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Newsalert

EU Direct Tax Group

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EU Direct Tax Group

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The European Commission has announced that it has decided to refer the UK to the European Court of Justice for improper implementation of the ECJ decision in the Marks & Spencer case concerning cross-border loss relief.

Following the ECJ's decision on 13 December 2005 in M&S (C-446/03), the UK introduced rules in ICTA 1988 Schedule 18A, effective from 1 April 2006, allowing for group relief for certain EEA losses. However the Commission considers that the conditions for the relief mean that, in practice, it is almost impossible for taxpayers to benefit from the relief - in particular due to:

1. an unnecessarily restrictive interpretation in Schedule 18A para 7 of the 'no possibilities' of future use test;
2. the fact that the taxpayer must demonstrate that the 'no possibilities' test is met immediately after the end of the accounting period in which the loss arises; and
3. the legislation only applying to losses incurred on or after 1 April 2006.

This is, according to the European Commission, an unjustifiable breach of the freedom of establishment, guaranteed by Article 43 and Article 48 of the EC Treaty and Article 31 and Article 34 of the EEA agreement.

In addition to the factors mentioned by the Commission in its press release, it is apparent from the recent Philips Electronics UK First Tax Tribunal decision [2009] UKFTT 226 in favour of the taxpayer, and the 2nd Marks and Spencer plc Tribunal decision on the quantification of losses for group relief in the Marks and Spencer appeal [2009] UKFTT 231 (TC) that other elements of the UK legislation constitute or are likely to constitute a breach of the freedom of establishment:

1. Relief is only available in situations that mirror the M&S facts. It is arguable that this should be extended to other situations, including sideways claims between subsidiaries and consortium claims, and possibly the surrender from an EEA parent company to a UK subsidiary;

2. There must be a tax loss in the territory of residence of the surrendering company. The M&S 2nd tribunal decision indicates that group relief should be given for the amount of the loss calculated on UK principles in the year in which the losses fall for UK computational purposes, even if there is no foreign tax loss for that year.

We would therefore recommend that groups with UK tax capacity revisit their ability to make cross-border loss relief claims for periods from 1 April 2006 onwards.

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For more detailed information, please do not hesitate to contact your local PwC contact person or a member of the EUDTG.

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