Reports of Cases

OPINION OF ADVOCATE GENERAL
KOKOTT
delivered on 19 July 2012 [1]

Case C-123/11

A Oy

(Reference for a preliminary ruling from the Korkein hallinto-oikeus (Finland))

(Tax law — Freedom of establishment — Directive 2009/133/EEC — National income tax law — Merger of two companies resident in different Member States — Deductibility of losses of the transferring company in the Member State of the receiving company)

I – Introduction

1. The name Marks & Spencer is actually that of a chain of department stores. In the Court's case-law on tax law, however, it stands for an express recognition that the allocation of taxation powers among the Member States may justify restrictions of the freedom of establishment. [2] In the Member States' case-law and in the works of commentators, on the other hand, the name Marks & Spencer appears also to be synonymous with chaos and despair. [3]

2. This is due to a single sentence of approximately 100 words which was formulated by the Court in the judgment named after Marks & Spencer and which describes the circumstances in which the Member States may be obliged, exceptionally, to take into account losses of non-resident subsidiary companies when taxing their resident parent companies. In spite of so many words, it is not clear how far that exception extends and whether – in view of the Court's subsequent case-law – it still exists at all.

3. The present reference for a preliminary ruling could provide an opportunity to put an end to the confusion which has arisen because of that exception. The taxable Finnish company in the main proceedings seeks to rely on the exception formulated by the Court. It wishes to merge with a Swedish subsidiary and to use the latter's accumulated Swedish losses in future in Finland, which however is not allowed by the Finnish tax rules.

1 — Original language: German.

2 — Case C-446/03 *Marks & Spencer* [2005] ECR I-10837.

3 — See, for example, *Cordewener*, Cross-Border Loss Relief and the 'Effet Utile' of EU Law: Are We Losing It? EC Tax Review 2011, p. 58.

II – Legal context

A – *Union law*

1. The freedom of establishment

4. Article 49 TFEU regulates the freedom of establishment as follows:

'Within the framework of the provisions set out below, restrictions on the freedom of establishment of nationals of a Member State in the territory of another Member State shall be prohibited. Such prohibition shall also apply to restrictions on the setting-up of agencies, branches or subsidiaries by nationals of any Member State established in the territory of any Member State.

Freedom of establishment shall include the right to take up and pursue activities as self-employed persons and to set up and manage undertakings, in particular companies or firms within the meaning of the second paragraph of Article 54, under the conditions laid down for its own nationals by the law of the country where such establishment is effected, subject to the provisions of the Chapter relating to capital.'

5. Article 54 TFEU extends the scope of the freedom of establishment as follows:

'Companies or firms formed in accordance with the law of a Member State and having their registered office, central administration or principal place of business within the Community shall, for the purposes of this Chapter, be treated in the same way as natural persons who are nationals of Member States.

…'

2. The Tax Merger Directive

6. Directive 2009/133/EC[4] ('Tax Merger Directive') regulates the tax consequences of certain cross-border mergers of limited liability companies. Recitals 2 and 3 explain the purpose of the Tax Merger Directive as follows:

'(2) The grouping together of companies of different Member States may be necessary in order to create within the Community conditions analogous to those of an internal market and in order thus to ensure the effective functioning of such an internal market. Such operations ought not to be hampered by restrictions, disadvantages or distortions arising in particular from the tax provisions of the Member States. …

(3) Tax provisions disadvantage such operations, in comparison with those concerning companies of the same Member State. It is necessary to remove such disadvantages.'

4 — Council Directive 2009/133/EC of 19 October 2009 on the common system of taxation applicable to mergers, divisions, partial divisions, transfers of assets and exchanges of shares concerning companies of different Member States and to the transfer of the registered office of an SE or SCE between Member States (OJ 2009 L 310, p. 34), which codified Council Directive 90/434/EEC of 23 July 1990 with the same title (OJ 1990 L 225, p. 1). This Directive is not to be confused with Council Directive 2005/56/EEC of the European Parliament and of the Council of 26 October 2005 on cross-border mergers of limited liability companies (OJ 2005 L 310, p. 1), which deals with the company-law aspects of certain cross-border mergers.

7. Recital 4 describes the path taken for that purpose by the Tax Merger Directive:

‘It is not possible to attain this objective by an extension at Community level of the systems in force in the Member States, since differences between these systems tend to produce distortions. Only a common tax system is able to provide a satisfactory solution in this respect.’

8. Specifically for dealing with tax losses of companies, recital 9 provides as follows:

‘It is also necessary to define the tax regime applicable to certain provisions, reserves or losses of the transferring company and to solve the tax problems occurring where one of the two companies has a holding in the capital of the other.’

