



International Tax

## European Union Tax Alert

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### AG releases opinion on Finland's loss forfeiture rules

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Advocate General (AG) Sharpston of the Court of Justice of the European Union (CJEU) issued her opinion on 7 February 2013 in a case involving Finland's loss forfeiture rules (Case C 6/12 P Oy). At issue was whether the granting of an exception to the loss forfeiture rules where there has been a change in control of a company constitutes state aid under EU rules. The Finnish Supreme Administrative Court requested a preliminary ruling from the CJEU on this issue at the end of 2011.

The purpose of the state aid rules (as found in the Treaty on the Functioning of the European Union, or TFEU) is to ensure that "government interventions do not distort competition and intra-EU trade." The TFEU contains a general prohibition on state aid measures, unless they are specifically approved and authorized by the European Commission ("standstill obligation").

#### Background

The case involves a Finnish company (Company P) whose shares were transferred (directly and indirectly) in 2004, and these transactions resulted in the expiration of Company P's losses. Company P applied to the tax authorities for the right to use the tax losses it incurred between 1998 and 2004. The tax office took the position that the company did not have any basis for maintaining its losses. After the Helsinki Administrative Court confirmed this position, Company P appealed to the Supreme Administrative Court, which decided to refer the case to the CJEU.

Under Finnish tax law, while tax losses generally may be carried forward for 10 years for set off against future profits, losses incurred by a company will be forfeited if more than 50% of the shares of the company are transferred (directly or indirectly). Nevertheless, the tax authorities have discretion to grant an exception to this rule if certain requirements are met and will allow the loss company to utilize the tax losses despite the change in control. This practice was well-established until 2008 when some tax offices began rejecting applications of companies, but in 2010 the Supreme Administrative Court confirmed the practice under which many applicants were allowed to utilize their tax losses.

The Supreme Administrative Court has asked the CJEU to rule on whether the

“selectivity requirement” in article 107 in the TFEU (formerly article 87 of the EC Treaty) creates an obstacle to allowing the retention of losses without a notification to the European Commission, or whether the approval mechanism used by the Finnish tax authorities is a measure that can be justified to prevent tax avoidance and evasion. The court also asked the CJEU to rule on whether the scope of the discretionary powers of the tax authorities to allow a taxpayer to retain the losses has any relevance when considering whether the mechanism is justified.

## AG opinion

AG Sharpston does not analyze the question of whether the Finnish exception system that allows companies to continue to carryforward losses and offset them against future profits after a change in ownership are incompatible with the state aid rules or whether the rules selectively favor certain undertakings. Instead, AG Sharpston examines whether the Finnish rules are (presumed) “existing aid” or (presumed) “new aid.”

In general, aid measures that predate accession of the member state to the EU and that continue to be operated thereafter qualify as existing aid. The monitoring procedures for existing aid and new aid differ significantly. Existing aid does not have to be notified to the European Commission -- instead, the aid is simply subject to constant monitoring by the Commission. With respect to new aid, however, the member state should inform the Commission of any plans to grant or alter such aid. In addition, the member state is prohibited from putting the proposed measures into effect before the Commission’s review procedure has resulted in a final Commission decision.

Since the loss forfeiture legislation was in effect before Finland joined the (then) European Communities and became bound by the EC Treaty, AG Sharpston concluded that the Finnish exception system for the retention of losses should be classified as (presumed) existing aid. Consequently, the monitoring procedures for existing aid should be applied. In this regard, the Commission has exclusive competence, so unless and until the Commission takes action, there is no presumption that the Finnish system is unlawful under EU state aid rules.

## Comment

If the CJEU follows AG Sharpston’s opinion, Finland can continue to apply the discretionary system for the retention of losses provided the European Commission does not consider the rules to be incompatible with the internal market.

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