

# Tax and Employee Benefits Law Update

May 2005

## EU CROSS-BORDER LOSS RELIEF

### An opportunity to reclaim tax

Tax relief for trading losses is a fundamental part of most corporate tax systems, but the rules allowing such relief are often narrowly drawn. The UK food and clothing retailer Marks & Spencer looks likely to score a significant victory that should increase the ability of businesses with operations in more than one EU member state to offset losses suffered in one member state against profits made in another, thus reducing their overall effective EU tax rate.

### Does this apply to your business?

If your business has operations in more than one EU member state, and it has incurred losses in at least one of those states, there is a possibility that you will be able to reclaim tax. The examples below are designed to show that the potential claims against tax authorities are precisely the same, irrespective of whether a business is ultimately owned by an EU parent or by a non-EU parent.

### The current position

In many EU member states, including the UK, France, the Netherlands and Germany, the loss

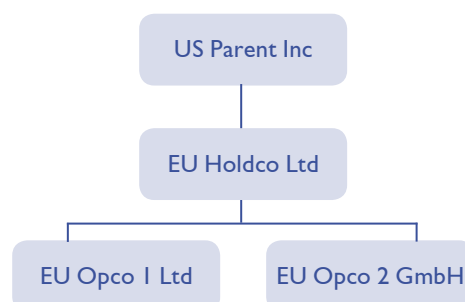
relief rules permit losses in one group company to be relieved against profits in another group company provided that both companies are tax resident in (or have operations in) the same member state. Generally, such rules would not permit losses of a group company resident in one member state to be relieved against profits of another group company in another member state. Marks & Spencer was profitable in the UK, but had loss-making subsidiaries in France, Belgium and Germany. It claimed that the UK loss relief rules were incompatible with EU law, in that they restricted Marks & Spencer's freedom of establishment within the EU – one of the so-called fundamental freedoms available to all EU residents.

### Have you made protective claims?

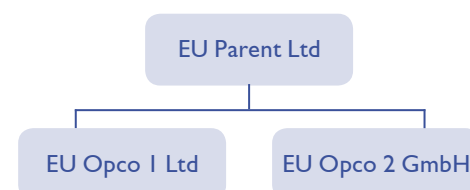
In his recently delivered opinion, Advocate General Maduro broadly agreed with Marks & Spencer's arguments, although he did indicate that the same losses should not be able to be used twice. Even so, it looks increasingly likely that Marks & Spencer will be successful before the European Court of Justice (ECJ) when its judgment is delivered later this year. Marks & Spencer's success would have a significant effect on how the loss relief rules of various EU member states would work

Baltimore  
Beijing  
Berlin  
Boston  
Brussels  
London  
Munich  
New York  
Northern Virginia  
Oxford  
Waltham  
Washington

Example 1



Example 2



NB - EU Opco 2 GmbH has trading losses; all other companies are profitable.

going forward, but it would also mean that the rules in those countries that do not presently permit cross-border loss relief are illegal. In the above examples, this would mean that any losses incurred in EU Opco 2 GmbH could be relieved against profits made in EU Holdco Ltd (Example 1) or EU Parent Ltd (Example 2). It may also be the case that the losses in EU Opco 2 GmbH could be relieved against profits in EU Opco 1 Ltd, a sister company rather than a parent or subsidiary. This (and a number of related questions) should be determined by the precise scope of the ECJ's judgment

It is important to carefully consider whether your business could make claims for repayment of taxes for previous tax years where, if cross-border loss relief had been allowed, losses of a group company in one EU member state could have been set against the profits of a group company in another EU member state. Since a time bar is highly likely to apply to claims for repayment of tax paid in previous tax years (the period of limitation will differ in different member states), you should consider whether protective claims could be made against the relevant tax authorities as soon as possible.

Finally, it is understood that the potential claims for repayment of tax in the UK could be as much as £20 billion, and could be as much as €50 billion in Germany. There is a lot of tax to be reclaimed – make sure that your business does not miss out!

## Further information

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