9. Finally, recital 14 states as follows:

‘One of the aims of this Directive is to eliminate obstacles to the functioning of the internal market, such as double taxation. In so far as this is not fully achieved by the provisions of this Directive, Member States should take the necessary measures to achieve this aim.’

10. The scope of the Tax Merger Directive extends, according to Article 1(a), to ‘mergers … involving companies from two or more Member States’. Article 2(a)(iii) defines ‘merger’ as an operation whereby, inter alia, ‘a company, on being dissolved without going into liquidation, transfers all its assets and liabilities to the company holding all the securities representing its capital’. Article 3 of the Tax Merger Directive lays down what is meant by ‘company from a Member State’.

11. With regard to losses of the transferring company, the Tax Merger Directive contains only one provision in Article 6:

‘To the extent that, if the operations referred to in Article 1(a) were effected between companies from the Member State of the transferring company, the Member State would apply provisions allowing the receiving company to take over the losses of the transferring company which had not yet been exhausted for tax purposes, it shall extend those provisions to cover the takeover of such losses by the receiving company’s permanent establishments situated within its territory.’

B – *Finnish law*

12. According to Article 7(1) of the Convention between the Republic of Finland and the Kingdom of Sweden for the avoidance of double taxation with respect to taxes on income and capital, the profits of a company resident in Sweden may be taxed in Finland only if the profit is attributable to a permanent establishment in Finland.

13. Under Finnish income tax law, losses in a tax period may be carried forward to succeeding tax periods. Paragraph 119(1) and (2) of the Finnish Tuloverolaki (Law on income tax), provides as follows:

‘A loss arising in the tax year from business activity and agriculture shall be deducted from the income from business activity and agriculture in the following ten tax years if an income is obtained.

Business loss refers to a financial loss that has been calculated in accordance with the Law on business income tax. Agricultural loss refers to a financial loss that has been calculated in accordance with the provisions of the Law on agricultural income tax.’

14. In the case of a company merger, Paragraph 123(2) of the Finnish Law on income tax provides as follows with regard to losses of the transferring company:

'Upon a merger of companies or the division of a company, the receiving company shall have the right to deduct from its taxable income any loss made by the merged or divided company in accordance with Paragraphs 119 and 120, provided that the receiving company or its shareholders or members, or the company and its shareholders or members jointly, have owned more than one half of the shares of the merged or divided company from the beginning of the loss-making year …'

15. In addition, according to the Finnish case-law, the right to take over a transferring company's loss is subject to the condition that the merger is not being carried out solely for that purpose.

III – Facts and questions referred

16. The main proceedings concern a preliminary ruling on Finnish corporation tax. This had been requested by A Oy ('the taxable company') from the Keskusverolautakunta ('Central Tax Board') in order to clarify with binding effect a question of tax law concerning the transfer of losses.

17. The taxable company resident in Finland holds all the shares in the Swedish company B AB. This subsidiary company has in the meantime ceased trading after previously operating three retail stores in Sweden. However, it still has liabilities arising from two long-term leases of business premises. In the Swedish taxation procedure the subsidiary's resultant losses for the period 2001 to 2007 were found to be SEK 44.8 million, which at the current rate of exchange is approximately EUR 5 million.

18. The taxable company now plans a merger with its Swedish subsidiary, which would result in the dissolution of the subsidiary and the acquisition of all its assets by the taxable company.

19. In the preliminary ruling of 25 March 2009, the Central Tax Board took the view that, after the merger, the taxable company would not be able to deduct the losses of its Swedish subsidiary in connection with Finnish corporation tax.

20. The case is now before the Korkein hallinto-oikeus (Supreme Administrative Court), which has held that the Finnish provisions do not allow a loss by a merged company to be taken over if it has its registered office in another country and its losses cannot be attributed to a Finnish permanent establishment. However, the referring court is uncertain whether that interpretation is compatible with Union law and, in particular, the freedom of establishment. Against that background, two questions have been referred to the Court for a preliminary ruling:

1) Are Articles 49 and 54 TFEU to be interpreted as meaning that a receiving company may, in the context of its taxation, deduct the losses of a company which was previously resident in another Member State and which has merged with the receiving company, when those losses arise from the merged company's business activity in that other Member State in the years prior to the merger and when no permanent establishment remains for the receiving company in the State of residence of the merged company and, under national law, the receiving company may deduct losses of the merged company only if the latter is a resident company or the losses arose in the permanent establishment situated in that State?

2) If the answer to the first question is in the affirmative, do Articles 49 and 54 TFEU have a bearing on whether the loss to be deducted is calculated in accordance with the tax legislation of the receiving company's State of residence, or should the losses found according to the law of the State of residence of the company which is to be merged be considered as deductible losses?

IV – Legal assessment

21. The questions referred are admissible [5] in the context of the main proceedings which are concerned with the tax consequences of a situation which has not yet arisen. I shall therefore refer to current Union law as the basis for replying to them.

