellations of *Marks & Spencer* would have been brought before the CJEU today, the Court would have not granted the exception.

Knowingly or not, Kollruss indirectly acknowledges the restrictive development of case-law which Kofler underlines. Whether the *W AG* decision in particular was 'the end' or 'the beginning of the end' is actually not interesting. Ismar, Kandal, Kofler and Kollruss all seem to agree on one point, that this debate is far from settled in the literature. Therefore, the actual status of *W AG* will not be settled until the next upcoming case where the CJEU will have to choose between an even more restrictive approach in the light of *Lidl Belgium*, *Timac Agro* and *W AG*, or to hold its ground by underlining the precedence of *Bevola*.

The Author asserts that the CJEU has in no manner indicated that it wants to overlook the objectives of equal treatment between resident and non-resident PE:s in cross-border arrangements. The Court has acted consistent by honoring the restrictive nature of the *Marks & Spencer* doctrine throughout its entire line of case-law. Nonetheless, as Kofler and Lang have highlighted, the political reality of the EU and the balance between Union and Member State competence in areas of taxation has changed rapidly the past decade. Due to the rise of OECD influence in EU-law and new secondary tax legislative initiatives that harmonizes the national laws of the Member States, the need for the CJEU to uphold its fundamental freedoms through case-law seems outdated. Hence, the Author believes that the *W AG* case, following *Lidl Belgium* and *Timac Agro*, indicates that the CJEU acknowledges the problems with the application of the *Marks & Spencer* doctrine. Thus, perhaps the CJEU does not want to exclude a legal position which makes it suitable for them to eventually or potentially abandon the doctrine in the future.

7. Conclusion

The Thesis concludes that the doctrine of *Marks & Spencer*, in terms of allowing a resident company to deduct the foreign final losses of a non-resident subsidiary, is applicable towards a non-resident PE. The CJEU makes no principal distinction between a subsidiary and a PE in cross-border tax situations. However, the CJEU believes that there is a principal distinction a resident and a non-resident PE with regard to deduction of foreign final losses. Furthermore, the Court will not grant the Marks & Spencer exception if the resident and non-resident PE:s are not objectively comparable to each other. In the event where a DTT exists between the Member State of the resident company and the Member State where the non-resident PE incurred its losses, and where the resident Member State has waived its power to tax foreign profits and losses, the CJEU holds the resident and non-resident PE:s are not objectively comparable, see *Timac Agro*. However, in the event where there is no international joint tax scheme between the Member States, the resident and non-resident PE may be regarded as objectively comparable, see *Bevola*. In the case of W AG, the factual constellations drew the CJEU:s attention to its decisions in *Lidl Belgium* and *Timac Agro* due to the DTT between Germany and the UK and where Germany had waived its power to tax foreign profits and losses. Nonetheless, the case of *W AG* is subject to a pattern of case-law where the CJEU is becoming more restrictive in its language and approach throughout its line of case-law. Thus, the *W AG* decision itself may not have been an abandonment of the *Marks & Spencer* doctrine, but the case is subject to one of many indicators that the CJEU wants to prepare itself for an eventual or potential abandonment in the future.

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