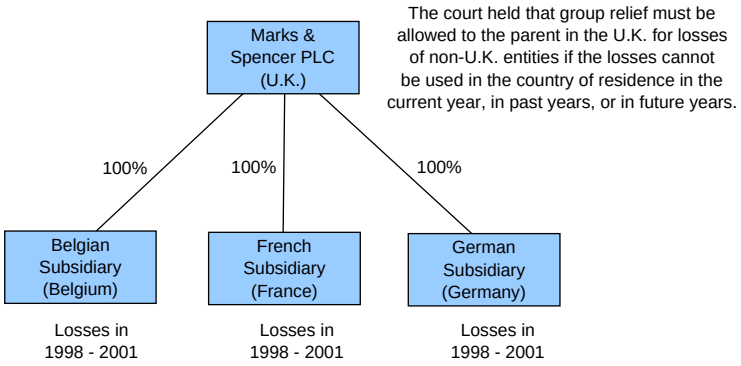
Marks & Spencer PLC v. Halsey (HM Inspector of Taxes)
[2005] C-446/03 ECR I-10837

U.K. Group Relief for Non-U.K. Losses

Marks & Spencer is a company incorporated and registered in England and Wales. It is the parent company of a number of companies established in the United Kingdom and in other States. It is one of the leading United Kingdom retailers of clothing, food, homeware and financial services.

From 1975 Marks & Spencer began to move into other States, with the opening of a store in France. By the end of the 1990s it had sales outlets in more than 36 countries, with a network of subsidiaries and a system of franchises. A trend towards increasing losses became evident in the mid-1990s. In March 2001 Marks & Spencer announced its intention to divest itself of its Continental European activity. By 31 December 2001 the French subsidiary had been sold to third parties, while the other subsidiaries, including those established in Belgium and Germany, had ceased trading.



In the United Kingdom, Marks & Spencer claimed group tax relief in respect of losses incurred by its subsidiaries in Belgium, Germany and France for the four accounting periods ended 31 March 1998, 31 March 1999, 31 March 2000 and 31 March 2001. The claims for relief were rejected on the ground that group relief could only be granted for losses recorded in the United Kingdom. The issue in the case was whether Articles 43 EC and 48 EC preclude provisions of a Member State which prevent a resident parent company from deducting losses incurred in another Member State by a subsidiary established in that Member State although they allow deductions for losses incurred by a resident subsidiary. In other words, the question was whether such provisions constitute a restriction on freedom of establishment, contrary to Articles 43 EC and 48 EC.

Although direct taxation falls within their competence, Member States must none the less exercise that competence consistently with Community law. Freedom of establishment entails the right to exercise their activity in the Member State concerned through a subsidiary, a branch or an agency. Even though the provisions concerning freedom of establishment are directed to ensuring 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.

Group relief such as that at issue constitutes a tax advantage for the companies concerned. By speeding up the relief of the losses of the loss-making companies by allowing them to be set off immediately against the profits of other group companies, such relief confers a cash advantage on the group. The exclusion of such an advantage in respect of the losses incurred by a subsidiary established in another Member State which does not conduct any trading activities in the parent company's Member State is of such a kind as to hinder the exercise by that parent company of its freedom of establishment by deterring it from setting up subsidiaries in other Member States. It thus constitutes a restriction on freedom of establishment within the meaning of Articles 43 EC and 48 EC, in that it applies different treatment for tax purposes to losses incurred by a resident subsidiary and losses incurred by a non-resident subsidiary.

Such a restriction is permissible only if it pursues a legitimate objective compatible with the Treaty and is justified by imperative reasons in the public interest. It is further necessary, that its application be appropriate to ensuring the attainment of the objective thus pursued and not go beyond what is necessary to attain it. Reduction in tax revenue cannot be regarded as an overriding reason in the public interest which may be relied on to justify a measure which is in principle contrary to a fundamental freedom.

Articles 43 EC and 48 EC do not preclude provisions of a Member State which generally prevent a resident parent company from deducting losses incurred in another Member State by a subsidiary established in that Member State although they allow it to deduct losses incurred by a resident subsidiary. However, it is contrary to Articles 43 EC and 48 EC to prevent the resident parent company from doing so where the non-resident subsidiary has exhausted the possibilities available in its State of residence of having the losses taken into account for the current accounting period and for previous accounting periods and where there are no possibilities for those 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.