A – *First question: transfer of accumulated loss*

22. In essence, the first question from the referring court is whether Union law precludes a national provision which, in the case of a merger, in principle allows the receiving company to use the transferring company's accumulated loss, but excludes this with regard to losses from business activity which is not subject to Finnish taxation (foreign accumulated loss).

23. In order to give the referring court a helpful reply concerning the applicable Union law, [6] I shall not confine my inquiries to the freedom of establishment regulated in Articles 49 and 54 TFEU, because Union law has its own legislation for the tax consequences of cross-border company mergers, namely the Tax Merger Directive. I shall begin my examination with that more specific measure.

1. Application of the Tax Merger Directive

24. Article 1(a) of the Tax Merger Directive provides that the Member States are to apply the directive to any merger involving companies from two or more Member States. Under Article 2(a)(iii), a merger arises where a company takes over a wholly-owned subsidiary. The taxable company resident in Finland plans to take over its Swedish subsidiary, in which it holds all the shares. The referring court has also found that both companies meet the requirements concerning company form, thus fulfilling the conditions of Article 3(a) of the Tax Merger directive, which in conjunction with Annex I Part A, lists the forms which are to be regarded as 'companies from a Member State' within the meaning of the directive. In addition, the requirements of Article 3(b) and (c) are no doubt fulfilled in the present proceedings with regard to residence for tax purposes and liability to taxes under the Finnish Law on income tax. Consequently the Tax Merger Directive must be applied to a situation such as that in the main proceedings.

25. This leads to the question of what legal consequences are laid down by the Tax Merger Directive in relation to the cross-border treatment of losses. In that connection the referring court states that the Tax Merger Directive contains no provisions on how the receiving company's Member State should handle losses which have been found for the transferring company in another Member State. The parties to the main proceedings took a similar view. This appears to have led to the conclusion that the Tax Merger Directive does not regulate the situation in the main proceedings and that it gives no indication as to whether the Finnish measures are admissible under Union law.

26. That view requires some correction. As I have already noted, a situation such as that in the main proceedings falls within the scope of the Tax Merger Directive. According to recitals 2 to 4 of the directive, its purpose is to lay down common rules in order, for the effective functioning of the internal market, to remove tax disadvantages for cross-border mergers as compared with mergers of companies of the same Member State. Recital 9 expressly includes in that aim the tax treatment of losses.

5 — Case C-200/98 *X and Y* [1999] ECR I-8261, paragraphs 21 and 22, which was concerned with Swedish law, which is similar in that connection.

6 — On this point, with regard to the possibility of a broad interpretation of a reference for a preliminary ruling, see Case 244/78 *Union Laitière Normande* [1979] ECR 2663, paragraph 5, and judgment of 26 April 2012 in Joined Cases C-578/10 to C-580/10 V*an Putten*, paragraph 23.

27. Accordingly Article 6 contains a provision also on the takeover by the receiving company of losses of the transferring company which have not been exhausted for tax purposes. Under that provision, the receiving company may transfer losses of a transferring company resident in another Member State to a permanent establishment in that Member State if such a transfer is possible between companies of that State.

28. Consequently Article 6 of the Tax Merger Directive provides for an accumulated loss of the transferring company to be taken into account only in its own Member State and not in the Member State of the receiving company. According to that provision, the taxable company in the main proceedings would have the right, under the conditions of the Swedish tax rules, to use, in the framework of the Swedish tax procedure, the accumulated loss of its Swedish subsidiary, after a merger, through a permanent establishment situated in Sweden. However, that right, existing in Sweden, is obviously of no use to the taxable company because, according to the referring court, it will not have a permanent establishment in Sweden after the merger. It neither already maintains a permanent establishment in Sweden nor will it be able to take over an establishment of the transferring company, because the latter has ceased trading in Sweden.

29. Ultimately, however, it must be found that the Tax Merger Directive regulates the situation in the main proceedings. It just does not provide for the legal consequence sought by the taxable company, namely using the Swedish accumulated loss for the purposes of Finnish taxation. According to the Tax Merger Directive, that loss can be used only in the framework of Swedish taxation. Consequently the receiving company's Member State has precisely no obligation under the directive to take account of the transferring company's accumulated loss from another Member State.

2. Infringement of the freedom of establishment

30. However, that conclusion does not answer the question whether Union law as a whole precludes a national provision which does not allow foreign accumulated losses to be transferred. An exclusion of that kind could be incompatible with the receiving company's freedom of establishment under Articles 49 and 54 TFEU.

31. If that were the case, the Union legislature would not, by adopting the Tax Merger Directive, have done everything necessary under the Treaty to ensure the effective functioning of the internal market by the removal of tax disadvantages for cross-border mergers. Recital 14 of the Tax Merger Directive, which calls upon the Member States to take unilateral measures, if necessary, to eliminate obstacles to the functioning of the internal market, shows that the Union legislature realised that that was at least a possibility.

32. Therefore it is necessary to determine whether the refusal in Finnish tax law to allow foreign accumulated losses to be transferred in the event of a merger is incompatible with the freedom of establishment.

a) Restriction of the freedom of establishment

33. Under Articles 49 and 54 TFEU restrictions of the freedom of establishment of companies formed in accordance with the law of a Member State are in principle prohibited in the territory of another Member State.

34. It is settled case-law that all measures which prohibit, impede or render less attractive the exercise of the freedom of establishment must be regarded as restrictions.[7] Even though, according to their wording, the provisions of the Treaty concerning freedom of establishment aim to ensure that foreign nationals and companies are treated in the host Member State in the same way as nationals of that State, they also prohibit the Member State of origin from hindering the establishment in another Member State of one of its nationals or of a company incorporated under its legislation.[8] The Court considers that there is a hindrance of that kind where the Member State of origin treats that company differently from companies operating only in that State and the difference in treatment is likely to discourage the company from exercising its freedom of establishment in another Member State.[9]

35. According to the findings of the referring court, Paragraphs 119 and 123 of the Finnish Law on income tax rule out a transfer of losses originating from an activity which is not subject to Finnish tax. Whereas a parent company may use for tax purposes the accumulated loss of a Finnish subsidiary in the event of a merger in Finland, that is not possible in the case of an accumulated loss of a foreign subsidiary from its activity in another Member State. As losses arising from an activity in another Member State cannot be utilised for tax purposes in Finland, a Finnish company could be deterred from even forming or acquiring a subsidiary company in another Member State. Consequently the Finnish tax rules may discourage Finnish companies from seeking a business opportunity by means of a subsidiary company in other Member States. Consequently the freedom of establishment is restricted by the Finnish tax legislation.

36. That finding is one thing, but the question whether the taxable company could rely on the freedom of establishment in a case such as that in the main proceedings is another. In particular, the United Kingdom Government submits that in the present case, because the Swedish subsidiary has ceased trading, it is not a matter of exercising the freedom of establishment but rather the opposite. Although a reply to that question is relevant only if, in the final outcome, the Finnish tax provisions constitute an infringement of the freedom of establishment, I think it is clear from the very beginning that restrictions arising from the theoretical tax consequences of a merger, which already hinder a cross-border business operation, can in fact be prevented only at the time of the merger. At that time the freedom of establishment was already being exercised by the taxable company in spite of the existing restriction. In order for the freedom of establishment to produce its full effect once it has been exercised, the taxable company can also challenge the actual application of the restriction. Therefore the taxable company can plead the exercise of the freedom of establishment even in the present case.

37. However, the United Kingdom Government has correctly pointed out that a restriction of the freedom of establishment cannot be presumed in cases where Finnish law does not distinguish, when losses are transferred, between national and foreign accumulated losses. According to the referring court, that is the case where the transfer of an accumulated loss is the only reason for the merger. In such a case Finnish law prohibits the transfer for any company whatever. To that extent a restriction of the freedom of establishment would be excluded as there would be no different treatment, nor would the national provision infringe Articles 49 and 54 TFEU.

38. The decision as to whether that is the situation in the main proceedings, which would mean that the interpretation of Articles 49 and 54 TFEU is irrelevant, is a matter for the national court. However, against that background, for the purpose of replying to the questions I shall assume that the question from the referring court on the interpretation of the freedom of establishment is limited to cases where the transfer of the accumulated loss is not the only reason for the merger.

7 — Case C-439/99 *Commission* v *Italy* [2002] ECR I-305, paragraph 22, and Case C-371/10 *National Grid Indus* [2011] ECR I-12273, paragraph 36.

8 — Case 81/87 *Daily Mail and General Trust* [1988] ECR 5483, paragraph 16, and *National Grid Indus*, cited in footnote 7, paragraph 35.

9 — Case C-9/02 *Lasteyrie du Saillant* [2004] ECR I-2409, paragraph 46, and *National Grid Indus*, cited in footnote 7, paragraph 37.

39. In the present case, therefore, no further discussion is necessary of the significance of any abusive practice on the part of the taxable company, as submitted by several parties to the proceedings. The mere fact that a commercially justified decision on a merger results in the transfer of an accumulated loss of the transferring company cannot give rise to a charge of abuse if that is precisely what is provided for by Finnish law for mergers in relation to accumulated losses within that State.

40. After finding that there is a difference in treatment, the Court sometimes goes on to consider, in the context of a restriction of the freedom of establishment, whether the situations are objectively comparable.[10] However, it is becoming increasingly unclear to me what significance the Court attaches to that condition in cases, such as the present, where a restriction of the freedom of establishment by the Member State of origin and, consequently, the comparability of the situation of residents, falls to be considered. If the Court finds it sufficient here that in both cases resident taxable companies seek to benefit from a tax scheme,[11] an examination of that condition is a mere formality because it will be fulfilled in each case, as here. The same applies if the Court finds, without stating reasons, that the situations are objectively comparable.[12]

41. Against that background, it seems to me sensible to follow the example of several of the Court's judgments and to refrain from considering the objective comparability of situations when establishing whether there is a restriction of the freedom of establishment by the Member State of origin.[13] This is also supported by the fact that examination of the objective comparability of situations cannot, in my view, be exhaustive without considering the reason for the different treatment. However, that is precisely a question of the justification for a restriction, which I shall deal with in the following section.

42. It remains to note, as an interim conclusion, that a national measure which in principle allows the use of the transferring company's accumulated losses on a merger with the receiving company, but does not allow it if the losses are from business activity in another Member State which are not subject to national tax, constitutes a restriction of the freedom of establishment.

b) Justification

43. It is clear from settled case-law that a restriction on freedom of establishment is warranted only if it is justified by overriding reasons in the public interest.[14] It has also consistently been held that justification may consist in preserving the allocation of powers of taxation between the Member States.[15] Accordingly, the Member States may take measures to preserve the allocation of powers of taxation between the Member States.[16] For that purpose it may be necessary to apply to the economic activities of companies established in one of those States only the tax rules of that State in respect of both profits and losses.[17]

10 — Case C-337/08 *X Holding* [2010] ECR I-1215, paragraphs 20 to 24, and *National Grid Indus*, cited in footnote 7, paragraph 38.

11 — *X Holding*, cited in footnote 10, paragraph 24.

12 — *National Grid Indus*, cited in footnote 7, paragraph 38.

13 — Case C-414/06 *Lidl Belgium* [2008] ECR I-3601, paragraphs 18 to 25, and Case C-157/07 *Krankenheim Ruhestiz am Wannsee-Seniorenheimstatt* [2008] ECR I-8061, paragraphs 27 to 39.

14 — Case C-231/05 *Oy AA* [2007] ECR I-6373, paragraph 44, and Case C-9/11 *Waypoint Aviation* [2011] ECR I-9697, paragraph 27.

15 — *Marks & Spencer*, cited in footnote 2, paragraph 45, and *National Grid Indus*, cited in footnote 7, paragraph 45.

16 — Case C-196/04 *Cadbury Schweppes and Cadbury Schweppes Overseas* [2006] ECR I-7995, paragraph 56, and *National Grid Indus*, cited in footnote 7, paragraph 46.

17 — *X Holding*, cited in footnote 10, paragraph 28.

44. As I have already explained in my Opinion in *Philips Electronics UK*, a Member State's power of taxation is impaired if losses incurred within the scope of the exclusive power of taxation of another Member State are taken into account.[18] The losses in question in the present case were incurred on the basis of the business activity of a Swedish company in Sweden. That activity, according to Article 7(1) of the Double Taxation Agreement applicable here, falls within the scope of the exclusive power of taxation of the Kingdom of Sweden. Consequently, Finland's power of taxation would be impaired as a result of these losses being taken into account. Finland would take account of losses from an activity which it cannot tax. Therefore Finland is in principle entitled to refuse, as against the taxable company, to take into account the losses of its Swedish subsidiary to that extent.

45. However, the question that has given rise to the present reference for a preliminary ruling is whether that applies also to a merger in which the transferring company ceases to exist legally and therefore cannot use its accumulated loss in the framework of Swedish taxation.

i) Need for the Finnish legislation

46. In that respect the Finnish legislation might go further than is necessary in order to preserve the allocation of powers of taxation between the Member States. It has consistently been held that a restrictive measure must not go beyond what is necessary for that purpose.[19]

– Applicability of the *Marks & Spencer* exception

47. In *Marks & Spencer* the Court, with regard to necessity and less restrictive measures, found an infringement of the freedom of establishment, exceptionally, in a case where the non-resident subsidiary had taken full advantage of the possibilities available in its Member State of residence of having the losses taken into account and there was no possibility for its losses to be taken into account there in the future.[20] Consequently the resident parent company had to be allowed to deduct losses incurred in another Member State by a non-resident subsidiary 'where … the non-resident subsidiary has exhausted the possibilities available in its State of residence of having the losses taken into account for the accounting period concerned by the claim for relief and also for previous accounting periods, if necessary by transferring those losses to a third party or by offsetting the losses against the profits made by the subsidiary in previous periods, and … 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'.[21]

48. I think that exception can be understood only against the background of the justifications considered in *Marks & Spencer*. The Court based the justification in that case not only on the objective of preserving the allocation of taxation powers among Member States but also, inter alia, on the right of the Member States to prevent losses from being used twice.[22] There will be no fear of losses being used twice where the losses of a foreign subsidiary can no longer be used in its State of residence. Consequently a national provision which refuses to allow the parent company to use the loss even in such a case goes further than is necessary in order to prevent losses from being used twice.

18 — Opinion of 19 April 2012 in Case C-18/11 *Philips Electronics UK*, pending before the Court, paragraph 50 et seq.

19 — Case C-436/00 *X and Y* [2002] ECR I-10829, paragraph 49; *Marks & Spencer*, cited in footnote 2, paragraph 53; and *Waypoint Aviation*, cited in footnote 14, paragraph 27.

20 — *Marks & Spencer*, cited in footnote 2, paragraph 54 et seq.

21 — *Marks & Spencer*, cited in footnote 2, paragraph 55.

22 — *Marks & Spencer*, cited in footnote 2, paragraph 47 *et seq*.

49. However, the Court's case-law has continued to develop since *Marks & Spencer*. As I showed in my Opinion in *Philips Electronics*, according to the later development of the case-law, the crucial factor for the justification is that the national legislation pursues the objective of preserving the allocation of the power to tax.[23] The objective of preventing the double use of losses is not an autonomous justification.[24]

50. The exception developed by the Court in *Marks & Spencer* is no longer appropriate for justifying the preservation of the allocation of the power to tax, that justification having in the meantime been recognised as independent.[25] With regard to preserving the allocation of taxation powers among the Member States it is immaterial whether there is a possibility of using losses in the Member State which has the power to tax a particular business activity. It is only relevant to which activity and, therefore, to which taxing power a loss belongs.

51. If the justification of preservation of the allocation of taxation powers among the Member States is taken as a criterion, this gives an entirely different perspective for assessing the need for a national measure. With regard to that justification, it is not a less restrictive measure if the Member State which does not have the right to tax has to take account of losses incurred under the taxing power of another Member State in a case where that possibility no longer exists there. In fact, in such a case, the objective of preserving the allocation of taxation powers is not achieved at all.

52. The further development of the significance of the justifications which were referred to in *Marks & Spencer* in parallel at first has therefore also altered the scope of the exception formulated in that judgment. That exception may now be referred to for examining the need for a national measure only if the prevention of the double use of losses is recognised as an independent justification. If, on the other hand, the justification is based on the allocation of taxation powers among the Member States alone, the development of the case-law means that the *Marks and Spencer* exception can no longer be applied.

53. That is the approach taken by the Court in its most recent judgment on the cross-border transfer of losses. Whereas in the *X Holding* judgment the Court based the justification solely on the objective of preserving the allocation of taxation powers, it was consistent in making no mention of the *Marks & Spencer* exception, although it considered at length the need for a national measure.[26]

54. Consequently the restriction of the freedom of establishment by refusing the transfer of foreign accumulated losses is necessary in view of the objective of preserving the allocation of taxation powers, and the question of whether it is still possible for the Swedish subsidiary to have its accumulated losses taken into account in its State of residence is irrelevant.

– Application of the *Marks and Spencer* exception

55. Even if this question were still considered significant, it must be concluded that, in the case of a merger such as that in the present case, the conditions laid down in *Marks & Spencer* for the losses of a non-resident subsidiary to be taken into account, as an exception, in the parent company's Member State are not fulfilled.

23 — Opinion in *Philips Electronics UK*, cited in footnote 18, paragraphs 40 to 42.

24 — Opinion in *Philips Electronics UK*, cited in footnote 18, paragraph 58 et seq.

25 — See *X Holding*, cited in footnote 10, paragraphs 28 to 33; *National Grid Indus*, cited in footnote 7, paragraphs 45 to 49; and, to that effect, Case C-470/04 *N* [2006] ECR I-7409, paragraph 42.

26 — *X Holding*, cited in footnote 10, paragraph 27 et seq.

56. In *Marks & Spencer* the Court clearly wished to assume an exception only *ultima ratio*. That is shown by the fact that the Court saw the possibility of further, less restrictive measures which, however, it left expressly to the Union legislature to regulate.[27] The exception is formulated very restrictively for that reason. According to the judgment, there must be no possibility for the foreign subsidiary's losses to be taken into account in its State of residence for past or future periods either by the subsidiary itself or by a third party.[28]

57. In the present case of a merger, it must be said that, by ceasing to exist as a legal person, the subsidiary would lose any possibility of the losses being taken into account in the Swedish taxation procedure. However, that would merely be the consequence of the merger decision. The merger itself arose from a free decision of the parent company. If the fact that there was no possibility of the losses being taken into account were regarded only as a consequence of the merger decision, any procedural act of the subsidiary company in the Swedish taxation procedure, such as a deliberately belated application for an accumulated loss to be taken into account or a waiver of a claim, could justify the exclusion of the possibility of using the losses within the meaning of the *Marks & Spencer* judgment.

58. Therefore, by deciding on a merger with its subsidiary, the taxable company would itself forgo the possibility of using the loss in Sweden. The Court has pointed out on numerous occasions that a taxable company cannot be allowed to choose freely the tax scheme applicable to the losses of its subsidiaries and the place where those losses are taken into account.[29] As the Finnish Government correctly observes, in the present case there would be such a free choice if the Swedish subsidiary's losses had to be taken into account for the purposes of Finnish taxation after a merger.

59. Furthermore, in my view the taxable company cannot successfully claim that the accumulated Swedish loss cannot be used even before the merger on the ground that the Swedish subsidiary has ceased trading. On the contrary, the taxable company still has the option of using the Swedish losses in the future by resuming trading and through the resulting profits. If, on the other hand, solely the cessation of trading by the taxable company were regarded as decisive, that would once again mean the possibility of a choice which, as we have seen, according to the Court's case-law, the taxable company does not have. For, as a rule, it is not possible to determine objectively whether the cessation of a business activity is necessary financially because its continuation cannot be profitable.

60. Finally, in the procedure before the Court the taxable company itself stated that, under certain conditions, the losses of its Swedish subsidiary could be transferred to another of its Swedish subsidiaries. If necessary, the referring court would have to ascertain whether that is in fact a possible way of using the losses in Sweden. In any case the possibility cannot be ruled out just because the conditions for transferring a loss under Swedish law are less favourable than under Finnish law. In connection with using the losses of a foreign establishment, the Court has held that a Member State cannot be required to take account, for the purposes of applying its tax law, of the possible negative results arising from particularities of legislation of another Member State.[30]

27 — *Marks & Spencer*, cited in footnote 2, paragraph 58.

28 — *Marks & Spencer*, cited in footnote 2, paragraph 55.

29 — *X Holding*, cited in footnote 10, paragraphs 29 to 32; see also, to that effect, *Oy AA*, cited in footnote 14, paragraph 64 et seq.

30 — *Krankenheim Ruhestiz am Wannsee-Seniorenheimstatt*, cited in footnote 13, paragraph 49.

ii) Proportionality of the Finnish provision

61. Having found that the Finnish provision is necessary for attaining the objective of preserving the allocation of taxation powers among the Member States, it is necessary to consider the different question of whether the disadvantages arising in the context of the freedom of establishment are proportionate to the desired purpose (proportionate within the narrower meaning of that term). [31]

62. That could be questionable because, as we have already seen, an accumulated foreign loss can never be used, as a result of a merger, by the receiving company in the context of the Finnish tax procedure. There are no situations where, exceptionally, in the context of a merger, such a transfer of accumulated losses would be possible from another tax jurisdiction.

63. However, it seems to me that the restriction of the freedom of establishment in the present case is not particularly serious. Ultimately, in certain cases, in economic terms a taxpayer has to bear a tax loss. That is nothing exceptional in the tax systems of the Member States and it may occur merely as a result of the expiry of time-limits for carrying forward a loss. Also, in the case of the Finnish provision, only a few companies are affected, namely those for which using a loss is not the only reason for the merger, but which, after the merger, do not have a permanent establishment in the other Member State and therefore using a loss under Article 6 of the Tax Merger Directive is ruled out.

64. It could be argued, in response to this, that the adverse effect on the allocation of taxation powers among the Member States is thus not great. However, it must be borne in mind that by means of the Tax Merger Directive the Union legislature has made certain fundamental decisions, which I think must be respected, with regard to the allocation of taxation powers.

65. In recital 4 of the directive the Union legislature has made it clear that, in order to prevent distortions of competition, it prefers a common tax system in the Union to an extension of the national tax systems in force in the Member States. Extending the Finnish tax system would mean the transfer of accumulated foreign losses in the event of a merger. Ultimately all the subsidiaries, established in the Union, of Finnish parent companies would have the benefit of the Finnish provisions on the use of losses on the occasion of a merger. Outside Finland, however, that would lead to distortions of competition because not all Member States have the same rules for the transfer of losses as Finnish tax law. [32] Consequently subsidiaries resident in Sweden, for example, would, with regard to the transfer of an accumulated loss in the event of a merger, be treated differently, depending on the tax system of the Member State in which the parent company is resident.

66. For that reason, Article 6 of the Tax Merger Directive provides, uniformly throughout the Union, for the accumulated loss to be used in the Member State in which the transferring company was resident. Consequently the Union legislature intentionally decided in favour of losses being used in principle in the Member State of the transferring company in the case of a merger. However, if the conditions for that basic possibility are not fulfilled in any particular case, the requirement for losses to be used in the Member State of the receiving company instead would be contrary to the Union legislature's fundamental decision and would also call into question the validity of the conditions laid down in Article 6 of the Tax Merger Directive. [33]

31 — See the Opinion of Advocate General Trstenjak in Case C-10/10 *Commission* v *Austria*, [2011] ECR I-5389, point 67 et seq. and my Opinion in Case C-231/05 *Oy AA* [2006] ECR I-6373, paragraphs 32 and 66; also Cases C-379/08 and C-380/08 *ERG and Others* [2010] ECR I-2007, paragraph 86.

32 — See the Commission Proposal for a Council directive concerning arrangements for the taking into account by enterprises of the losses of their permanent establishments and subsidiaries situated in other Member States, 24 January 1991, COM(90) 595 final, Explanatory Memorandum, Article 12.

33 — For the conclusive binding nature of constituent elements, see Case C-285/07 *A.T.* [2008] ECR I-9329, paragraph 27, regarding Article 8 of the Merger Directive.

67. Finally, I think it would assist legal certainty to stress the importance of a clear demarcation between the taxation powers of the Member States. Detailed differentiations such as those in the *Marks & Spencer* judgment, for example, are not in the interest of the freedom of establishment if they lead to uncertainty and dispute in the application of the law. In the course of the hearing the taxable company gave a striking account of how complex the tax and company law questions are to which such an exception can give rise. However, the uniform application of Union law would be called into question if the clarification of those questions were left to the national courts alone, as the Commission proposes.

68. Therefore I consider that the disadvantages caused by the Finnish law in the context of the freedom of establishment are reasonably proportionate to the intended preservation of the allocation of taxation powers among the Member States.

3. Interim conclusion

69. Consequently the reply to be given to the first question is that neither the Tax Merger Directive nor Articles 49 and 54 TFEU preclude a national measure which provides that a receiving company resident in a Member State may not deduct for tax purposes the losses arising from the business activity in another Member State of a company which was resident in that other Member State and which has merged with it where that activity was subject exclusively to that other Member State's right of taxation.

B – *The second question: calculation of loss*

70. The second question from the referring court is whether the accumulated foreign loss to be taken into account is to be calculated in accordance with the tax law of the State of residence of the receiving company or that of the transferring company.

71. In view of my reply to the first question, it is unnecessary to reply to the second question because the receiving company's Member State is not required by Union law to take account of the accumulated foreign loss.

72. However, should the Court not accept my proposed reply to the first question and decide that the receiving company can deduct the transferring company's losses, the second question will also have to be answered

73. In my view, the reply to the second question should then be that the losses to be taken into account must *in principle* be calculated according to the tax law of the receiving company's State of residence. As the French Government also submitted, only in that way would calculation of the losses lead to equal treatment in cases within a single Member State and in cross-border situations, that is to say, a merger with a resident subsidiary and a merger with a foreign subsidiary would receive equal treatment for tax purposes. Equal treatment in that way would remove the restriction of the freedom of establishment which, as we have seen, arises precisely from the different treatment of the two situations. [34]

34 — See paragraph 33 et seq. above.

74. Against that background it is impossible to accept the submissions of the Commission and the Finnish Government, which assert that the maximum loss to be taken into account should be the amount calculated according to the tax law of the transferring company's State of residence, that is to say, in the present case Sweden. If that were the case, equal treatment of the tax-law consequences of an inland and a cross-border merger would precisely not be guaranteed. A restriction of the freedom of establishment would continue to exist because the loss taken into account in cross-border mergers would be less than in purely domestic mergers.

75. However, the principle of calculating the losses to be taken into account according to the tax law of the receiving company's State of residence may need to be limited, depending on the cause of a loss calculation differing from the operating result. Exceptions could apply, for example, for fiscal promotion measures of the receiving company's State of residence, such as higher depreciation, which result in a bigger loss. It could be justifiable to limit the application of such measures just to domestic activities. The consequence of this would be that to that extent losses would not have to be calculated according to the tax law of the receiving company's State of residence.

76. However, as the reference for a preliminary ruling provides no information on any differences between Finnish law and Swedish law with regard to the calculation of losses or which provisions concerning the calculation of losses are of doubtful application, a conclusive reply cannot be given to the referring court in this respect.

V – Conclusion

77. In the light of the foregoing I propose that the Court give the following answer to the questions raised by the Korkein hallinto-oikeus:

Neither the Tax Merger Directive nor Articles 49 and 54 TFEU preclude a national measure which provides that a receiving company resident in a Member State may not deduct for tax purposes the losses arising from the business activity in another Member State of a company which was resident in that other Member State and which has merged with it where that activity was subject exclusively to that other Member State's right of taxation.